LightInTheBox Holding Co., Ltd.
Form 20-F
March 30, 2017
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UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

WASHINGTON, D.C. 20549

FORM 20-F

(Mark One)

o	**REGISTRATION STATEMENT PURSUANT TO SECTION 12(b) OR 12(g) OF THE SECURITIES EXCHANGE ACT OF 1934**
	OR
x	**ANNUAL REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934** **For the fiscal year ended December 31, 2016**
	OR
o	**TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934**
	OR
o	**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 001-35942

LightInTheBox Holding Co., Ltd.

(Exact name of Registrant as specified in its charter)

Cayman Islands
(Jurisdiction of incorporation or organization)

Tower 2, Area D, Diantong Square

No. 7 Jiuxianqiao North Road

Chaoyang District, Beijing 100015

People s Republic of China
(Address of principal executive offices)

Quji (Alan) Guo, Chief Executive Officer

Telephone: +(86-10) 5692-0099

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Tower 2, Area D , Diantong Square

No. 7 Jiuxianqiao North Road

Chaoyang District, Beijing 100015

People s Republic of China
(Name, Telephone, E-mail and/or Facsimile number and Address of Company Contact Person)

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

Title of each class	Name of each exchange on which registered
Ordinary Shares, par value $0.000067 per share American Depositary Shares, each representing two Ordinary Shares	New York Stock Exchange

Securities registered or to be registered pursuant to Section 12(g) of the Act: None

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Securities for which there is a reporting obligation pursuant to Section 15(d) of the Act: None

Indicate the number of outstanding shares of each of the issuer s classes of capital or common stock as of the close of the period covered by the annual report:

137,820,605 Ordinary Shares

Indicate by check mark if the registrant is a well-known seasoned issuer, as defined in Rule 405 of the Securities Act.

o Yes x 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.

o Yes x 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.

x Yes o 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).

x Yes o 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 o Accelerated filer x Non-accelerated filer o

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

U.S. GAAP x	International Financial Reporting Standards as issued by the International Accounting Standards Board o	Other o

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.

o Item 17 o 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 Securities Exchange Act of 1934).

o Yes x No

(APPLICABLE ONLY TO ISSUERS INVOLVED IN BANKRUPTCY PROCEEDINGS DURING THE PAST FIVE YEARS)

Indicate by check mark whether the registrant has filed all documents and reports required to be filed by Sections 12, 13 or 15(d) of the Securities Exchange Act of 1934 subsequent to the distribution of securities under a plan confirmed by a court.

o Yes o No

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CONVENTIONS THAT APPLY TO THIS ANNUAL REPORT ON FORM 20-F

Unless where the context otherwise requires, references in this annual report on Form 20-F to:

- ADRs are to the American depositary receipts, which, if issued, evidence the ADSs;
- ADSs are to the American depositary shares, each of which represents two ordinary shares;
- China and the PRC are to the People s Republic of China, excluding, for the purposes of this annual report only, Taiwan and the special administrative regions of Hong Kong and Macau;
- shares or ordinary shares are to our ordinary shares, par value $0.000067 per share;
- North America are to, for the purposes of this annual report only, the United States and Canada;
- Our number of customers are to the number of customer accounts that have purchased at least once from our company during the relevant period;
- repeat customers are to customers who have purchased products from us more than once since our inception;
- RMB and Renminbi are to the legal currency of China;
- we, us, our company and our are to LightInTheBox Holding Co., Ltd., its consolidated subsidiaries and its variable interest entities, or VIEs, including Lanting Huitong, Lanting Gaochuang and Shanghai Ouku, the subsidiary of Lanting Huitong; and

- $, dollars and U.S. dollars are to the legal currency of the United States.

Our reporting and functional currency is the U.S. dollar. In addition, this annual report also contains translations of certain foreign currency amounts into U.S. dollars for the convenience of the reader. Unless otherwise stated, all translations of Renminbi into U.S. dollars were made at RMB6.9430 to $1.00, the noon buying rate on December 30, 2016 as set forth in the H.10 statistical release of the U.S. Federal Reserve Board. 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. On March 24, 2017, the noon buying rate for Renminbi was RMB6.8803 to $1.00.

FORWARD-LOOKING STATEMENTS

This annual report on Form 20-F contains statements of a forward-looking nature. All statements other than statements of historical facts are forward-looking statements. These forward-looking statements are made under the safe harbor provision under Section 21E of the Securities Exchange Act of 1934, as amended, or the Exchange Act, and as defined in the Private Securities Litigation Reform Act of 1995. These statements involve known and unknown risks, uncertainties and other factors that may cause our actual results, performance or achievements to be materially different from those expressed or implied by the forward-looking statements. In some cases, these forward-looking statements can be identified by words or phrases such as may, will, expect, anticipate, aim, estimate, intend, plan, believe, potential, contin other similar expressions. These forward-looking statements relate to, among others:

- our growth strategies;
- our future business development, results of operations and financial condition;
- trends in online consumer retailing;

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- trends in Chinese manufacturing;
- expected changes in our revenues and certain cost and expense items; and
- assumptions underlying or related to any of the foregoing.

We have based these forward-looking statements largely on our current expectations and projections about future events and financial trends that we believe may affect our financial condition, results of operations, business strategy and financial needs.

You should read these statements in conjunction with the risks disclosed in Item 3.D. Risk Factors of this annual report and other risks outlined in our other filings with the Securities and Exchange Commission, or the SEC. Moreover, we operate in an emerging and evolving environment. New risks may emerge from time to time, and it is not possible for our management to predict all risks, nor can we assess the impact of such risks on our business or the extent to which any risk, or combination of risks, may cause actual results to differ materially from those contained in any forward-looking statements. 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. Except as required by law, we undertake no obligation to update any forward-looking statements to reflect events or circumstances after the date on which the statements are made or to reflect the occurrence of unanticipated events. You should read this annual report and the documents that we have referred to in this annual report, completely and with the understanding that our actual future results may be materially different from what we expect.

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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 Financial Data.

The selected consolidated statements of operations data for 2014, 2015 and 2016, and the selected consolidated balance sheet data as of December 31, 2015 and 2016 have been derived from our audited consolidated financial statements included elsewhere in this annual report on Form 20-F. Our selected consolidated statements of operations data for 2012 and 2013 and the selected consolidated balance sheet data as of December 31, 2012, 2013 and 2014 has been derived from our audited consolidated financial statements not included in this annual report on Form 20-F. Our audited consolidated financial statements are prepared and presented in accordance with generally accepted accounting principles in the United States, or U.S. GAAP. The following selected consolidated financial data for the periods and as of the dates indicated are qualified by reference to and should be read in conjunction with our consolidated financial statements and related notes and Item 5. Operating and Financial Review and Prospects, both of which are included elsewhere in this annual report.

Our historical results for any prior period do not necessarily indicate our results to be expected for any future period.

	Year Ended December 31, (U.S. dollars in thousands, except per share data)				
	2012	2013	2014	2015	2016
Selected Consolidated Statements of Operations Data					
Net revenues					
Product sales	$ 200,010	$ 292,417	$ 382,282	$ 312,332	$ 262,083
Services			125	11,431	30,404
Total net revenues	200,010	292,417	382,407	323,763	292,487

Cost of revenues					
Product sales	116,465	165,267	236,982	196,753	160,566
Services			113	10,601	28,371
Total cost of revenues	116,465	165,267	237,095	207,354	188,937
Gross profit	83,545	127,150	145,312	116,409	103,550
Operating expenses					
Fulfillment	10,088	15,963	23,926	22,419	17,052
Selling and marketing	53,418	84,245	105,186	91,614	61,090
General and administrative	22,369	31,929	46,916	41,535	34,492
Loss from operations	(2,330)	(4,987)	(30,716)	(39,159)	(9,084)
Net loss	(4,230)	(4,819)	(29,987)	(39,407)	(8,723)
Accretion for Series C convertible redeemable preferred shares	2,971	1,621			
Net loss attributable to ordinary shareholders	(7,201)	(6,440)	(29,987)	(39,407)	(8,723)
Net loss per ordinary share					
Basic	(0.20)	(0.09)	(0.30)	(0.41)	(0.07)
Diluted	(0.20)	(0.09)	(0.30)	(0.41)	(0.07)
Other Consolidated Financial Data					
Gross Margin(1)	41.8%	43.5%	38.0%	36.0%	35.4%

(1) Gross margin represents gross profit as a percentage of total net revenues.

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	Year Ended December 31,				
	2012	2013	2014	2015	2016
	(U.S. dollars in thousands)				
Summary Consolidated Balance Sheet Data					
Cash and cash equivalents	$ 19,972	$ 23,745	$ 75,358	$ 30,901	$ 89,517
Term deposit		79,958	5,802		
Inventories	5,753	7,081	9,845	11,261	10,587
Total current assets	37,753	121,293	99,156	49,741	113,738
Total assets	39,838	125,891	104,467	55,493	118,201
Total current liabilities	36,847	44,500	61,284	57,616	52,365
Total liabilities	36,847	44,500	61,284	57,616	52,365
Total shareholders equity (deficit)	(38,480)	81,391	43,183	(2,123)	65,836

B. Capitalization and Indebtedness

Not Applicable.

C. Reasons for the Offer and Use of Proceeds

Not Applicable.

D. Risk Factors

Risks Related to Our Business and Industry

Our limited operating history may make our growth and future prospects uncertain and difficult to evaluate.

Our limited operating history may not provide a meaningful basis to evaluate our business. It may be difficult for you to make accurate predictions of our future results of operations and our past results of operations should not be taken as indicative of our future growth. Additionally, we will continue to encounter risks and difficulties frequently experienced by companies at a similar stage of development, including our potential inability to:

- implement our business model and strategy and adapt and modify them as needed;

- increase awareness of our brands, protect our reputation and develop customer loyalty;
- acquire customers cost-effectively;
- manage our expanding operations and offerings, including the integration of any future acquisitions;

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- anticipate and adapt to changing conditions in online retail industry globally and in China;

- anticipate and adapt to changes in government regulations, industry consolidation, technological developments and other significant competitive and market dynamics;

- manage risks related to intellectual property rights;

- upgrade our technology or infrastructure to support increased user traffic and product offerings; and

- manage relationships with a growing number of suppliers and couriers.

The online retail industry is intensely competitive and we may not compete successfully against new and existing competitors, which may materially and adversely affect our results of operations.

The market for products sold on our websites and mobile applications is intensely competitive. Consumers have many choices online and offline, including global, regional and local retailers. For example, our current and potential competitors include global and regional online retailers such as other China-based global online retail companies, retail chains, specialty retailers, and sellers on online marketplaces. In the future, we may also face competition from new entrants, consolidations of existing competitors or companies spun off from our larger competitors.

We face a variety of competitive challenges, including sourcing products efficiently, pricing our products competitively, maintaining optimal inventory levels, selling our products effectively, maintaining the quality of our products, anticipating and responding quickly to changing consumer demands and preferences, building our customer base, conducting effective marketing activities and maintaining favorable recognition of our brands, websites and products. In addition, as we further develop our business, we will face increasing challenges to compete for and retain high quality suppliers. If we cannot properly address these challenges, our business and prospects could be materially and adversely affected.

Some of our current and potential competitors have significantly more established brands or greater financial, sourcing, marketing, operational or other resources than we do. In addition, other online retailers may be acquired by, receive investments from or enter into strategic relationships with well-established and well-financed companies or investors, which would help enhance their competitive positions. Certain of our competitors may be able to secure more favorable terms with suppliers, devote greater resources to marketing campaigns, adopt more aggressive pricing or inventory policies and devote substantially more resources to infrastructure development. Increased competition may reduce our gross and operating margins, market share and brand recognition. We may not be able to compete successfully against current and future competitors, and competitive pressures may materially and adversely affect our business, financial condition and results of operations.

Our failure to quickly identify and adapt to changing industry conditions may have a material and adverse effect on our business, financial condition and results of operations.

The online and offline retail industries are subject to changing consumer preferences and industry conditions. This is particularly true with respect to products such as apparel, small accessories and gadgets, electronics and communication devices and home and garden products. Consequently, we must stay abreast of emerging fashion, lifestyle, design, technological and other industry and consumer trends. This requires timely collection of market feedback, accurate assessments of market trends, deep understanding of industry dynamics and flexible manufacturing capabilities.

We must also maintain relationships with suppliers who can adapt to fast-changing consumer preferences. If one or more of our existing suppliers cannot meet these requirements effectively, we will need to source from new suppliers, which may be costly and time-consuming. We or our suppliers may overestimate customer demand, face increased overhead expenditures without a corresponding increase in product sales and incur inventory write-downs, which will adversely affect our results of operations.

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If we cannot offer appealing products on our websites or our mobile applications, our customers may purchase fewer products from us, stop purchasing products from us, visit our websites or our mobile applications less often or stop visiting our websites or our mobile applications all together. Our reputation may also be negatively impacted. If we do not anticipate, identify and respond effectively to consumer preferences or changes in consumer trends at an early stage, we may not be able to generate our desired level of product sales. Failure to properly address these challenges may materially and adversely affect our business, financial condition and results of operations.

Any failure to manage our growth or execute our strategies effectively may materially and adversely affect our business and prospects.

We anticipate spending significant resources on marketing, supply chain management, fulfillment infrastructure, technology and other business expenditures as our business continues to grow. We will need to continue to expand, train, manage and motivate our workforce and manage our relationships with customers, suppliers, wholesalers and third-party service providers. To accommodate our future growth, we plan to implement a variety of new and upgraded operational and financial systems, procedures and controls, including the improvement of our accounting and other internal management systems, although we have not yet entered into any commitments related to such plan. We have experienced a period of rapid growth and expansion that has placed, and will continue to place, a significant strain on our management and resources. If we are not successful in managing our growth or executing our strategies effectively, our business may be materially and adversely affected.

As part of our growth strategy, we intend to broaden the range of our product offerings, which will require us to introduce new products, work with different suppliers and address the needs of different kinds of consumers. We may incur significant costs in trying to expand our offerings into these new products, or fail to introduce new products that meet anticipated consumer demand. For example, we launched our own brand of fast fashion apparel for women, *Three Seasons* and our own brand of wedding dresses, *TS* and *Lan Ting*, as well as our own brand of faucets, *Sprinkle*, but it is currently uncertain whether these brands will be competitive in the marketplace, reach broad consumer acceptance and become profitable in the long run.

We have incurred net losses since our inception and experienced negative cash flow from operating activities in the past. We may continue to incur net losses and experience negative cash flow from operating activities and, as a result, we may need to obtain additional capital in the future.

We incurred net losses attributable to our ordinary shareholders of $30.0 million, $39.4 million and $8.7 million, in 2014, 2015 and 2016, respectively, and we may continue to incur losses in the future. In addition, although we generated positive cash flow from operating activities of $15.2 million in 2013, we experienced negative cash flow from operating activities of $6.9 million, $37.9 million and $15.3 million in 2014, 2015 and 2016, respectively, and we may continue to experience negative cash flows in the future.

We expect our costs and expenses, especially our selling and marketing expenses, to increase as we expand our operations. Our ability to achieve and maintain profitability and positive cash flow from operating activities depends on various factors, including but not limited to, the acceptance of our products by consumers, the growth and maintenance of our customer base, our ability to control our costs and expenses and grow our revenues and the effectiveness of our selling and marketing activities. We may not be able to achieve or sustain profitability or positive cash flow from operating activities, and if we achieve positive operating cash flow, it may not be sufficient to satisfy our anticipated capital expenditures and other cash needs. As such, we may not be able to fund our operating expenses and expenditures and may be unable to fulfill our financial obligations as they become due, which may result in voluntary or involuntary dissolution or liquidation proceeding of our Company and a total loss of your investment.

We have financed our operations to date primarily with proceeds from the sale of equity securities and convertible notes. As of December 31, 2016, we had approximately $91.1 million in cash and cash equivalents and restricted cash. In March 2016, we issued a total of 42,500,000 ordinary shares to an indirect wholly-owned subsidiary of Zall Group Ltd. (HKSE Code: 2098), or Zall Group, that amounted to $76.5 million for our working capital and capital expenditures purposes. We expect that our existing cash and restricted cash will be sufficient to fund our capital requirements for at least the next 12 months. However, we may need to raise additional capital to fund our continued operations. We cannot be certain that additional funding will be available on acceptable terms, or at all. Our failure to obtain sufficient capital or sufficient capital on acceptable terms could significantly harm our business, financial condition and prospects.

Products manufactured by our suppliers may be defective or inferior in quality or infringe on the intellectual property rights of others, which may materially and adversely affect our business and our reputation.

We source our products from over 4,800 selected active suppliers in China. Some of the products provided by our suppliers may be defective or of inferior quality. Such products may also infringe on the intellectual property rights of third parties. Defective, inferior or infringing products may adversely affect consumer perceptions of our company or the products we sell, which may lead to negative reviews that could harm our reputation. Although we have adopted internal policies and guidelines during our procurement process to make sure our suppliers and products we offer do not infringe on third-party intellectual property rights, we may receive, from time to time, notices claiming that our products have infringed on the intellectual property rights of others. If we determine that products sold on our websites and mobile applications are infringing on intellectual property rights, we will remove them from our websites and mobile applications. We are also involved in several intellectual property rights claims related to certain products sold on our website and mobile applications. Although such claims are insignificant and we expect them to be resolved in the near future, we cannot assure you that future claims will not have a material impact on our business and financial condition.

Irrespective of the validity of such allegations or claims, we may experience lost product sales or incur significant costs and efforts in defending against or settling such allegations or claims. If there is a successful claim against us, we may be required to refrain from further sale of the relevant products or pay substantial damages, and we may be unable to recoup our losses from our suppliers. In addition, since our products are sold to customers in many different countries and regions, we are subject to numerous different legal regimes governing mandatory product standards, intellectual property and tort. Such regimes may impose burdensome legal obligations, which may increase the costs and complexity of compliance. Regardless of whether we successfully defend against such claims, our reputation could be severely damaged. Any of these events could have a material adverse effect on our business, financial condition and results of operations**.**

We may have difficulties managing our marketing efforts and may face increased competition in our marketing efforts, which could materially and adversely affect our business and growth prospects.

We may have difficulty managing our marketing efforts as our business expands. Currently, we actively manage millions of keywords in 23 languages and display advertising on over 800,000 publisher sites. In addition, we actively engage with our users on social networking sites. However, given the rapid changes of Internet advertising, consumer preferences, the development of new forms of Internet marketing and the different forms of social media in each of our target countries and regions, we may have difficulties adapting our marketing techniques quickly and we may not sustain our customer acquisition rates, which may have a material and adverse effect on our business prospects.

We are highly dependent on our continuing relationships with our affiliate websites and major search engines around the world. Our advertising publishing partners for our affiliate marketing programs may cease, suspend or change the business terms in which we work with them. Search engines may introduce new products and features or modify their page ranking algorithms, which may make our marketing efforts more challenging and costly, or reduce our web traffic. They may also modify existing features or interfere with our ability to advertise on their platforms or to change the business terms on which we advertise. The occurrence of any such event could materially and adversely affect our ability to acquire new customers and thus negatively impact our business, growth prospects, financial condition and results of operations. Furthermore, as search engine marketing is based on a bidding system, other online advertisers may outbid us on our chosen advertising keywords, which may cause us to increase our marketing expenses and adversely affect our results of operations.

We currently derive our revenues from a limited number of product categories and any event that adversely affects the demand for our products in those product categories may harm our growth strategies and business prospects.

In 2016, we derived 34.1% and 65.9% of our net revenues of product sales from the sale of apparel and other general merchandise, respectively. A decrease in the demand for any of these product categories could have a material and adverse effect on our business prospects. While we have expanded and diversified our product offerings and revenue sources, sales in new products may not reach a level that would reduce our dependence on our existing product categories. In addition, if we are unable to deliver consistently high quality products in our new products, the number of customers for our products may decline. Our failure to successfully introduce new products may have a material and adverse effect on our business prospects and limit our growth.

Our expansion may lower our profit margins and materially and adversely affect our business, financial condition and results of operations.

We have traditionally focused on the sale of apparel and electronics and communication devices and derived a large percentage of our total net revenues from such products. We have since expanded our offerings by increasing the number of products in our other general merchandise product category, with a particular focus on small accessories and gadgets and home and garden, as well as beauty and sports and outdoor. We have also operated websites which focus on certain specific products, such as our *www.miniinthebox.com* website for the sale of small accessories and gadgets and launched mobile applications that offer a rich shopping experience across all product categories. This has required improvements to our technology and logistics infrastructure and increased marketing spending. We intend to continue to expand our product offerings and increase the variety and customization options of the products we offer in each of our categories.

These new businesses involve risks and challenges different from the sale of our traditional products. The introduction of other products imposes additional complications in logistics, supply chain management and marketing. For example, home and garden products introduced new complications due to shipping heavier and more fragile products. Furthermore, we may have to deal with customers in demographics that we have previously not targeted. We also face inventory risks and other challenges when addressing changing consumer demands and preferences. We may introduce new products, which may increase the risks of inventory write-downs and financing costs. As a result, we may not be able to compete successfully in these new markets, our costs may increase and our revenues and profit margins may decrease, all of which may materially and adversely affect our business, financial condition and results of operations.

We may not be able to successfully adopt new technologies or adapt our websites, mobile applications and systems to consumer requirements or emerging industry standards, which may materially and adversely affect our business, financial condition and results of operations.

The Internet and the online retail industry are characterized by rapid technological evolution. Changes in user and consumer preferences and the emergence of new industry standards and practices may render our existing proprietary technologies and systems obsolete. To remain competitive, we must enhance our technology infrastructure and adapt to the evolving online retail landscape. Not only do we need to constantly improve our user experience through personal computers, but we also need to enhance our user experience through mobile phones, handheld tablets or other devices. As new platforms and new devices are continually being released, it is difficult to predict the problems we may encounter to reach customers. If we are unable to adapt to changing market conditions or customer requirements in a cost-effective and timely manner, whether for technical, financial or other reasons, our business prospects, financial condition and results of operations may be materially adversely affected.

We use third-party couriers to deliver products and their failure to provide high quality delivery services or our failure to effectively manage our relationships with them may materially and adversely affect our business, financial condition and results of operations.

We use a network of third-party courier companies to deliver parcels to over 200 countries and territories. Interruptions to or failures in these third parties shipping services could prevent the timely or successful delivery of our products or the products of small business customers with whom we provide logistics services. These interruptions may be due to unforeseen events such as inclement weather, natural disasters, import or export restrictions, or labor unrest, which may be beyond our control or the control of these third-party couriers. For example, our distribution network is sensitive to fluctuation in oil prices, which may result in increased shipping costs from third- party courier companies, which may, in turn, increase the prices of our products and services and render our products and services less competitive.

If we do not deliver products to our customers in a timely manner or deliver damaged products, our customers may refuse to accept our products and become less confident in us. Many of our bestselling products, such as apparel, may be especially sensitive to delivery delays given that they are often purchased in anticipation of a specific date. Other products, such as electronics and fast fashion apparel for women, have a limited shelf-life and become quickly outdated. Certain products may not be delivered through certain couriers or may not be delivered to certain countries or regions. As a result, certain products may not be deliverable to certain customers or they may not be deliverable at a sufficiently low cost. In addition, if we are unable to ensure the delivery of products of the small businesses in which we provide logistics services to in a timely manner or such products became damaged during delivery, our business customers may no longer utilize services that we provide. Our third-party couriers may also offer us less favorable terms, which may increase our shipping cost and materially and adversely affect our financial condition and results of operations. Furthermore, if our third-party couriers terminate their cooperation with us or do not renew their agreements with us on terms acceptable to us upon the expiry of the existing agreements, we may not be able to find alternative couriers to provide delivery services in a timely and reliable manner, or at all, which may materially and adversely affect our financial condition and results of operations. We may not be able to promptly and successfully deliver products to consumers, which may result in the loss of their business and a material and adverse effect on our financial condition and reputation.

Our websites, mobile applications or product offerings may not receive positive market recognition and wide acceptance, which may materially and adversely affect our business, financial condition and results of operations. In addition, negative publicity, including negative Internet and blog postings from anonymous sources, about our company, our business, our management or our products could have a material adverse effect on our business, our reputation and the trading price of our ADSs.

Maintaining and enhancing the level of customer visits to and volume of customer purchases on our websites and mobile applications are critical to our ability to compete effectively. We intend to enhance the recognition of our websites and mobile applications and product offerings by expending significant time and resources on marketing and customer relations. However, we may not be able to achieve our goals in a short period of time and our marketing efforts may not achieve expected results.

Such efforts may also be jeopardized if we fail to maintain high product quality, fulfill orders for popular items, maintain and enhance high customer experience, provide high quality customer services, or offer efficient and reliable delivery. In addition, any negative publicity or disputes regarding our products, company, management or affiliated individuals or other online retailers in China may also materially and adversely affect our websites or branded products. For example, certain products sold on our websites were the subject of intellectual property right disputes, we have had difficulties receiving customer orders due to disruptions to the fiber optic cable connections out of China and there have been certain negative online reviews of our company, our websites and some of the products we sell. Furthermore, if our customer service representatives fail to satisfy the individual needs of customers, our reputation and customer loyalty could be negatively affected and we may lose potential or existing customers and experience a decrease in product sales. Failure to successfully promote and maintain positive consumer experience and awareness of our websites and mobile applications, damage to our reputation or brands or loss of consumer confidence could materially and adversely affect our results of operations and financial condition.

Factors important to maintaining and increasing the sales volumes of goods purchased from our websites and mobile applications include:

- our ability to maintain a convenient and reliable user experience as consumer preferences evolve and as we expand into new products and new business lines;

- our ability to increase repeat purchases by customers;

- our ability to increase purchase by mobile application users;

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- our ability to provide high quality customer services;
- our ability to offer products of sufficient quality at competitive prices;
- our ability to manage new and existing technologies and sales channels;
- our ability to increase website awareness among existing and potential consumers through various means of marketing and promotional activities;
- our ability to assure our customers of the security of our websites and mobile applications for online purchases; and
- the efficiency, reliability and service quality of our logistics and payment service providers.

Any failure to properly manage these factors could negatively impact our websites and mobile applications. Such failures may materially and adversely affect our business, financial condition and results of operations.

In addition, we have from time to time received negative publicity, including negative Internet and blog postings from anonymous sources, and anonymous allegations about our company, our business, our management and our products. We cannot assure you that we will not receive similar negative publicity, negative Internet or blog postings or anonymous allegations in the future. Any such negative publicity, negative Internet or blog postings or anonymous allegations, regardless of veracity, may have a material adverse effect on our business, our reputation and the trading price of our ADSs.

Failure to protect confidential information of our customers and our network against security breaches could damage our reputation and substantially harm our business and results of operations.

A significant challenge to online commerce and communications is the secure transmission of confidential information over public networks. Currently, product orders and payments for products we offer are made through our websites and mobile applications, except for certain orders and payments related to the sale of our products to customer in China. In addition, some online payments for our products are settled through third-party electronic platforms. In such transactions, maintaining complete security for the transmission of confidential information, such as our customers credit card information, personal information and billing addresses, on our websites and mobile applications are essential to maintain consumer confidence. We have no control over the security measures of third-party electronic payment service providers. We also hold certain other private information about our customers, such as their names, addresses, phone numbers and browsing and purchasing records.

We may not be able to prevent third parties, such as hackers or criminal organizations, from stealing information provided by our customers to us through our websites and mobile applications. Furthermore, our third- party logistics and payment service providers may accidentally or purposefully disclose information about our customers. We may also accidentally disclose such information due to employee negligence.

Significant capital and other resources may be required to protect against security breaches or to alleviate problems caused by such breaches. The methods used by hackers and others engaged in online criminal activities are increasingly sophisticated and constantly evolving. Even if we successfully adapt to and prevent new security breaches, any perception by the public that online commerce and transactions are becoming increasingly unsafe could inhibit the growth of e-commerce and other online services generally, which, in turn, may reduce the number of purchase orders we receive. Any compromise of our security or third-party service providers security could materially and adversely affect our reputation, business, prospects, financial condition and results of operations.

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We derive our revenues from products that represent discretionary spending and changes in global macroeconomic conditions may decrease the demand for our products and adversely affect our growth strategies and business prospects.

Many of our products may be viewed as discretionary items rather than necessities. Consequently, our results of operations tend to be sensitive to changes in macroeconomic conditions that impact consumer discretionary spending. During an economic downturn similar to the economic downturn in 2008 and 2009, customers may be less willing to purchase products that we offer. Challenging macroeconomic conditions also impact our customers ability to obtain consumer credit. While growth in the Europe, which represented the largest region to which our products were sold in 2014, 2015 and 2016, picked up in the first quarter of 2015, to the highest levels since Spring 2013, growth in this region has since fluctuated. It is difficult to predict household spending patterns in light of the global economic challenges and the European Central Bank s attempts to stimulate growth in the Eurozone. Other factors, including consumer confidence, employment levels, interest rates, tax rates, consumer debt levels and fuel and energy costs, could reduce consumer spending or change consumer purchasing habits.

We rely on third-party suppliers for our products and any deterioration in such business relationships or the quality of those products may materially and adversely affect our business, financial condition and results of operations.

We source our products from selected third-party suppliers. Our continued growth will increase our product demands, which will require us to increase our ability to source products of commercial quality on reasonable terms.

Our suppliers may:

- cease selling merchandise to us on terms acceptable to us;

- fail to deliver goods that meet consumer demands;

- encounter financial difficulties;

- terminate our relationships or enter into agreements with our competitors;

- have economic or business interests or goals that are inconsistent with ours and take actions contrary to our instructions, requests or objectives;

- be unable or unwilling to fulfill their obligations, including their obligations to meet our production deadlines, quality standards and product specifications;

- fail to expand their production capacities to meet our demands;

- encounter raw material or labor shortages or increases in raw material or labor costs, which may impact our procurement costs; or

- engage in other activities or employment practices that may harm our reputation.

Furthermore, agreements with our suppliers do not typically establish a fixed price for the purchase of products. As a result, we may be subject to price fluctuations based on changes in our suppliers businesses, cost structures or other factors. The occurrence of any of these events, alone or together, may have a material and adverse effect on our business, financial condition and results of operations. For example, suppliers in the coastal areas of eastern and southern China experienced labor shortages in 2010. Although our suppliers were not significantly affected by this event and managed to complete our orders in a timely manner, similar events may happen again in the future and our suppliers and, in turn, we, may be adversely impacted. In addition, our agreements with some of our suppliers do not contain non-compete clauses that would prevent those suppliers from producing similar products for any other third party. Any breakdown in our supplier relationships or our failure to timely resolve disputes with or complaints from our suppliers, could materially and adversely affect our business, financial condition and results of operations.

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Our business and profitability depend, to a significant extent, on international trade relationships between China and other countries and consumer confidence in Chinese products and any trade restrictions or losses in consumer confidence may materially and adversely affect our results of operations.

We are a China-based online retail company selling goods to consumers globally. As a result, if our consumers lose confidence in Chinese products or sovereign nations restrict trade with Chinese companies, we may suffer a competitive disadvantage. For example, such countries could support locally produced goods with subsidies, which may render our goods relatively more expensive. In addition, such countries could place quotas or taxes, such as retaliatory tariffs and anti-dumping restrictions, on goods produced in China, which would restrict our ability to export products to such countries. Consumers may also develop the presumption that products made in China are inferior in quality, more likely to be defective or more likely to violate intellectual property rights.

Such policies and attitudes could target Chinese companies in general, Chinese companies that export to foreign countries in specific or our company individually. We may not be able to affect the implementation of governmental policies or the prevalence of such biases and such policies and biases may reflect political relationships between the countries in which we conduct our businesses rather than any action taken by our company. To the extent that we suffer a competitive disadvantage as a result of restrictions in free trade or adverse consumer perceptions, our business, financial condition and results of operations may be materially and adversely affected.

We plan to expand our warehouses and distribution network. If we are not able to manage such expansion successfully, we may suffer a material and adverse effect on our business, financial condition and results of operations.

We believe our strategically located warehouses and our distribution network are essential to our success. We intend to expand our warehouses and distribution network in China and internationally to accommodate more purchase orders and provide better coverage of our target markets. We cannot assure you that we will be able to lease suitable facilities at commercially acceptable terms in accordance with our expansion plan. In addition, the expansion of our warehouses and distribution network will put pressure on our managerial, financial, operational and other resources, especially for warehouses outside of China. If we are unable to secure new facilities or effectively manage our expanded logistics operations and control increasing costs, our growth potential, results of operations and business could be materially and adversely affected. Furthermore, since the fourth quarter of 2011, we have entered into arrangements with certain suppliers under which the suppliers store their products at our warehouses. Such products are referred to in this annual report as co-location inventory. We record these products as inventory only when all liabilities and rights of ownership of the products are passed on to us upon the confirmation of orders by our customers. However, we bear the costs and expenses incurred related to the storage of co-location inventory in our warehouses, which increases our costs and expenses and reduces our profit and the warehousing spaces available for our own inventory. In addition, we are responsible for loss of and damages to such products in certain circumstances prior to the confirmation of orders by our customers, such as in the event of theft, but are not responsible for any loss of and damages to such products as a result of a force majeure event.

Increases in labor costs or restrictions in the supply of labor in China may materially and adversely affect our business, financial condition and results of operations.

We source our products primarily from third-party suppliers in China. With the rapid development of the Chinese economy, the cost of labor has risen and may continue to rise. Our results of operations will be materially and adversely affected if the labor costs of our suppliers increase. In addition, even if labor costs do not increase, we and our suppliers may not be able to find a sufficient number of workers to produce the products we offer.

Furthermore, pursuant to the new PRC labor contract law that became effective in 2008 and was amended on December 28, 2012, employers in China are subject to stricter requirements when signing labor contracts, paying remuneration, determining the term of employees probation and unilaterally terminating labor contracts. The new labor contract law and related regulations impose greater liabilities on employers and may significantly increase the costs of workforce reductions. If we or our suppliers decide to significantly change or reduce our workforces, the new labor contract law could adversely affect our ability to make such changes in a timely, favorable and effective manner. Any of these events may adversely affect our business, financial condition and results of operations.

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The proper functioning of our information infrastructure is essential to our business and any failure to maintain the satisfactory performance, security and integrity of our information infrastructure may materially and adversely affect our business, reputation, financial condition and results of operations.

Our net revenues from product sales depend on the number of visitors who purchase products on our websites and mobile applications and the volume of orders we fulfill. Telecommunications failures, errors encountered during system upgrades or system expansions, failures related to imbedded social networking functions, computer viruses, attempts to harm our systems, or any inability to maintain, develop and upgrade our existing information infrastructure may damage our hardware and software systems and database, interrupt access to our websites and mobile applications, disrupt our business activities, reveal confidential customer information, slow response times, degrade customer service, increase shipping and handling costs or delay order fulfillment, which may individually or collectively materially and adversely affect our business, reputation, financial condition and results of operations. For example, disruptions in the fiber optic cables used to connect computers located in the United States and China rendered us temporarily unable to receive orders placed by customers, which caused delays in our ability to process and deliver products to customers.

Our technology infrastructure may not function properly as a result of third-party action, employee error, malfeasance or otherwise and resulting in unauthorized access to our customers data. In addition, our domain names may not point to our IP address correctly due to malfeasance or neglect by our hosting solutions or domain name registries. For example, they may determine that we have violated contractual, civil or criminal duties and, as a result, suspend our domain names. Such errors would render our sites inaccessible for a period of time. Additionally, third parties may attempt to fraudulently induce employees or consumers into disclosing sensitive information such as user names, passwords or other information in order to gain access to our or our consumers data.

Even if we are successful in preventing security breaches, any perception by the public that online commercial transactions, or the privacy of user information, are increasingly unsafe or vulnerable to attack could inhibit the growth of online retailers and other online services generally, which, in turn, may have a material adverse effect on our business, reputation, financial condition and results of operations.

Taxation risks could materially and adversely affect our business and financial condition.

We generally do not collect product sales or other taxes on shipments of our goods to most countries in the world except mainland China, Hong Kong and Poland. However, since we are deepening our penetration of geographic markets globally, we may be subject to tax regulations in other geographic markets. In addition, we may become subject to new regulations as regional and national governments may impose new tax laws or revise existing tax laws, especially with regards to Internet sales.

Levy of sales taxes may increase the costs of our products to our consumers and reduce our competitive advantage over our competitors that do not collect such sales taxes. The imposition by regional or national governments of various taxes upon Internet commerce could create administrative burdens for us, put us at a competitive disadvantage if they do not impose similar obligations on all of our online competitors and decrease our future product sales. A successful assertion by one or more foreign countries that we should collect sales or other taxes on the sale of merchandise or services could result in substantial tax liabilities for past product sales, decrease our competitiveness with local retailers, and materially and adversely affect our business, financial condition and results of operations. In addition, we may be required to incorporate corporate entities in different jurisdictions around the world in order to deliver our products to such jurisdictions, which may have uncertain tax implications.

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Our growth depends on expanding in various geographic markets and such expansion may pose new logistical, operational and marketing challenges that may materially and adversely affect our business prospects.

We plan to further increase the sales of our products by deepening our penetration of geographic markets globally. Although our products are sold to customers in over 200 countries and territories, we still have relatively little experience in many countries in the world. It is costly to establish, develop and maintain international operations and websites and mobile applications and promote our brand internationally. The expansion of product sales into such geographic markets may not be profitable on a sustained basis for many reasons including, but not limited to:

- local economic and political conditions;
- government regulation of online retail, other online services and electronic devices and restrictive governmental actions (such as trade protection measures, including export duties and quotas and custom duties and tariffs), nationalization and restrictions on foreign ownership;
- restrictions on sales or distribution of certain products or services and uncertainty regarding intellectual property rights and liability for products, services and content on our websites and mobile applications or social marketing channels;
- business licensing or certification requirements, such as for imports, exports and electronic devices;
- limited fulfillment and technology infrastructure;
- laws and regulations regarding consumer protection, import and export requirements, duties, tariffs, other trade-related barriers or restrictions, data protection, privacy, network security, encryption and restrictions on pricing or discounts;
- lower levels of Internet use;
- lower levels of consumer spending and fewer growth opportunities compared to our current geographic markets;

- lower levels of credit card usage and increased payment risk; and

- difficulty in staffing, developing and managing foreign operations as a result of language and cultural differences.

As we expand the sale of our products to other countries, competition will intensify. Local companies may have a substantial competitive advantage because of their greater understanding of, and focus on, local consumers, as well as their more established local brand names. This may benefit from reduced logistics costs and marketing. We may not be able to hire, train, retain and manage required personnel, which may limit our international growth.

As new markets have different business practices and consumer demand may vary significantly by region, our experience in the geographic markets on which we currently focus may not be applicable in other parts of the world. For example, we may need to build infrastructure in foreign countries to remain competitive in such markets. Furthermore, deepening our geographic penetration entails increased complexity for our managers and employees including, but not limited to, difficulties associated with managing a more diverse customer base, the challenges of meeting different regulatory regimes and requirements, partnering with different local logistics providers and other business partners, managing more complex marketing efforts and providing customer support in different languages.

We currently derive only a small portion of our product sales from customers in China, but we may expand our operations in China in the future. We will encounter new challenges in operations, marketing and logistics. Our ability to operate competitively in international markets may not render us similarly competitive in the market in China. For example, our logistics networks will need to be optimized locally. To the extent that we cannot increase our market share in China, we may incur costs that we may not recover. Even if we are successful in increasing our market share in China, we may suffer from increased competition from other Chinese companies. We may not compete successfully against companies with stronger brands, greater financial resources, greater political support or more attractive terms for their suppliers, managers or employees.

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In addition, our expansion into China may suffer due to uncertainties and various factors affecting the development of online retail in China. For example, Internet and broadband use and penetration may decline, consumer confidence in online shopping may decrease, the quality of alternative retail channels may increase, sufficiently reliable or secure logistic or payment methods may not be available or the Chinese economy may deteriorate.

To the extent that we cannot successfully expand our operations in other geographic markets, our business, financial condition and results of operations may be materially and adversely affected.

Fluctuations in currency exchange rates may make us less competitive and may make our growth and future prospects uncertain and difficult to evaluate.

We are exposed to fluctuations in foreign currency exchange rates. We sell to customers in over 200 countries and territories. Many of our customers pay for our products in currencies other than U.S. dollars but we report our financial results in U.S. dollars and, as a result, our financial results may be impacted by fluctuations in foreign currency exchange rates. Since January 2014, the U.S. Dollar Index, a measure of the value of the U.S. dollars against a basket of six major world currencies, has appreciated over 20%. In particular, Europe represented the largest region to which our products were sold in 2016 and our net revenues generated from Europe was 49.6% of our total net revenues for the same year. Since January 2014, the U.S. dollar has, on the whole, been appreciating against the Euro and in December 2016, the Euro fell to a 13-year low against the U.S. dollar with 1 Euro equating 1.04 U.S. dollars. If the U.S. dollar continues to appreciate against foreign currencies, our translation of foreign currency denominated transactions will result in lower total net revenues, operating expenses and net income. As we are deepening our penetration of geographic markets globally, our exposure to exchange rate fluctuations has increased. We have no hedges against currency risk. Fluctuations in foreign currency exchange rates could significantly impact our financial results, which may result in an impact on our share prices.

Our business depends substantially on the continued efforts of our executive officers and our business may be severely disrupted if we lose their services.

Our future success depends substantially on the continued efforts of our executive officers. Competition for senior management and other key personnel is intense, and the pool of suitable candidates is very limited. We may not be able to retain the services of our senior executives or other key personnel, or attract and retain senior executives or key personnel in the future. If one or more of our executive officers are unable or unwilling to continue their employment with us, we may not find replacements in a timely manner, or at all, our business may be severely disrupted and our financial condition and results of operations may be materially and adversely affected. We may also incur additional expenses to recruit and retain qualified replacements.

If any of our executive officers joins a competitor or forms a competing company, we may lose customers, suppliers, partners and know-how. Each of our executive officers has entered into an employment agreement with us, which contains confidentiality and non-compete provisions. However, if any dispute arises between our executive officers and us, we may not be able to enforce these non-compete provisions in China, where these executive officers reside, in light of uncertainties with China s legal system.

If we are unable to attract, train and retain qualified personnel, our business, financial condition and results of operations may be materially and adversely affected.

Our business is supported and enhanced by a team of highly skilled employees who are critical to maintaining the quality and consistency of our business and reputation. It is important for us to attract qualified employees, especially marketing personnel, designers, supply chain managers, or engineers with high levels of experience in creative design, software development and Internet-related services. Competition for these employees is intense. In order to attract prospective employees and retain current employees, we may have to increase our employee compensation by a larger amount and at a faster pace than expected, which would increase our operating expenses. In addition, we must hire and train qualified employees in a timely manner to keep pace with our rapid growth while maintaining the quality of our operations in various geographic locations.

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We must also provide continuous training to our employees so that they have up-to-date knowledge of various aspects of our operations and can meet our demand for high quality services. If we fail to do so, the quality of our services may deteriorate in one or more of the markets where we operate, which may cause a negative perception of our brand and adversely affect our business. Finally, disputes between us and our employees may arise from time to time and if we are not able to properly handle our relationship with our employees, our business, financial condition and results of operations may be adversely affected.

Our branding efforts for our products may be costly and may not obtain positive market recognition which may materially and adversely affect our business, financial condition and results of operations.

We have launched our own branded product lines, which require more research, design and marketing costs than our private label products. These costs may not be recovered from sufficient sales of these branded products. These brands may not receive or maintain positive market recognition. Furthermore, it may take time and additional expenditures before we realize that our branding efforts have been unsuccessful. As a result of these efforts to develop branded products, we may incur costs without corresponding increases in revenues which may materially and adversely affect our business, financial condition and results of operations.

Our results of operations are subject to quarterly fluctuations due to a number of factors that could adversely affect our business and the trading price of the ADSs.

We experience seasonality in our business, reflecting seasonal fluctuations in online and offline retail patterns in general and for our products. For example, product sales may be higher in the fourth quarter of a calendar year due to the Christmas holidays. Our product mix may experience quarterly shifts which may cause our margins to fluctuate from quarter to quarter.

Due to the foregoing factors, our operating results in one or more future quarters may fall below the expectations of securities analysts and investors. In such event, the trading price of the ADSs may be materially and adversely affected.

We may not be able to prevent unauthorized use of our intellectual property, which could harm our business and competitive position.

We regard our trademarks, service marks, domain names, trade secrets, proprietary technologies and similar intellectual property critical to our success and we currently rely on a mix of trademark law, trade secret protection and confidentiality and license agreements with our employees, suppliers, partners and others to protect our proprietary rights. Our trademarks and service marks may be invalidated, circumvented or challenged. Trade secrets are difficult to protect and our trade secrets may be leaked or otherwise become known or be independently discovered by competitors. Confidentiality agreements may be breached and we may not have adequate remedies for any breach.

It is often difficult to create and enforce intellectual property rights in China. Even where adequate laws exist in China, it may not be possible to obtain swift and equitable enforcement of such laws, or to obtain enforcement of a court judgment or an arbitration award delivered in another jurisdiction and, accordingly, we may not be able to effectively protect our intellectual property rights or enforce agreements in China. Preventing any unauthorized use of our intellectual property is difficult and costly and the steps we have taken may be inadequate to prevent the misappropriation of our technologies.

We are subject to payment-related risks which may materially and adversely affect our business, financial condition and results of operations.

Our customers may choose from a wide range of payment methods. As we offer new payment options to our customers, we may be subject to additional regulations, compliance requirements and fraud.

We rely on third parties, such as PayPal, WorldPay and Global Collect, to provide certain payment processing services, including the processing of credit card and debit card transactions. Our business may be disrupted if these companies become unwilling or unable to provide these services to us. We are also subject to payment card association operating rules, certification requirements and rules governing electronic funds transfers, which could change or be reinterpreted to make it difficult or impossible for us to comply. If we fail to comply with these rules or requirements, we may be subject to fines and higher transaction fees and lose our ability to accept credit and debit card payments from our customers, process electronic funds transfers, or facilitate other types of online payments and our business and operating results could be adversely affected.

Under current credit card practices, we are liable for fraudulent credit card transactions because we do not require a cardholder s signature. We do not currently carry insurance against this risk. Although we have only experienced minimal losses from credit card fraud, we face the risk of significant losses from this type of fraud as our net product sales increase and as we expand internationally. Our failure to adequately control fraudulent credit card transactions could damage our reputation and brand and substantially harm our business and results of operations. Additionally, for certain payment transactions, including credit and debit cards, we pay interchange and other fees. These fees may increase over time, which would raise our operating costs and lower our operating margins.

Our business is subject to the laws of various jurisdictions, many of which are unsettled and still developing and could subject us to claims or otherwise harm our business.

We are subject to a variety of laws in various jurisdictions, including Hong Kong, China, the United States and other countries, including laws regarding data retention, privacy and consumer protection, that are continuously evolving and developing. The scope and interpretation of the laws that are or may be applicable to us are often uncertain and may be conflicting. For example, laws relating to the liability of providers of online services for activities of their users and other third parties are currently being tested by a number of claims, including actions based on invasion of privacy and other torts, unfair competition, copyright and trademark infringement and other theories based on the nature and content of the materials searched, the advertisements posted, or the content provided by users. In addition, regulatory authorities around the world are considering a number of legislative and regulatory proposals concerning data protection and other matters that may be applicable to our business. It is also likely that as our business grows and evolves and our solutions are used in a greater number of countries, we will become subject to laws and regulations in additional jurisdictions. It is difficult to predict how existing laws will be applied to our business and the new laws to which we may become subject.

If we are not able to comply with these laws or regulations or if we become liable under these laws or regulations, we could be directly harmed and we may be forced to implement new measures to reduce our exposure to this liability. This may require us to expend substantial resources or to discontinue certain solutions. In addition, the increased attention focused upon liability issues as a result of lawsuits and legislative proposals could harm our reputation or otherwise impact the growth of our business. Any costs incurred as a result of this potential liability could harm our business, financial condition and results of operations.

We do not have any business liability, disruption or litigation insurance and any business disruption or litigation we experience might result in our incurring substantial costs and diversion of resources.

As the insurance industry in China is still in an early stage of development, insurance companies in China currently offer limited business insurance products. We have determined that the difficulties associated with acquiring product liability or business interruption insurance coverage in China on commercially reasonable terms make it impractical for us to have such insurance. As such, we currently only have limited insurance covering certain of our warehouses. Any product liability claims or business disruption, natural disaster could result in our incurring substantial costs and diversion of resources, which would have an adverse effect on our business, financial condition and results of operations.

If we fail to maintain an effective system of internal control over financial reporting, we may be unable to accurately report our financial results or prevent fraud and investor confidence in our company and the market price of the ADSs may be adversely affected.

In preparing our consolidated financial statements as of and for the year ended December 31, 2016 included in our annual report on Form 20-F for 2016, we identified certain control deficiencies in our internal control over financial reporting. We have taken a variety of measures to address these control deficiencies. With these measures over the identified deficiencies, we concluded that our internal control over financial reporting was effective as of December 31, 2016. See also Item 15. Controls and Procedures Management s Annual Report on Internal Control over Financial Reporting. We cannot assure you that we will be able to continue to implement an effective system of internal control, or that we will not identify material weaknesses or significant deficiencies in the future.

As a public company in the United States, we are subject to the Sarbanes-Oxley Act of 2002, or the Sarbanes-Oxley Act. Our independent registered public accounting firm will be required to attest to the effectiveness of our internal control over financial reporting beginning with our annual report on Form 20-F following the date on which we cease to qualify as an emerging growth company, which may be up to five full fiscal years following the date of our initial public offering in June 2013. Even if our management concludes that our internal control over financial reporting is effective, our independent registered public accounting firm, after conducting its own independent testing, may issue a report that is qualified if it is not satisfied with our internal controls or the level at which our controls are documented, designed, operated or reviewed, or if it interprets the relevant requirements differently from us**.** As a public company, our reporting obligations may place a significant strain on our management, operational and financial resources and systems for the foreseeable future. See also Item 15. Controls and Procedures Management s Annual Report on Internal Control over Financial Reporting.

In addition, if we fail to maintain the adequacy of our internal control over financial reporting, as these standards are modified, supplemented or amended from time to time, we may not be able to conclude on an ongoing basis that we have effective internal control over financial reporting in accordance with Section 404 of the Sarbanes-Oxley Act. If we fail to achieve and maintain an effective internal control environment, we could suffer material misstatements in our financial statements and fail to meet our reporting obligations, which would likely cause investors to lose confidence in our reported financial information. This could in turn limit our access to capital markets, harm our results of operations, and lead to a decline in the trading price of our ADSs. Additionally, ineffective internal control over financial reporting could expose us to increased risk of fraud or misuse of corporate assets and subject us to potential delisting from the stock exchange on which we list, regulatory

investigations and civil or criminal sanctions.

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As an emerging growth company, we will not be required to have auditor attestation of the effectiveness of our internal controls.

We are an emerging growth company as defined in the JOBS Act, and we intend to take advantage of certain exemptions from various requirements that are applicable to other public companies that are not emerging growth companies including, most significantly, not being required to comply with the auditor attestation requirements of Section 404 of the Sarbanes-Oxley Act for so long as we are an emerging growth company, which may be for as long as five years following our initial public offering in June 2013 . As a result of our current status as an emerging growth company, our investors may not have access to certain information that they may deem important.

The JOBS Act also provides that an emerging growth company need not comply with any new or revised financial accounting standard until such date that a non-reporting company is required to comply with such new or revised accounting standard. However, we have elected to opt out of this provision and, as a result, we will comply with new or revised accounting standards as required when they are adopted for public companies. This decision to opt out of the extended transition period under the JOBS Act is irrevocable.

We may engage in acquisitions that may present integration challenges, disrupt our business and lower our operating results and the value of your investment.

As part of our business strategy, we regularly evaluate investments in, mergers with or acquisitions of, complementary businesses, joint ventures, services and technologies. For example, in May 2010, Lanting Huitong acquired Shanghai Ouku, which operates *www.ouku.com* , for $2.2 million (RMB14.3 million). In addition, we acquired the fashion focused site business from Ador, Inc. in December 2013. In February 2015, we made a minority investment in Shantou Demon Network Technology Co., Ltd., which owns an online website that specialized in cross-border packages tracking, for $2.1 million (RMB12.9 million). Acquisitions and investments involve numerous risks, including:

- potential failure to achieve the expected benefits of the combination or acquisition;
- difficulties in and the cost of integrating operations, technologies, services and personnel; and
- potential write-offs of acquired assets or investments.

Furthermore, as a result of Lanting Huitong s acquisition of Shanghai Ouku, we have recorded goodwill as well as certain acquired intangibles. Such goodwill and intangible assets are tested for impairment by us. In 2011, we recorded an impairment loss on goodwill and intangible assets of $1.9 million.

In addition, if we finance acquisitions by issuing equity or convertible debt securities, our existing shareholders may be diluted, which could affect the market price of the ADSs. Further, if we fail to properly evaluate and execute acquisitions or investments, our business and prospects may be seriously harmed and the value of your investment may decline.

Furthermore, we may fail to identify or secure suitable acquisition opportunities or our competitors may capitalize on such opportunities before we do, which could impair our ability to compete with our competitors and adversely affect our growth prospects and results of operations.

Any catastrophe, including outbreaks of health pandemics and other extraordinary events, could severely disrupt our business operations.

Our operations are vulnerable to interruption and damage from natural and other types of catastrophes, including earthquakes, fire, floods, hail, windstorms, severe winter weather (including snow, freezing water, ice storms and blizzards), environmental accidents, power loss, communications failures, explosions, man-made events such as terrorist attacks and similar events. Due to their nature, we cannot predict the incidence, timing and severity of catastrophes. In March 2011, Japan was struck by a 9.0-magnitude earthquake. In May 2008 and April 2013, Sichuan Province in southwest China experienced severe earthquakes. Although the Japan earthquake together with the resulting tsunami and the Sichuan Province earthquakes did not materially affect our business, other occurrences of natural disasters, as well as accidents and incidents of adverse weather in or around our warehouses, sourcing offices or suppliers may materially and adversely affect our business and results of operations. We may also be particularly vulnerable to catastrophes in Europe and North America, where most of our customers are located. In addition, the recent uncertainty on the Korean Peninsula may also have an adverse impact on our business operations.

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Changing climate conditions, primarily rising global temperatures, may be increasing, or may in the future increase, the frequency and severity of natural catastrophes. If any such catastrophe or extraordinary event occurs in the future, our ability to operate our business could be seriously impaired. Such events could make it difficult or impossible for us to deliver our services and products to our consumers and could decrease demand for our products. Because we only have limited insurance covering certain of our warehouses and do not maintain insurance for all of our properties, significant time could be required to resume our operations and our financial position and operating results could be materially and adversely affected in the event of any major catastrophic event.

In addition, our business could be materially and adversely affected by the outbreak of influenza A (H1N1), commonly referred to as swine flu, avian influenza, including H7N9, severe acute respiratory syndrome (SARS), Ebola virus disease or other pandemics. Any occurrence of these pandemic diseases or other adverse public health developments in China or elsewhere could severely disrupt our staffing or the staffing of our suppliers and couriers and otherwise reduce the activity levels of our work force and the work force of our suppliers and couriers, causing a material and adverse effect on our business operations.

Failure to renew the lease of our existing premises or to renew such leases at acceptable terms could materially and adversely affect our business.

All of our offices and warehouses are presently located on leased premises. At the end of each lease term, we may not be able to negotiate an extension of the lease and may therefore be forced to move to a different location, or the rent we pay may increase significantly. This could disrupt our operations and adversely affect our profitability. A number of our leases will expire in the near future and are subject to renewal at market prices, which could result in a substantial increase in the rent at the time of renewal. We compete with other businesses for premises at certain locations or of desirable sizes and some landlords may have entered into long-term leases with our competitors for such premises. We may not be able to obtain new leases at desirable locations or renew our existing leases on acceptable terms or at all, which could materially and adversely affect our business.

We rely on certain individuals and their affiliates to register at and receive funds from some of our supplemental online outlets.

In addition to the sale of our products through our websites and mobile applications, we also sell through outlets on other high traffic online marketplace platforms. In addition to such supplemental online outlets registered under our company name, some of our employees have also registered for online outlets in their own name to sell our products and hold the title to these online outlets on the marketplace platforms and in certain cases, their associated bank accounts. We enter into contractual relationships with such employees to obligate them to transfer to us payments corresponding to amounts they receive from customers for the sale of our products on these supplemental online outlets. Prior to our receipt of such payments, we classify cash held in these accounts in our prepaid expenses and other current assets. If such employees choose not to perform their contractual obligations with us, we may incur costs to recover such payments and we may not be able to recover these cash balances.

We are exempted from certain corporate governance requirements of the New York Stock Exchange.

We are exempted from certain corporate governance requirements of the New York Stock Exchange by virtue of being a foreign private issuer. We are required to provide a brief description of the significant differences between our corporate governance practices and the corporate

governance practices required to be followed by U.S. domestic companies under the New York Stock Exchange. The standards applicable to us are considerably different than the standards applied to U.S. domestic issuers. For instance, we are not required to:

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- have a majority of the board be independent (other than due to the requirements for the audit committee under the Exchange Act);

- have a minimum of three members in our audit committee;

- have a compensation committee, a nominating or corporate governance committee;

- have regularly scheduled executive sessions with only independent directors;

- have executive session of solely independent directors each year; or

- adopt and disclose a code of business conduct and ethics for directors, officers and employees.

We have relied on and intend to continue to rely on some of these exemptions. As a result, you may not be provided with the benefits of certain corporate governance requirements of the New York Stock Exchange.

Risks Related to Our Corporate Structure

Substantial uncertainties exist with respect to the enactment timetable, final scope, interpretation and implementation of the draft PRC Foreign Investment Law recently published for public comments, including how it may impact the viability of our current corporate structure, corporate governance and business operations.

The PRC Ministry of Commerce published a discussion draft of the proposed Foreign Investment Law in January 2015 aiming to, upon its enactment, replace the trio of existing laws regulating foreign investment in China, namely, the Sino-foreign Equity Joint Venture Enterprise Law, the Sino-foreign Cooperative Joint Venture Enterprise Law and the Wholly Foreign-invested Enterprise Law, together with their implementation rules and ancillary regulations. The draft Foreign Investment Law embodies an expected PRC regulatory trend to rationalize its foreign investment regulatory regime in line with prevailing international practice and the legislative efforts to unify the corporate legal requirements for both foreign and domestic investments. The Ministry of Commerce solicited comments on this draft in 2015, but no timetable as to when it will be enacted has been published so far. As such, substantial uncertainties exist with respect to its enactment timetable, final scope, interpretation and implementation. The draft Foreign Investment Law, if enacted as proposed, may materially impact the viability of our current corporate structure, corporate governance and business operations in several ways.

Among other things, the draft Foreign Investment Law expands the definition of foreign investment and introduces the principle of actual control in determining whether a company is considered a foreign-invested enterprise, or FIE. The draft Foreign Investment Law specifically provides that entities established in China but controlled by foreign investors will be treated as FIEs, whereas an entity set up in a foreign jurisdiction would nonetheless be, upon market entry clearance by the Ministry of Commerce, treated as a PRC domestic investor provided that the entity is controlled by PRC entities and/or citizens. In this connection, control is broadly defined in the draft law to cover the following summarized categories: (i) holding 50% of more of the voting rights of the subject entity; (ii) holding less than 50% of the voting rights of the subject entity but having the power to secure at least 50% of the seats on the board or other equivalent decision making bodies, or having the voting power to materially influence the board, the shareholders meeting or other equivalent decision making bodies; or (iii) having the power to exert decisive influence, via contractual or trust arrangements, over the subject entity s operations, financial matters or other key aspects of business operations. Once an entity is determined to be an FIE, it will be subject to the foreign investment restrictions or prohibitions set forth in a negative list, to be separately issued by the State Counsel at a later time, if the FIE is engaged in an industry included on the negative list. Unless the underlying business of the FIE falls within the negative list, which calls for market entry clearance by the Ministry of Commerce, prior approval from the government authorities as mandated by the existing foreign investment legal regime would no longer be required for establishment of the FIE.

The VIE structure has been adopted by many PRC-based companies, including us, to obtain necessary licenses and permits in industries that are currently subject to foreign investment restrictions in China. See We conduct certain aspects of our businesses in China through our VIEs by means of contractual arrangements. If the PRC government determines that these contractual arrangements do not comply with applicable regulations, our business could be materially and adversely affected. and Item 4. Information on the Company C. Organizational Structure. Under the draft Foreign Investment Law, VIEs that are controlled via contractual arrangements would also be deemed FIEs, if they are ultimately controlled by foreign investors. Therefore, for any companies with a VIE structure in an industry category that is on the negative list, the VIE structure may be deemed legitimate only if the ultimate controlling person(s) is/are of PRC nationality (either PRC companies or PRC citizens). Conversely, if the actual controlling person(s) is/are of foreign nationalities, then the variable interest entities will be treated as FIEs and any operation in the industry category on the negative list without market entry clearance may be considered illegal. There are uncertainties as to whether the Foreign Investment Law, once it is enacted, will have retrospective effect on existing VIE structures such as ours, or whether it will grant real and full grandfathering and grace periods for such existing VIE structures.

The draft Foreign Investment Law has not taken a position on what actions will be taken with respect to existing companies with a VIE structure, whether or not these companies are controlled by Chinese parties, and the Ministry of Commerce is soliciting comments from the public on this point. Moreover, it is uncertain whether the Internet industry, in which our VIEs operate, will be subject to the foreign investment restrictions or prohibitions set forth in the negative list to be issued. The value-added telecommunications services (e-commerce) that we conduct through our VIEs are no longer subject to foreign investment restrictions as set forth in the Catalogue for the Guidance of Foreign Investment Industries issued by the National Development and Reform Commission and the Ministry of Commerce in March 2015, or the Catalogue. It is unclear whether the new negative list will be different from the Catalogue. If the enacted version of the Foreign Investment Law and the final negative list mandate further actions, such as Ministry of Commerce market entry clearance or certain restructuring of our corporate structure and operations, to be completed by companies with existing VIE structure like us, we face substantial uncertainties as to whether these actions can be timely completed, or at all, and our business and financial condition may be materially and adversely affected.

The draft Foreign Investment Law, if enacted as proposed, may also materially impact our corporate governance practice and increase our compliance costs. For instance, the draft Foreign Investment Law imposes stringent ad hoc and periodic information reporting requirements on foreign investors and the applicable FIEs. Aside from investment implementation report and investment amendment report that are required at each investment and alteration of investment specifics, an annual report is mandatory, and large foreign investors meeting certain criteria are required to report on a quarterly basis. Any company found to be non-compliant with these information reporting obligations may potentially be subject to fines and/or administrative or criminal liabilities, and the persons directly responsible may be subject to criminal liabilities.

We conduct certain aspects of our businesses in China through our VIEs by means of contractual arrangements. If the PRC government determines that these contractual arrangements do not comply with applicable regulations, our business could be materially and adversely affected.

We conduct the operation of our domestic websites as well as certain technology research and development and other supporting functions through Lanting Huitong and its subsidiary, Shanghai Ouku, and conduct certain technology research and development functions through Lanting Gaochuang in China. We receive substantially all of the economic benefits of Lanting Huitong and Lanting Gaochuang as their primary beneficiary through contractual arrangements with them and their shareholders. For a description of these contractual arrangements, see Item 4. Information on the Company C. Organizational Structure.

Although we believe we comply and will continue to comply with current PRC regulations, the PRC government may not agree that these contractual arrangements comply with PRC licensing, registration or other regulatory requirements, with existing requirements or policies or with requirements or policies that may be adopted in the future, particularly with regards to Lanting Huitong as a key operator of our domestic websites. If the PRC government determines that we are not in compliance with applicable laws, it may revoke our business and operating licenses, require us to discontinue or restrict our operations, restrict our right to collect revenues, block our websites, require us to restructure our operations, impose additional conditions with which we may not be able to comply, impose restrictions on our business operations or on our customers, or take other regulatory or enforcement actions against us that could be harmful to our business.

We rely on contractual arrangements with Lanting Huitong and its shareholders for the operation of our domestic websites as well as conduct certain technology research and development and other supporting functions in China and contractual arrangements with Lanting Gaochuang and its shareholders for certain technology research and development functions, which may not be as effective as direct ownership. If Lanting Huitong and its shareholders or Lanting Gaochuang and its shareholders fail to perform their obligations under these contractual arrangements, we may have to resort to litigation or arbitration to enforce our rights, which may be time-consuming, unpredictable, expensive and damaging to our operations and reputation.

We have relied and expect to continue to rely on contractual arrangements with Lanting Huitong to operate our domestic websites as well as conduct certain technology research and development and other supporting functions in China and contractual arrangements with Lanting Gaochuang to perform certain technology research and development functions. For a description of these contractual arrangements, see Item 4. Information on the Company C. Organizational Structure. These contractual arrangements provide us with effective control over these entities and allow us to obtain economic benefits from them. Although we have been advised by our PRC counsel, TransAsia Lawyers, that these contractual arrangements are in compliance with current PRC laws, these contractual arrangements may not be as effective in providing control as direct ownership. For example, Lanting Huitong and its shareholders could breach their contractual arrangements with us by failing to operate our online retail business in an acceptable manner or taking other actions that are detrimental to our interests. In addition, if the shareholders of Lanting Huitong or Lanting Gaochuang refuse to transfer their equity interests in Lanting Huitong or Lanting Gaochuang to us or our designee when we exercise our call option pursuant to these contractual arrangements, we may have to take legal actions to compel them to perform their contractual obligations.

If we were the controlling shareholder of our VIEs with direct ownership, we would be able to exercise our rights as shareholders, rather than our rights under the powers of attorney, to effect changes to their boards of directors, which in turn could implement changes at the management and operational level. However, under the current contractual arrangements, as a legal matter, if our VIEs or their respective shareholders fail to perform their obligations under these contractual arrangements, we may incur substantial costs to enforce such arrangements and rely on legal remedies under PRC law, which may not be sufficient or effective.

All of these contractual arrangements are governed by PRC law and provide for the resolution of disputes through arbitration in the PRC. Accordingly, these contracts would be interpreted in accordance with PRC law and any disputes would be resolved in accordance with PRC legal procedures. The legal system in the PRC is not as developed as in other jurisdictions, such as the United States. As a result, uncertainties in the PRC legal system could limit our ability to enforce these contractual arrangements. Under PRC law, rulings by arbitrators are final, parties cannot appeal the arbitration results in court and the prevailing parties may only enforce the arbitration awards in PRC courts through arbitration award recognition proceedings, which would incur additional expenses and delay. If we are unable to enforce these contractual arrangements, we may not be able to exert effective control over our VIEs and our ability to conduct our businesses may be negatively affected.

If we are unable to enforce these contractual arrangements, or if we suffer significant delay or other obstacles in the process of enforcing these contractual arrangements, our business and operations in China could be disrupted, which could materially and adversely affect our results of operations and damage our reputation. See Item 3. Key Information D. Risk Factors Risks Related to Doing Business in China Uncertainties with respect to the Chinese legal system could adversely affect us.

The shareholders of Lanting Huitong and Lanting Gaochuang have potential conflicts of interest with us, which may adversely affect our business.

Certain of our founding shareholders, Mr. Quji (Alan) Guo, Mr. Xin (Kevin) Wen and Mr. Liang Zhang, who collectively owned 9.6% of the shares of our company as of March 24, 2017, are also the shareholders of Lanting Huitong. Mr. Guo also holds 51.0% of Lanting Gaochuang. Thus, conflicts of interest between their duties to our company and their interests as the controlling shareholders of Lanting Huitong or Lanting Gaochuang may arise. They may not act entirely in our interests when conflicts of interest arise and conflicts of interest may not be resolved in our favor. In addition, Mr. Guo, Mr. Wen and Mr. Zhang could violate their non-competition or employment agreements with us or their legal duties by diverting business opportunities from us. If we are unable to resolve any such conflicts, or if we suffer significant delays or other obstacles as a result of such conflicts, our business and operations could be severely disrupted, which could materially and adversely affect our results of operations and reputation. See Item 3. Key Information D. Risk Factors Risks Related to Doing Business in China Uncertainties with respect to the Chinese legal system could adversely affect us.

We may lose the ability to use and enjoy assets held by Lanting Huitong and its subsidiary or assets held by Lanting Gaochuang that are important to the operations of our business if such entity goes bankrupt or becomes subject to a dissolution or liquidation proceeding.

Lanting Huitong and its subsidiary, Shanghai Ouku, manage *www.ouku.com* and other websites targeting consumers in China. Lanting Gaochuang performs certain research and development functions. Both hold certain assets and perform certain functions that are important to the operations of our business. If Lanting Huitong, Shanghai Ouku or Lanting Gaochuang go 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 Lanting Huitong, Shanghai Ouku or Lanting Gaochuang undergoes a voluntary or involuntary dissolution or liquidation proceeding, third-party creditors may claim rights to some or all of these assets, thereby hindering our ability to operate our business in the PRC, which may materially and adversely affect our business, financial condition and results of operations.

If Lanting Huitong, Shanghai Ouku or Lanting Gaochuang fail to obtain and maintain the requisite assets, licenses and approvals required 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 and numerous regulatory authorities of the central PRC government are empowered to issue and implement regulations governing various aspects of the Internet industry. See Item 4. Information on the Company B. Business Overview Regulation. Lanting Huitong and Shanghai Ouku, due to their operation of our domestic websites, are required to obtain and maintain certain assets relevant to their business as well as applicable licenses and approvals from different regulatory authorities in order to provide their current services. These assets and licenses are essential to our business operations in China and are generally subject to annual review by the relevant governmental authorities. Furthermore, Lanting Huitong, Shanghai Ouku or Lanting Gaochuang may be required to obtain additional licenses other than those currently in place. If they fail to obtain or maintain any of the requisite assets, licenses or approvals, their continued business operations in the Internet industry may subject them to various penalties, such as confiscation of illegal total net revenues, fines and the discontinuation or restriction of their operations. Any such disruption in the business operations of Lanting Huitong, Shanghai Ouku or Lanting Gaochuang may materially and adversely affect our business, financial condition and results of operations.

Contractual arrangements with Lanting Huitong or Lanting Gaochuang may result in adverse tax consequences.

Under PRC laws and regulations, an arrangement or transaction among related parties may be subject to audit or challenge by the PRC tax authorities within ten years after the taxable year when the arrangement or transaction takes place. If this occurs, the PRC tax authorities could request that Lanting Huitong or Lanting Gaochuang adjust their taxable income in the form of a transfer pricing adjustment for PRC tax purposes if contractual arrangements among related parties do not represent arm s length prices. Such a pricing adjustment could adversely affect us by increasing Lanting Huitong or Lanting Gaochuang s tax expenses without a corresponding reduction in our tax expenses, which, in turn, could subject Lanting Huitong or Lanting Gaochuang to late payment fees and other penalties for underpayment of taxes. As a result, our contractual arrangements with Lanting Huitong or Lanting Gaochuang may result in adverse tax consequences to us. In 2016, Lanting Huitong did not generate net income from the contractual arrangements with our PRC subsidiary and therefore was not subject to PRC income tax. If the PRC tax authorities decide to make transfer pricing adjustments on Lanting Huitong s net income in the future, our results of operations may be adversely affected. In addition, if Lanting Huitong or Lanting Gaochuang generate net income from transactions with our PRC subsidiary under the contractual arrangements in the future and the PRC tax authorities decide to make transfer pricing adjustments on their net incomes, our consolidated net income may be adversely affected.

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Risks Related to Doing Business in China

We may be adversely affected by the uncertainties and changes in the PRC regulations and policies of cross- border business activities.

We are a China-based global online retailer. The PRC government extensively regulates the Internet industry and cross-border business activities. While the PRC government has been encouraging the export industry, such policy may change in the future. Currently laws and regulations relating to online retail, including export online retail, are still evolving and the interpretation and enforcement of these laws and regulations are subject to significant uncertainties. As a result, in certain circumstances, it may be difficult to determine what actions or omissions may be deemed to be in violation of applicable laws or regulations. Issues, risks and uncertainties relating to PRC regulation of export online retail include, but are not limited to:

- how our online retail activities are subject to the laws and regulations pertaining to traditional cross-border transactions or international trade, especially those related to customs declarations, statutory inspections, couriers and commodities export payments; and

- new regulations, or new interpretations of existing regulations, requiring additional licenses, declarations or inspections for our products.

The varying interpretations and applications of existing PRC laws, regulations and policies, along with possible new laws, regulations or policies relating to cross-border online retail, create substantial uncertainty regarding the licenses, customs declarations and inspections that may be required for our products. We cannot guarantee that all of the licenses, customs clearances and/or approvals for commodity inspections currently required, or in the future may be required, will be obtained.

For example, we work with third-party couriers to ship and export merchandise purchased by our customers around the world as articles or product samples on a parcel-by-parcel basis in accordance with procedures applicable to articles or product samples. This differs from the customs declaration, clearance and inspection procedures for traditional large-scale export shipments. Despite that the current PRC regulatory regime on customs declaration and inspection being formulated, interpreted and enforced primarily with the regulation of traditional large-scale exports in mind, the regulatory regime could technically be interpreted as being applicable to the shipment of merchandise on a parcel-by-parcel basis.

If the relevant PRC governmental authorities determine that we or our sourcing agents, suppliers or third-party couriers do not comply with the applicable laws and regulations, they could:

- require us, or our sourcing agents, suppliers or third-party couriers, to restructure business operations, including a possible change to our current method and manner of contracting with such sourcing agents, suppliers or

third-party couriers, or require us or third-party couriers to go through customs declaration, clearance and inspection procedures for the merchandise sold to our customer under our business arrangements in accordance with procedures for goods rather than for articles;

- impose fines or confiscate income from our PRC subsidiary or the operations of the affiliates of our sourcing agents, suppliers or third-party couriers that are subject to PRC jurisdiction; and

- impose additional conditions or requirements with which we may not be able to comply or take other regulatory or enforcement actions against us.

Substantial uncertainties exist with respect to the interpretation and implementation of Cyber Security Law as well as any impact it may have on our business operations.

On July 1, 2015, the Standing Committee of the National People s Congress issued the National Security Law, which came into effect on the same day. The National Security Law provides that the state shall safeguard its sovereignty, security and cybersecurity development interests, and that the government shall establish a national security review and supervision system to review, among other things, foreign investment, key technologies, internet and information technology products and services, and other important activities that are likely to impact the national security of China.

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On November 7, 2016, the Standing Committee of the National People s Congress issued the Cyber Security Law, which will come into effect on June 1, 2017. This is the first Chinese law that focuses exclusively on cyber security. The Cyber Security Law provides that network operators must set up internal security management systems that meets the requirements of a classified protection system for cybersecurity, including appointing dedicated cybersecurity personnel, taking technical measures to prevent computer viruses, network attacks and intrusions, taking technical measures to monitor and record network operation status and cybersecurity incidents, and taking data security measures such as data classification, backups and encryption. The Cyber Security Law also imposes a relatively vague but broad obligation to provide technical support and assistance to the public and state security authorities in connection with criminal investigations or for reasons of national security. The Cyber Security Law also requires network operators that provide network access or domain name registration services, landline or mobile phone network access, or that provide users with information publication or instant messaging services, to require users to provide a real identity when they sign up.

The Cyber Security Law sets high requirements for the operational security of facilities deemed to be part of the PRC s key information infrastructure. These requirements include data localization, i.e., storing personal information and important business data in China, and national security review requirements for any network products or services that may have an impact on national security. Among other factors, key information infrastructure is defined as critical information infrastructure, that will, in the event of destruction, loss of function or data leak, result in serious damage to national security, the national economy and people s livelihood, or the public interest. Specific reference is made to key sectors such as public communication and information services, energy, transportation, water-resources, finance, public service and e-government. A prior draft of the Cyber Security Law included reference to any networks with a large number of users, but this language was deleted in the final version of the law.

We do not believe that we are an operator of key information infrastructure as defined in the Cyber Security Law. However, there is no assurance that we may not be considered an operator of key information infrastructure in the future as the definition is not precise, and there are substantial uncertainties as to the law s ultimate interpretation and implementation of the Cyber Security Law. The Cyber Security Law, if enacted as proposed, could cause us to incur substantial costs or require us to change our business practices in a manner materially adverse to our business.

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 products, services, news, information, audio-video programs and other content through the Internet. In the past, the PRC government has prohibited the distribution of information through the Internet that it deems to be in violation of PRC laws and regulations. If any of our Internet content were deemed by the PRC government to violate any 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 consumers or users of our websites 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, which would materially and adversely affect our business, financial condition and results of operations.

Changes in China s political, economic or social conditions or government policies could have a material adverse effect on our business and operations.

Most of our suppliers and some of our business operations are located in China. Our business, financial condition, results of operations and prospects may be influenced by political, economic and social conditions in China generally and by continued economic growth in China as a whole.

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The Chinese economy differs from the economies of most developed countries in many respects, including the level of government involvement, level of development, growth rate, control of foreign exchange and allocation of resources. Although the PRC government has implemented measures since the late 1970s emphasizing the utilization of market forces for economic reform, the reduction of state ownership of productive assets and the establishment of improved corporate governance in business enterprises, a substantial portion of productive assets in China is still owned by the Chinese government. In addition, the PRC government continues to play a significant role in regulating industry development by imposing industry policies. The Chinese government also exercises significant control over China s economic growth through allocating resources, controlling payment of foreign currency-denominated obligations, setting monetary policy and providing preferential treatment to particular industries or companies. From 2003 to mid-2008, the PRC government implemented a number of measures, such as increasing the deposit reserve ratio requirements for banks and imposing commercial bank lending guidelines, designed to slow the growth of the PRC economy. In response to the global financial crisis, in 2008, the PRC government began instituting policies aimed at expanding credit and stimulating the economy, including an announced RMB4.0 trillion stimulus spending program. More recently, as the PRC economy has shown signs of recovering quickly from the global financial crisis, the PRC government has again begun implementing policies aimed at slowing the PRC economy, including raising interest rates and tightening fiscal expenditures.

While the PRC economy has experienced significant growth over the past decades, growth has been uneven, both geographically and among various sectors of the economy. The PRC government has implemented various measures to encourage economic growth and guide the allocation of resources. Some of these measures benefit the overall Chinese economy, but 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. In addition, in the past the PRC government has implemented certain measures, including interest rate increases, to control the pace of economic growth. These measures may increase the costs of business activities for us and our suppliers in China and adversely affect our business, financial condition and results of operations.

In addition, China s social and political conditions are not as stable as those of the United States and other developed countries. Any sudden changes in China s political system, the occurrence of widespread social unrest, or a significant deterioration in its relations with its neighbors could negatively affect the Chinese economy and our business.

Uncertainties with respect to the Chinese legal system could adversely affect us.

The PRC legal system is based on written statutes. Unlike under common law systems, decided legal cases have little value as precedents in subsequent legal proceedings. In 1979, the PRC government began to promulgate a comprehensive system of laws and regulations governing economic matters in general and forms of foreign investment (including in respect of wholly foreign owned enterprises) in particular. These laws, regulations and legal requirements are relatively new and are often changing, and their interpretation and enforcement depend to a large extent on relevant government policy and involve significant uncertainties that could limit the reliability of the legal protections available to us. We cannot predict the effects of future developments in government policy or the PRC legal system in general. We may be required in the future to procure additional permits, authorizations and approvals for our existing and future operations, which may not be obtainable in a timely fashion or at all, or may involve substantial costs and unforeseen risks. An inability to obtain, or the incurrence of substantial costs in obtaining, such permits, authorizations and approvals may have a material adverse effect on our business, financial condition and results of operations.

We may be adversely affected by the complexity and uncertainties of and changes in PRC regulation of Internet business and related companies.

The PRC government extensively regulates the Internet industry, including with respect to foreign ownership of and licensing and permit requirements pertaining to companies in the Internet industry. These Internet-related laws and regulations are relatively new and evolving and their interpretation and enforcement involve significant uncertainties. As a result, in certain circumstances, it may be difficult to determine what actions or omissions may be deemed to be in violation of applicable laws and regulations. Issues, risks and uncertainties relating to PRC regulation of Internet businesses include, but are not limited to:

- have contractual control over our websites that target consumers in China as compared to legal title over our websites that target consumers outside of China. Due to restrictions on foreign investment in businesses providing value-added telecommunication services in China, including Internet content provision services, we do not own *www.ouku.com*, *www.kuailebox.com* and other affiliated websites which target consumers in China. This may significantly disrupt our business, subject us to sanctions, compromise enforceability of related contractual arrangements, or have other harmful effects on us.

- there are uncertainties relating to the regulation of Internet businesses in China, including evolving licensing practices. This means that permits, licenses or operations at some of our companies may be subject to challenge, or we may fail to obtain permits or licenses that may be deemed necessary for our operations, or we may not be able to obtain or renew certain permits or licenses.

- the evolving PRC regulatory system for the Internet industry may lead to the establishment of new regulatory agencies. For example, the Cyberspace Administration of China was established in 2014, as the central Internet censorship, oversight and control agency for the PRC. Further, new laws, regulations or policies may be promulgated or announced that will regulate Internet activities, including the online video and online advertising businesses. If these new laws, regulations or policies are promulgated, additional licenses may be required for our operations. If our operations do not comply with these new regulations after they become effective, or if we fail to obtain any licenses required under these new laws and regulations, we could be subject to penalties.

The interpretation and application of existing PRC laws, regulations and policies and possible new laws, regulations or policies relating to the Internet industry have created substantial uncertainties regarding the legality of existing and future foreign investments in and the businesses and activities of, Internet businesses in China, including our business. We cannot assure you that we have obtained all the permits or licenses required for conducting our business in China or will be able to maintain our existing licenses or obtain any new licenses required under any new laws or regulations. There are also risks that we may be found to violate the existing or future laws and regulations given the uncertainty and complexity of China s regulation of Internet business.

Fluctuations in the value of the Renminbi may have a material adverse effect on your investment.

Most of our revenues are denominated in U.S. dollars while certain expenses are denominated in Renminbi. As a result, there are certain mismatches between our revenues in U.S. dollars and costs denominated in Renminbi. In addition, most of our suppliers are based in China and their operating costs are denominated in Renminbi. If the Renminbi appreciates relative to the U.S. dollar, the cost of our products will become more expensive in U.S. dollar terms, the currency in which we price our products. We have no hedges against currency risk. Consequently, any increase in the value of the Renminbi against the U.S. dollar may reduce our margins, reduce our competiveness against retailers who source their products from suppliers with costs denominated in U.S. dollars or other currencies or render us unable to meet our costs.

The value of the Renminbi against the U.S. dollar and other currencies may fluctuate and is affected by, among other things, changes in political and economic conditions and the foreign exchange policy adopted by the PRC government. On July 21, 2005, the PRC government changed its

policy of pegging the value of the Renminbi to the U.S. dollar. Under the current policy, the Renminbi is permitted to fluctuate within a narrow and managed band against a basket of certain foreign currencies. Following the removal of the U.S. dollar peg, the Renminbi appreciated more than 20% against the U.S. dollar over the following three years. During the period between July 2008 and June 2010, the Renminbi has traded stably within a narrow range against the U.S. dollar. Since June 2010, the Renminbi has appreciated further against the U.S. dollar, though there have been periods, especially during 2014, when the U.S. dollar has appreciated against the Renminbi as well. Since August 2015, the U.S. dollar has also started to gradually appreciate against the Renminbi. It is difficult to predict how market forces or PRC or U.S. government policy may impact the exchange rate between the Renminbi and the U.S. dollar in the future.

There remains significant international pressure on the PRC government to adopt an even more flexible currency policy, which could result in a further and more significant appreciation of the Renminbi against foreign currencies. Any significant fluctuations in the exchange rate between the Renminbi and the U.S. dollar may materially and adversely affect our cash flows, revenues, earnings and financial position and the amount of and any dividends we may pay on the ADSs in U.S. dollars. Any fluctuations in the exchange rate between the Renminbi and the U.S. dollar could also result in foreign currency translation losses for financial reporting purposes.

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PRC regulations relating to the establishment of offshore special purpose companies by PRC domestic residents and registration requirements for employee stock ownership plans or share option plans may subject our PRC resident beneficial owners or the plan participants to personal liability, limit our ability to inject capital into our PRC subsidiary, limit our PRC subsidiary s ability to increase their registered capital or distribute profits to us, or may otherwise adversely affect us.

On July 4, 2014, SAFE promulgated the Notice on Relevant Issues Concerning Foreign Exchange Control of Domestic Residents Overseas Investment and Financing and Roundtrip Investment through Offshore Special Purpose Vehicles, or SAFE Circular No. 37, which replaced the former Notice on Relevant Issues Concerning Foreign Exchange Administration for PRC Residents to Engage in Financing and Inbound Investment via Overseas Special Purpose Vehicles (generally known as SAFE Circular No. 75) promulgated by SAFE on October 21, 2005.

SAFE Circular No. 37 requires PRC residents to register with local branches of SAFE in connection with their direct establishment or indirect control of an offshore entity, for the purpose of overseas investment and financing, with such PRC residents legally owned assets or equity interests in domestic enterprises or offshore assets or interests, which is referred to in SAFE Circular No. 37 as a special purpose vehicle. SAFE Circular No. 37 further requires amendment to the registration in the event of any significant changes with respect to the special purpose vehicle, such as an increase or decrease of capital contributed by PRC residents, share transfer or exchange, merger, division or other material events. In the event that a PRC resident holding interests in a special purpose vehicle fails to complete the required SAFE registration, the PRC subsidiaries of that special purpose vehicle may be prohibited from making profit distributions to the offshore parent and from carrying out subsequent cross-border foreign exchange activities and the special purpose vehicle may be restricted in its ability to contribute additional capital into its PRC subsidiaries. Furthermore, failure to comply with the various SAFE registration requirements described above could result in liability under PRC law for evasion of foreign exchange controls.

We have requested PRC residents that, to our knowledge, hold direct or indirect interest in our company to make the necessary applications, filings and amendments as required under the SAFE regulations. Mr. Quji (Alan) Guo, Mr. Xin (Kevin) Wen and Mr. Liang Zhang, all of whom are PRC domestic residents and hold interests in our company, have registered with the Shenzhen SAFE branch.

We may not be fully informed of the identities of all of our beneficial owners who are PRC residents, we do not have control over our beneficial owners and we cannot provide any assurances that all of our shareholders who are PRC residents will make or obtain any applicable registrations or approvals required by these SAFE regulations. The failure or inability of our PRC resident shareholders and beneficial owners to comply with the registration procedures set forth above may subject us to fines and legal sanctions, restrict our cross-border investment activities or limit our PRC subsidiary s ability to distribute dividends or obtain foreign-exchange-denominated loans for our company.

As it is uncertain how the SAFE regulations will be interpreted or implemented, we cannot predict how these regulations will affect our business operations or future strategy. For example, we may be subject to more stringent review and approval processes with respect to our foreign exchange activities, such as remittance of dividends and foreign-currency-denominated borrowings, which may adversely affect our results of operations and financial condition. In addition, if we decide to acquire a PRC company, we or the owners of such company will be able to obtain the necessary approvals or complete the necessary filings and registrations required by the SAFE regulations. This may restrict our ability to acquire PRC companies and could adversely affect our business and prospects.

In December 2006, the People s Bank of China promulgated the Implementation Rules of the Administrative Measures for Individual Foreign Exchange, or the Individual Foreign Exchange Rules, setting forth the respective requirements for foreign exchange transactions by PRC individuals under either the current account or the capital account. In January 2007, the SAFE issued implementing rules for the Individual Foreign Exchange Rules, which, among other things, specified approval requirements for certain capital account transactions, such as a PRC

citizen s participation in the employee stock ownership plans or stock option plans of an overseas publicly-listed company. On March 28, 2007, the SAFE promulgated the Application Procedure of Foreign Exchange Administration for Domestic Individuals Participating in Employee Stock Holding Plan or Stock Option Plan of Overseas-Listed Company, or the Stock Option Rule. In February 2012, the SAFE promulgated the Notice on the Administration of Foreign Exchange Matters for Domestic Individuals Participating in the Stock Incentive Plans of Overseas Listed Companies, or the Stock Option Notice. This Stock Option Notice replaced the previous Stock Option Rules. The Stock Option Notice simplifies the requirements and procedures for the registration of stock incentive plan participants, especially with respect to the required application documents and the absence of strict requirements on offshore and onshore custodian banks that were stipulated in the Stock Option Rules. Under the Stock Option Notice, PRC resident individuals who are granted stock options by an overseas publicly-listed company are required, through a PRC agent or PRC subsidiary of such overseas publicly-listed company, to register with the SAFE and complete certain other procedures. As a public company listed in the United States, we and our PRC employees who have been granted stock options are subject to the Stock Option Notice. If we or our PRC optionees fail to comply with these regulations, we or our PRC optionees may be subject to fines and legal sanctions. See Item 4. Information on the Company B. Business Overview Regulation Regulations on Employee Stock Option Plans.

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PRC regulation of loans and direct investment by offshore holding companies to PRC entities may delay or prevent us from using the proceeds of our initial public offering and private placements to make loans or additional capital contributions to our PRC subsidiary.

In utilizing the proceeds of our initial public offering and private placements, as an offshore holding company of our PRC operating subsidiary, we may make loans or additional capital contributions to our PRC subsidiary. Any loans to our PRC subsidiary, which is a FIE, cannot exceed statutory limits, being the difference between the registered capital and the investment amount of the PRC subsidiary as approved by the MOFCOM or its local branches and must be approved by and registered with the SAFE or its local branches. In addition, our PRC subsidiary is required to pay withholding tax at the rate of 10% (or a maximum of 7% if the interest is paid to a Hong Kong resident) on our behalf on any interest paid under such shareholder loan. See Item 4. Information on the Company B. Business Overview Regulation Regulations Relating to Foreign Currency Exchange Foreign Exchange Relating to FIEs.

We may also decide to finance our PRC subsidiary by means of capital contributions. According to the relevant PRC regulations on FIEs in China, depending on the nature of the business conducted by the relevant subsidiary, capital contributions to FIEs in China are subject to approval by the MOFCOM or its local branches. We may not obtain these government approvals or registrations on a timely basis, if at all, with respect to future loans and capital contributions by us to our PRC subsidiary. If we fail to receive such approvals or registrations, our ability to use the proceeds of our initial public offering and private placements and to capitalize our PRC operations may be negatively affected, which could adversely affect our liquidity and our ability to fund and expand our business.

On August 29, 2008, the SAFE promulgated the Circular on the Relevant Operating Issues Concerning the Improvement of the Administration of the Payment and Settlement of Foreign Currency Capital of Foreign-Invested Enterprises, or SAFE Circular 142, regulating the conversion by a FIE of foreign currency registered capital into Renminbi by restricting how the converted Renminbi may be used. SAFE Circular 142 provides that the Renminbi capital converted from foreign currency registered capital of a FIE may only be used for purposes within the business scope approved by the applicable governmental authority and unless otherwise provided by law, such Renminbi capital may not be used for equity investments within the PRC. In addition, the SAFE strengthened its oversight of the flow and use of the Renminbi capital converted from foreign currency registered capital of a foreign-invested company. The use of such Renminbi capital may not be altered without the SAFE s approval and such Renminbi capital may not in any case be used to repay Renminbi loans if the proceeds of such loans have not been used. Violations of SAFE Circular 142 could result in severe monetary or other penalties. We expect that if we convert the net proceeds we receive from our initial public offering into Renminbi, our use of Renminbi funds will be for purposes within the approved business scope of our PRC subsidiary in compliance with SAFE Circular 142. However, we may not be able to use such Renminbi funds to make equity investments in the PRC through our PRC subsidiary.

Furthermore, the SAFE promulgated the Notice on Relevant Issues Concerning Strengthening the Administration of Foreign Exchange Business, or Circular 59, on November 19, 2010, which requires the government to closely examine the authenticity of settlement of net proceeds from offshore offerings and the net proceeds to be settled in the manner described in the offering documents. Circular 142 and Circular 59 may significantly limit our ability to transfer the net proceeds from our initial public offering to Lanting Jishi (as defined below) and our VIEs and convert such net proceeds into Renminbi, which may adversely affect our liquidity and our ability to fund and expand our business in the PRC.

We may be deemed a PRC resident enterprise under the New EIT Law and be subject to PRC taxation on our income.

Under the Enterprise Income Tax Law of the PRC, or the New EIT Law, which was issued in 2007 and amended in 2017, and its implementation rules which was issued in 2007, 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 State Administration of Taxation, or 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. Further to Circular 82, on July 27, 2011, the SAT issued the Administrative Measures of Enterprise Income Tax of Chinese- controlled Offshore Incorporated Resident Enterprises (Trial), or Bulletin No. 45, which took effect on September 1, 2011, to provide more guidance on the implementation of Circular 82. See Item 4. Information on the Company B. Business Overview Regulation Regulations on Tax PRC Enterprise Income Tax.

According to Circular 82, a Chinese-controlled offshore-incorporated enterprise will be regarded as a PRC tax resident by virtue of having a de facto management body in China and will be subject to PRC enterprise income tax on its worldwide income only if all of the following conditions set forth in Circular 82 are met: (i) the primary location of the day-to-day operational management is in the PRC; (ii) decisions relating to the enterprise s financial and human resource matters are made or are subject to approval by organizations or personnel in the PRC; (iii) the enterprise s primary assets, accounting books and records, company seals and board and shareholder resolutions are located or maintained in the PRC; and (iv) at least 50% of voting board members or senior executives habitually reside in the PRC. In addition, Bulletin No. 45 provides clarification on the resident status determination, post-determination administration and competent tax authorities. It also specifies that when provided with a copy of a PRC resident determination certificate from a resident Chinese-controlled offshore- incorporated enterprise, the payer should not withhold 10% income tax when paying certain Chinese- sourced income such as dividends, interest and royalties to the PRC-controlled offshore-incorporated enterprise.

Although both the circular and the bulletin only apply to offshore enterprises controlled by PRC enterprises and not those by PRC individuals, the determination criteria set forth in the circular and administration clarification made in 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 the administration measures should be implemented, 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 or meet all of the conditions above, it is possible that the PRC tax authorities could reach a different conclusion. In such case, we may be considered a resident enterprise and

may therefore be subject to enterprise income tax at a rate of 25% on our global income. If we are considered a resident enterprise and earn income other than dividends from our PRC subsidiary, a 25% enterprise income tax on our global income could significantly increase our tax burden and materially and adversely affect our cash flow and profitability.

Pursuant to the New EIT Law and its implementation rules, dividends generated after January 1, 2008 and payable by a FIE in China to its foreign investors, which are non-PRC tax resident enterprises without an establishment in China, or whose income has no connection with their institutions and establishments inside China, are subject to withholding tax at a rate of 10%, unless any such foreign investor s jurisdiction of incorporation has a tax treaty with China that provides for a different withholding arrangement. We are a Cayman Islands holding company and we plan to conduct substantially all of our business in China through Lanting Jishi, which is 100% owned by Light In the Box Limited, our wholly owned subsidiary located in Hong Kong. According to the Mainland and Hong Kong Special Administrative Region Arrangements on the Avoidance of Double Taxation and the Prevention of Fiscal Evasion with Respect to Taxes on Income, or the Double Taxation Avoidance Arrangement, dividends that Light In The Box Limited receives from Lanting Jishi may be subject to withholding tax at a rate of 5%, provided that: (a) Light In The Box Limited is determined by the relevant PRC tax authorities to be a non-resident enterprise under the New EIT Law; (b) Light In The Box Limited is the beneficial owner of the PRC sourced income; (c) Light In The Box Limited holds at least 25% of the equity interest of Lanting Jishi and (d) all other conditions and requirements under the Double Taxation Avoidance Arrangement shall be satisfied. Light In The Box Limited has not obtained the approval for a withholding tax rate of 5% from the local tax authority and does not plan to obtain such approval in the near future, as Lanting Jishi has not paid dividends in the past and does not plan to pay dividends in the future as it may continue to incur losses. In addition, as described above, our company or our Hong Kong subsidiary may be considered a PRC resident enterprise for PRC enterprise income tax purposes, in which case dividends received by it, as the case may be, from our PRC subsidiary would be exempt from the PRC withholding tax because such income is exempt under the New EIT Law for a PRC resident enterprise recipient.

As uncertainties remain regarding the interpretation and implementation of the New EIT Law and its implementation rules, we cannot assure you that if we are regarded as a PRC resident enterprise, any dividends to be distributed by us to our non-resident enterprise shareholders and ADS holders would not be subject to any PRC withholding tax at a rate of up to 10%. Similarly, any gain recognized by such non-resident enterprise shareholders or ADS holders on the sale of shares or ADSs, as applicable, may also be subject to PRC withholding tax. Furthermore, if we are considered a PRC resident enterprise and the competent PRC tax authorities consider dividends we pay with respect to our shares or ADSs and the gains realized from the transfer of our shares or ADSs to be income derived from sources within the PRC, such dividends and gains earned by non-resident individuals may be subject to PRC individual income tax at a rate of 20%, unless any such non-resident individuals jurisdiction has a tax treaty with China that provides for a preferential tax rate or a tax exemption. It is also unclear whether, if we are considered a PRC resident enterprise, holders of our shares or ADSs would be able to claim the benefit of income tax treaties or agreements entered into between China and other countries or areas. If we are required under PRC law to withhold PRC income tax on our dividends payable to our non-PRC shareholders and ADS holders, or the PRC authorities tax gain recognized by such non-PRC shareholders or ADS holders, such investors investment in our ordinary shares or ADSs may be materially and adversely affected.

The labor contract law and its implementation regulations may increase our operating expenses and may materially and adversely affect our business, financial condition and results of operations.

As the PRC Labor Contract Law, or Labor Contract Law, and the Implementation Regulation for the PRC Labor Contract Law, or Implementation Regulation, have been enforced for only a relatively short period of time, the interpretation and implementation of these laws and regulations are still evolving, substantial uncertainty remains as to its potential impact on our business, financial condition and results of operations. See Item 4. Information on the Company B. Business Overview Regulation Labor Laws and Social Insurance. The implementation of the Labor Contract Law and the Implementation Regulation may increase our operating expenses, in particular our human resources costs and our administrative expenses.

In addition, as the interpretation and implementation of these regulations are still evolving, we cannot assure you that our employment practices will at all times be deemed to be in full compliance with the law. In the event that we decide to significantly modify our employment or labor policy or practice, or reduce the number of our sales professionals, the labor contract law may limit our ability to effectuate the modifications or changes in the manner that we believe to be most cost-efficient or otherwise desirable, which could materially and adversely affect our business, financial condition and results of operations. If we are subject to severe penalties or incur significant liabilities in connection with labor disputes or investigations, our business and results of operations may be adversely affected. In the event that we decide to significantly modify our employment or labor policy or practice, or reduce the number of our sales professionals, the labor contract law may limit our ability to effectuate the modifications or changes in the manner that we believe to be most cost-efficient or otherwise desirable, which could materially and adversely affect our business, financial condition and results of operations.

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PRC labor-related laws and individual income tax obligations expose us to potential penalty risks.

Companies operating in China are generally required to contribute to the mandatory social insurance and housing funds. Lanting Jishi, Lanting Huitong and Shanghai Ouku have not fully contributed to the employee benefit plans as required by applicable PRC regulations. While we believe we have made adequate provisions for any payments due on our audited consolidated financial statements, our prior failure to make payments may constitute a violation of the applicable PRC regulations and, as of December 31, 2016, we were potentially subject to late fees, fines and penalties for up to a maximum of $33.0 million related to employee benefit plans. In addition, we have previously not withheld appropriate amounts of individual income taxes as required by applicable PRC regulations. However, such amounts were substantially paid by us on a voluntary basis in March 2013 to the relevant tax authority. Although as of the date of this annual report, no action has been initiated by the relevant authorities against us, future fines or levies may materially and adversely affect our results of operations and financial condition.

Failure to obtain prior approval required under the M&A Rules and/or any other regulations promulgated by relevant PRC regulatory agencies in the future could have a material adverse effect on our business, financial condition and results of operations as well as the trading price of the ADSs.

On August 8, 2006, six PRC regulatory agencies, including the Ministry of Commerce, the State- Owned Assets Supervision and Administration Commission, the SAT, the State Administration of Industry and Commerce, or the SAIC, the China Securities Regulatory Commission, or the CSRC, and the SAFE, jointly adopted the Regulations on Mergers and Acquisitions of Domestic Enterprises by Foreign Investors, or the M&A Rules, which came into effect on September 8, 2006 and was amended on June 22, 2009. The M&A Rules, among other things, include provisions that purport to require that an offshore special purpose vehicle formed for the purpose of an overseas listing of a PRC company obtain the approval of the CSRC prior to the listing and trading of such special purpose vehicle s securities on an overseas stock exchange. On September 21, 2006, the CSRC published on its official website procedures regarding its approval of overseas listings by special purpose vehicles. However, substantial uncertainty remains regarding the scope and applicability of the M&A Rules to offshore special purpose vehicles.

The application of the M&A Rules with respect to our initial public offering and our corporate structure established under contractual arrangements remains unclear. Our PRC counsel, TransAsia Lawyers, has advised us that we were not required to apply to the relevant PRC regulatory agencies, including the CSRC and the Ministry of Commerce, for approval of our initial public offering or our current corporate structure because:

- the CSRC currently has not issued any definitive rule or interpretation concerning whether international public offerings like ours under our prospectus are subject to this regulation;

- we established our PRC subsidiary by means of direct investment rather than by merger or acquisition of the equity or assets of PRC domestic companies; and

- no provision in this regulation clearly classified contractual arrangements as a type of transaction subject to its regulation.

However, we cannot assure you that relevant PRC government agencies, including the CSRC, would reach the same conclusion as our PRC counsel. If prior approval is required but not obtained, we may face regulatory actions or other sanctions from the CSRC or other PRC regulatory agencies. These regulatory agencies may impose fines and penalties on our operations in China, limit our operating privileges in China, delay or restrict the repatriation of the proceeds from our initial public offering into China or take other actions that could have a material adverse effect on our business, financial condition, results of operations and prospects, as well as the trading price of the ADSs. In addition, if the CSRC or other regulatory agencies later promulgate new rules or explanations requiring that we obtain their approvals for our initial public offering, we may be unable to obtain a waiver of such approval requirements, if and when procedures are established to obtain such a waiver. Any uncertainties and/or negative publicity regarding such approval requirement could have a material adverse effect on the trading price of the ADSs.

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We may rely on dividends and other cash distributions on equity paid by our subsidiaries to fund future cash and financing requirements we may have, and any limitation on the ability of our subsidiaries to make payments to us could have a material adverse effect on our ability to conduct our businesses.

We are a holding company, and we may rely on dividends and cash distributed by our Hong Kong subsidiary and may, in the future, rely on dividends and cash distributed by our PRC subsidiary through our Hong Kong subsidiary for our cash requirements. However, current PRC regulations permit our PRC subsidiary to pay dividends only out of its accumulated profits, if any, determined in accordance with Chinese accounting standards and regulations. In addition, under applicable PRC laws, rules and regulations, our PRC subsidiary is required to set aside at least 10% of its accumulated after-tax profits each year, if any, to fund certain statutory reserves until the accumulative amount of such reserves reaches 50% of the respective subsidiary s registered capital. These reserves are not distributable as cash dividends. Furthermore, if our PRC subsidiary incurs debt on its own behalf in the future, the instruments governing the debt may restrict their ability to pay dividends or make other payments to us or our Hong Kong subsidiary. If we or our Hong Kong subsidiary require dividends and cash contributions from our PRC subsidiary in the future, any limitation on the ability of our PRC subsidiary to distribute dividends or other payments to us or our Hong Kong subsidiary could materially and adversely limit our ability to grow, make investments or acquisitions that could be beneficial to our businesses, pay dividends, or otherwise fund and conduct our businesses.

The audit report included in this annual report is prepared by auditors who are not inspected by the Public Company Accounting Oversight Board and, as such, you are deprived of the benefits of such inspection.

Our independent registered public accounting firm that issues the audit reports included in this annual report, as auditors of companies that are traded publicly in the United States and a firm registered with the US Public Company Accounting Oversight Board (United States), or the PCAOB, is required by the laws of the United States to undergo regular inspections by the PCAOB to assess its compliance with the laws of the United States and professional standards. Because our auditors are located in the Peoples Republic of China, a jurisdiction where the PCAOB is currently unable to conduct inspections without the approval of the Chinese authorities, our auditors are not currently inspected by the PCAOB.

Inspections of other firms that the PCAOB has conducted outside China have identified deficiencies in those firms audit procedures and quality control procedures, which may be addressed as part of the inspection process to improve future audit quality. This lack of PCAOB inspections in China prevents the PCAOB from regularly evaluating our auditors audits and its quality control procedures. As a result, investors are deprived of the benefits of PCAOB inspections.

The inability of the PCAOB to conduct inspections of auditors in China makes it more difficult to evaluate the effectiveness of our auditor s audit procedures or quality control procedures as compared to auditors outside of China that are subject to PCAOB inspections. Investors may lose confidence in our reported financial information and procedures and the quality of our financial statements.

If additional remedial measures are imposed on the big four PRC-based accounting firms, including our independent registered public accounting firm, in administrative proceedings brought by the SEC alleging the firms failure to meet specific criteria set by the SEC with respect to requests for the production of documents, we could be unable to timely file future financial statements in compliance with the requirements of the Exchange Act.

Starting in 2011 the Chinese affiliates of the big four accounting firms, (including our independent registered public accounting firm) were affected by a conflict between United States and Chinese law. Specifically, for certain listed companies in the United States operating and audited in mainland China, the SEC and the PCAOB sought to obtain from these Chinese accounting firms access to their audit work papers and related documents. These accounting firms were, however, advised and directed that under China law they could not respond directly to the United States regulators on those requests, and that requests by foreign regulators for access to such papers in China had to be channeled through the CSRC.

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In late 2012 the SEC commenced administrative proceedings under Rule 102(e) of its Rules of Practice and also under the Sarbanes-Oxley Act against the Chinese accounting firms (including our independent registered public accounting firm). In July 2013, the SEC s internal administrative court issued an adverse judgment against these firms and the administrative law judge s proposed penalties on the firms included a temporary suspension of their right to practice before the SEC, although that proposed penalty did not take effect pending review by the Commissioners of the SEC, or the Commissioners. On February 6, 2015, before a review by the Commissioner had taken place, these firms reached a settlement with the SEC. Under the settlement, the SEC accepts that future requests by the SEC for the production of documents will normally be made to the CSRC. These accounting firms will receive matching Section 106 requests, and are required to abide by a detailed set of procedures with respect to such requests, which in substance require them to facilitate production of documents via the CSRC. If they fail to meet specified criteria, the SEC retains authority to impose a variety of additional remedial measures on these accounting firms depending on the nature of the failure. Remedies for any future noncompliance could include, as appropriate, an automatic six-month bar on a single firm s performance of certain audit work, commencement of a new proceeding against a firm, or in extreme cases the resumption of the current proceeding against all four accounting firms.

In the event that the SEC restarts the administrative proceedings, depending upon the final outcome, listed companies in the United States with major PRC operations may find it difficult or impossible to retain auditors in respect of their operations in the PRC, which could result in financial statements being determined to not be in compliance with the requirements of the Exchange Act, including possible delisting. Moreover, any negative news about any such future proceedings against these accounting firms may cause investor uncertainty regarding China-based companies listed in the United States and the market price of our ADSs may be adversely affected.

If our independent registered public accounting firm were denied, even temporarily, the ability to practice before the SEC and we were unable to timely find another registered public accounting firm to audit and issue an opinion on our financial statements, our financial statements could be determined not to be in compliance with the requirements of the Exchange Act. Such a determination could ultimately lead to the delisting of our ordinary shares from the NYSE or deregistration with the SEC, or both, which would substantially reduce or effectively terminate the trading of our ADSs in the United States.

Risks Related to the ADS

The market price for the ADSs has fluctuated and may be volatile.

The market price for our ADSs has fluctuated since we listed our ADSs. Since our ADSs became listed on the NYSE on June 6, 2013, the trading price of our ADSs have ranged from US$1.95 to US$23.38 per ADS, and the last reported trading price on March 29, 2017 was US$2.74 per ADS. In addition to the volatility in the price of the ADSs which could be caused by the materialization of any of the risks described in this section, the securities markets in the United States, China and elsewhere have from time to time experienced significant price and volume fluctuations that are not related to the operating performance of particular companies. These market fluctuations may also materially and adversely affect the market price of our ADSs.

The securities of some China-based companies that have listed their securities in the United States have experienced significant volatility since their initial public offerings in recent years, including, in some cases, substantial declines in the trading prices of their securities. The trading performances of these companies securities after their offerings may affect the attitudes of investors towards Chinese companies listed in the United States in general, which consequently may impact the trading performance of our ADSs, regardless of our actual operating performance. In addition, any negative news or perceptions about inadequate corporate governance practices or fraudulent accounting, corporate structure or other matters of other Chinese companies may also negatively affect the attitudes of investors towards Chinese companies in general, including

us, regardless of whether we have engaged in any inappropriate activities. In particular, the global financial crisis and the ensuing economic recessions in many countries have contributed and may continue to contribute to extreme volatility in the global stock markets. These broad market and industry fluctuations may adversely affect the market price of our ADSs. Volatility in our ADS price may also adversely affect our ability to retain key employees, most of whom have been granted options or other equity incentives.

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Our voting structure limits your ability to influence matters related to change of control and could discourage others from pursuing any change of control transactions that holders of our common shares and ADSs may view as beneficial.

We have one class of ordinary shares, and each holder of our ordinary shares is entitled to one vote per share. However, in matters related to change of control, pursuant to our amended and restated memorandum and articles of association, certain founding shareholders, namely Wincore Holdings Limited, a British Virgin Islands company wholly owned by Mr. Quji (Alan) Guo, Vitz Holdings Limited, a British Virgin Islands company wholly owned by Mr. Xin (Kevin) Wen, and Clinet Investments Limited, a British Virgin Islands company wholly owned by Mr. Liang Zhang, are entitled to three votes per share in matters related to a change of control. As of March 24, 2017, each of Wincore Holdings Limited, Vitz Holdings Limited and Clinet Investments Limited held 5.2%, 2.6% and 1.9% of the shares of our company, respectively, entitling them to 13.1%, 6.5% and 4.7% of voting rights, respectively, and an aggregate of 24.3% of voting rights in such matters related to a change of control, assuming all the ADSs owned by such founding shareholders were converted into ordinary shares of the Company. This voting structure could limit your ability to influence matters related to change of control and could discourage others from pursuing any potential merger, takeover or other change of control transactions that you or other ordinary shareholders may view as beneficial.

We may need additional capital, and the sale of additional ADSs or other equity securities or incurrence of additional indebtedness could result in additional dilution to our shareholders or increase our debt service obligations.

Historically, we have relied principally on the issuance of our preferred shares, convertible notes and ADRs to fund our operations and capital expansion needs. We may require additional cash resources due to changed business conditions or other future developments, including any investments or acquisitions we may pursue. If our resources are insufficient to satisfy our cash requirements, we may seek to sell additional equity, equity- linked or debt securities or enter into a credit facility. The sale of additional equity securities could result in additional dilution to our shareholders. The incurrence of indebtedness would result in increased debt service obligations and could result in operating and financing covenants that would restrict our operations. It is uncertain whether financing will be available in amounts or on terms acceptable to us, if at all.

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

Additional sales of our ordinary shares in the public market, or the perception that these sales could occur, could cause the market price of the ADSs to decline. As of December 31, 2016, we had 137,820,605 ordinary shares outstanding, including 39,007,880 ordinary shares represented by ADSs. All our ordinary shares represented by ADSs were freely transferable by persons other than our affiliates without restriction or additional registration under the Securities Act of 1933, as amended, or Securities Act. The remaining ordinary shares will be available for sale subject to volume and other restrictions as applicable under Rules 144 and 701 under the Securities Act.

In addition, certain holders of our ordinary shares have the right to cause us to register the sale of those shares under the Securities Act. Registration of these shares under the Securities Act would result in these shares becoming freely tradable without restriction under the Securities Act immediately upon the effectiveness of the registration. Sales of these registered shares in the public market could cause the price of the ADSs to decline.

You may not have the same voting rights as the holders of our ordinary shares and may not receive voting materials in time to be able to exercise your right to vote.

Except as described in the deposit agreement, holders of the ADSs are not able to exercise voting rights attaching to the shares evidenced by the ADSs. You have a right to instruct the depositary how to exercise those voting rights. However, the depository or its nominee may not successfully comply with your instructions or intentions. You may not receive voting materials in time to instruct the depositary to vote, and it is possible that you, or persons who hold their ADSs through brokers, dealers or other third parties, will not have the opportunity to exercise a right to vote.

You may not be able to participate in rights offerings and may experience dilution of your holdings as a result.

We may from time to time distribute rights to our shareholders, including rights to acquire our securities. Under the deposit agreement for the ADSs, the depositary will not offer those rights to ADS holders unless both the rights and the underlying securities to be distributed to ADS holders are either registered under the Securities Act of 1933, as amended, or the Securities Act, or exempt from registration under the Securities Act with respect to all holders of ADSs. We are under no obligation to file a registration statement with respect to any such rights or underlying securities or to endeavor to cause such a registration statement to be declared effective. In addition, we may not be able to take advantage of any exemptions from registration under the Securities Act. Accordingly, holders of the ADSs may be unable to participate in our rights offerings and may experience dilution in their holdings as a result.

You may be subject to limitations on transfer of your ADSs.

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

You may face difficulties in protecting your interests and your ability to protect your rights through the U.S. federal courts may be limited, because we are incorporated under Cayman Islands law, primarily operate our business from mainland China and Hong Kong and a majority of our officers reside outside the United States.

We are incorporated in the Cayman Islands and primarily conduct our operations through our subsidiaries in Hong Kong and mainland China and through our VIEs, Lanting Huitong and its subsidiary, Shanghai Ouku, and Lanting Gaochuang, in China. Most of our directors and officers reside outside the United States and all or a substantial portion of their assets are located outside of the United States. As a result, it may be difficult or impossible for you to effect service of process within the United States upon us or these persons, or to bring an original action against us or against these individuals in a Cayman Islands or PRC court in the event that you believe that your rights have been infringed under the U.S. federal securities laws or otherwise. Even if you are successful in bringing an action of this kind, the laws of the Cayman Islands and of China may render you unable to enforce a judgment against our assets or the assets of our directors and officers. There is no statutory enforcement in the Cayman Islands of judgments obtained in the federal or state courts of the United States (and the Cayman Islands are not a party to any treaties for the reciprocal enforcement or recognition of such judgments), a judgment obtained in such jurisdiction will be recognized and enforced in the courts of the Cayman Islands at common law, without any re-examination of the merits of the underlying dispute, by an action commenced on the foreign judgment debt in the Grand Court of the Cayman Islands, provided such judgment (a) is given by a foreign court of competent jurisdiction, (b) imposes on the judgment debtor a liability to pay a liquidated sum for which the judgment has been given, (c) is final, (d) is not in respect of taxes, a fine or a penalty, and (e) was not obtained in a manner and is not of a kind the enforcement of which is contrary to natural justice or the public policy of the Cayman Islands. However, the Cayman Islands courts are unlikely to enforce a judgment obtained from the U.S. courts under civil liability provisions of the U.S. federal securities law if such judgment is determined by the courts of the Cayman Islands to give rise to obligations to make payments that are penal or punitive in nature. Because such a determination has not yet been made by a court of the Cayman Islands, it is uncertain whether such civil liability judgments from U.S. courts would be enforceable in the Cayman Islands.

Our corporate affairs are governed by our memorandum and articles of association, as amended and restated from time to time, and by the Companies Law (2016 Revision) and common law of the Cayman Islands. The rights of shareholders to take legal action against our directors and us, actions by minority shareholders and the fiduciary duties 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 duties of our directors under Cayman Islands law are not as clearly established as they would be under statutes or judicial precedents in the United States. In particular, the Cayman Islands have a less developed body of securities laws as compared to the United States, and provide significantly less protection to investors. In addition, shareholders of Cayman Islands companies may not have standing to initiate a shareholder derivative action before the federal courts of the United States. As a result, your ability to protect your interests if you are harmed in a manner that would otherwise enable you to sue in a United States federal court may be limited to direct shareholder lawsuits.

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As a result of all of the above, our public shareholders may have more difficulty in protecting their interests through actions against our management, directors or major shareholders than would shareholders of a corporation incorporated in a jurisdiction in the United States.

We are an emerging growth company and we cannot be certain if the reduced disclosure requirements applicable to emerging growth companies will make our ADSs less attractive to investors.

We are a foreign private issuer, as such term is defined in Rule 405 under the Securities Act, and are not required to comply with certain periodic disclosure and current reporting requirements of the Exchange Act. In addition, we are an emerging growth company, as defined in the Jumpstart Our Business Startups Act of 2012, and we may take advantage of certain exemptions from various reporting requirements that are applicable to other public companies that are not emerging growth companies including, but not limited to, not being required to comply with the auditor attestation requirements of Section 404 of the Sarbanes-Oxley Act of 2012 for up to five fiscal years after the date of our initial public offering. Section 404(b) of the Sarbanes-Oxley Act of 2002 requires our independent registered public accounting firm to attest to and report on the effectiveness of the internal control structure and procedures for financial reporting.

In addition, Section 107(b) of the Jumpstart Our Business Startups Act of 2012 provides that an emerging growth company can take advantage of the extended transition period provided in Section 7(a)(2)(B) of the Securities Act for complying with new or revised accounting standards. In other words, an emerging growth company can delay the adoption of certain accounting standards until those standards would otherwise apply to private companies. We have elected to take advantage of the extended transition period. Although as of the date of this annual report, we have not delayed the adoption of any accounting standard, as a result of this election, our future financial statements may not be comparable to other public companies that comply with the public company effective dates for these new or revised accounting standards.

We will cease to be an emerging growth company upon the earliest of: (i) the last day of the fiscal year during which we have gross revenues of $1 billion or more, (ii) the last day of the fiscal year following the fifth anniversary of the date of our initial public offering, (iii) the date on which we have issued more than $1 billion in non-convertible debt during the previous three-year period, or (iv) when we become a large accelerated filer, as defined in Rule 12b-2 under the Exchange Act.

We have incurred increased costs as a result of becoming a public company, and our compliance costs may continue to increase in the future.

As a public company, we have incurred significant legal, accounting and other expenses that we did not have as a private company prior to our initial public offering. In addition, new rules and regulations relating to information disclosure, financial reporting and control and corporate governance, which could be adopted by the Securities and Exchange Commission, or the SEC, the New York Stock Exchange and other regulatory bodies and exchange entities from time to time, could result in a significant increase in legal, accounting and other compliance costs and to make certain corporate activities more time-consuming and costly, which could materially affect our business, financial condition and results of operations.

We have no present plan to pay dividends in the foreseeable future, and you may only rely on price appreciation of our ADSs for return on your investment.

Since our inception, we have not declared or paid any dividends on our ordinary shares. Since we intend to retain most, if not all, of our available funds and any future earnings to operate and expand our business, we have no present plan to pay any dividends on our ordinary shares in the foreseeable future. Therefore, you should not reply on an investment in our ADSs as a source for any future dividend income.

Any future determination to pay dividends will be made at the sole discretion of our board of directors and may be based on a number of factors, including our future operations and earnings, capital requirements and surplus, general financial condition, contractual restrictions and other factors that the board of directors may deem relevant. If we pay any dividends, we will pay the ADS holders to the same extent as holders of our ordinary shares, subject to the terms of the deposit agreement, including the fees and expenses payable thereunder. See Item 12. Description of Securities Other Than Equity Securities D . American Depositary Shares. Accordingly, the return on your investment in our ADSs will likely depend entirely upon any future price appreciation of our ADSs. There is no guarantee that our ADSs will appreciate in value or even maintain the price at which you purchased the ADSs. You may not realize a return on your investment in our ADSs and you may even lose your entire investment in our ADSs.

We may become a passive foreign investment company, or PFIC, which could result in adverse United States tax consequences to United States investors.

Based on the past and projected composition of our income and valuation of our assets, including goodwill, we do not believe that we were a passive foreign investment company (a PFIC) for 2016. The determination of whether or not we are a PFIC is made on an annual basis and will depend on the composition of our income and assets from time to time. Specifically, for any taxable year we will be classified as a PFIC for United States federal income tax purposes if either (i) 75% or more of our gross income in that taxable year is passive income or (ii) the average percentage of our assets by value in that taxable year which produce or are held for the production of passive income (which includes cash) is at least 50%. The calculation of the value of our assets will be based, in part, on the quarterly market value of our ordinary shares and ADSs, which is subject to change. Due to the volatility of the market price of our ADSs, we may become a PFIC in the future. See Item 10. Additional Information E. Taxation Material United States Federal Income Tax Considerations.

In addition, there is uncertainty as to the treatment of our corporate structure and ownership of our VIEs for United States federal income tax purposes. If it is determined that we do not own the stock of our VIEs for United States federal income tax purposes, we may be treated as a PFIC.

If we are a PFIC for any taxable year during which you hold the ADSs or ordinary shares, such characterization could result in adverse United States federal income tax consequences to you if you are a United States Holder, as defined under Item 10. Additional Information E. Taxation Material United States Federal Income Tax Considerations. For example, if we are or become a PFIC, you may become subject to increased tax liabilities under United States federal income tax laws and regulations, and will become subject to burdensome reporting requirements. See Item 10. Additional Information E. Taxation Material United States Federal Income Tax Considerations. We cannot assure you that we were not a PFIC for 2016 or that we will not be a PFIC for 2017 or any future taxable year. Moreover, the determination of our PFIC status is based on an annual determination that cannot be made until the close of a taxable year, and involves extensive factual investigation, including ascertaining the fair market value of all of our assets on a quarterly basis and the character of each item of income we earn, as discussed under Item 10. Additional Information E. Taxation Material United States Federal Income Tax Considerations Passive Foreign Investment Company. Our United States counsel expresses no opinion with respect to our PFIC status.

Our fourth amended and restated memorandum and articles of association contain anti-takeover provisions that could have a material adverse effect on the rights of holders of our ordinary shares and ADSs.

Our fourth amended and restated memorandum and articles of association contains provisions limiting the ability of others to acquire control of our company or cause us to engage in change-of-control transactions. These provisions could have the effect of depriving our shareholders of an opportunity to sell their shares at a premium over prevailing market prices by discouraging third parties from seeking to obtain control of our

company in a tender offer or similar transaction. For example, under our fourth amended and restated memorandum and articles of association, on a resolution relating to (a) a merger, amalgamation, consolidation or similar transaction involving our company, (b) the filing of a petition for a scheme of arrangement involving our company, or the giving of consent to such a filing or the co-operation by our company in the making of such filing, and (c) a sale, transfer or other disposition of all or substantially all of the assets of our company, Wincore Holdings Limited, a British Virgin Islands company wholly owned by Mr. Quji (Alan) Guo, Vitz Holdings Limited, a British Virgin Islands company wholly owned by Mr. Xin (Kevin) Wen, and Clinet Investments Limited, a British Virgin Islands company wholly owned by Mr. Liang Zhang, are entitled to three votes per share held by them, and the remaining shareholders are entitled to one vote per share held.

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Furthermore, our board of directors has the authority, without further action by our shareholders, to issue preferred shares in one or more series and to fix their designations, powers, preferences, privileges, and relative participating, optional or special rights and the qualifications, limitations or restrictions, including dividend rights, conversion rights, voting rights, terms of redemption and liquidation preferences, any or all of which may be greater than the rights associated with our ordinary shares, in the form of ADSs or otherwise. Preferred shares could be issued quickly with terms calculated to delay or prevent a change in control of our company or make removal of management more difficult. If our board of directors decides to issue preferred shares, the price of the ADSs may fall and the voting and other rights of the holders of our ordinary shares and ADSs may be materially and adversely affected.

ITEM 4. INFORMATION ON THE COMPANY

A. History and Development of the Company

We were founded in June 2007 by Mr. Quji (Alan) Guo, Mr. Xin (Kevin) Wen, Mr. Liang Zhang, Mr. Jun Liu and Mr. Chit Jeremy Chau. We operated our business at the time through Light In The Box Limited. In March 2008, we incorporated LightInTheBox Holding Co., Ltd., which, through a corporate restructuring, became our ultimate holding company.

We currently conduct our businesses primarily through the following wholly owned subsidiaries and affiliated entities:

- Light In The Box Limited, our wholly owned subsidiary incorporated in Hong Kong, that primarily engages in product sourcing, marketing and the operation of our websites and mobile applications and the sale of our products targeted towards consumers outside of China. In 2014, 2015 and 2016, we derived 99.7%, 96.6% and 89.6%, respectively, of our consolidated total net revenues from Light In The Box Limited;

- Lightinthebox Trading (Shenzhen) Co. Ltd., previously Lanting Jishi Trade (Shenzhen) Co., Ltd., or Lanting Jishi, our wholly owned subsidiary incorporated in the PRC, that primarily engages in providing supplier and warehouse management services for Light In The Box Limited. In 2014 and 2015, we derived 0.2% and 0.1%, respectively, of our consolidated total net revenues from Lanting Jishi. We did not derive any consolidated net revenues from Lanting Jishi in 2016;

- Shenzhen Lanting Huitong Technologies Co. Ltd., or Lanting Huitong, a company incorporated in the PRC by certain of our directors and executive officers which is our consolidated VIE through a series of contractual arrangements. Lanting Huitong primarily engages in technology research and development and support, the operation of certain of our websites in China and the general operations of our business in China;

- Shanghai Ouku Network Technologies Co., Ltd., or Shanghai Ouku, a PRC incorporated company that was acquired from its then shareholders for $2.2 million (RMB14.3 million) and is wholly owned by Lanting Huitong. Shanghai Ouku primarily engages in the product sourcing, marketing, fulfillment and the operation of our websites targeted towards consumers in China. In 2014, 2015 and 2016, we did not derive any consolidated net revenues from Lanting Huitong and Shanghai Ouku;

- Beijing Lanting Gaochuang Technologies Co., Ltd., or Lanting Gaochuang, a company incorporated in the PRC by Mr. Guo, and Lanting Huitong, our consolidated VIE through a series of contractual arrangements. Lanting Gaochuang primarily engages in technology research and development. We have not derived any consolidated net revenues from Lanting Gaochuang since its inception, and we do not expect to derive any significant contributions to our consolidated net revenues from Lanting Gaochuang going forward, if at all;

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- Lanting International Holding Limited, or Lanting International, our wholly owned subsidiary incorporated in Hong Kong as an intermediary holding company for our U.S. subsidiary, LITB, Inc.;

- LITB, Inc., our wholly owned subsidiary incorporated under the laws of the State of Delaware, USA, that primarily engages in marketing and software development and technology support . We have not derived any consolidated net revenues from LITB, Inc. since its inception;

- LightInTheBox International Logistic Co., Limited, or Lightinthebox Logistics, our wholly owned subsidiary incorporated in Hong Kong that primarily focuses on the expansion of our warehouses and distribution network outside of China. In 2015 and 2016, we derived an aggregate of 3.4% and 10.0% of our consolidated total net revenues from Lightinthebox Logistics, respectively;

- LITB Netherlands B.V., our wholly owned subsidiary incorporated in the Netherlands that primarily engages in marketing in Europe;

- Light In The Box (Chengdu) Technology Co. Limited, our wholly owned subsidiary incorporated in the PRC that primarily engages in mobile application software development and information technology support;

- Light In The Box (Suzhou) Trading Co., Limited, our wholly owned subsidiary incorporated in the PRC that primarily engages in providing supplier and warehouse management services for Light In The Box Limited. In 2015 and 2016, we did not derive any consolidated net revenues from Light In The Box (Suzhou) Trading Co., Limited; and

- Each of Light Square Limited, or Light Square, Light Hill Limited, or Light Hill, Light Linnet Limited, or Light Linnet, Light Xiao Limited, or Light Xiao, and Fashion Easy-go International Trading Co., Ltd. or Fashion Easy-go, our wholly owned subsidiary incorporated under the laws of Hong Kong that primarily engages or expected to be engaged in the wholesale business distribution of products. The entire share capital of these subsidiaries are registered in the name of our employees who hold such shares on trust for the benefit of Light In The Box Limited pursuant to the respective declaration of trust executed on various dates in June and July of 2016. As of the date of this annual report, the business operation of each of Light Hill, Light Linnet, Light Xiao and Fashion Easy-go remain inactive. In 2016, we derived an aggregate of 0.3% of our consolidated total net revenues from Light Square.

Our principal executive offices are located at Tower 2, Area D, Diantong Square, No. 7 Jiuxianqiao North Road, Chaoyang District, Beijing 100015, People s Republic of China. Our telephone number at this address is +(86-10) 5692-0099. Our registered office in the Cayman Islands is located at the office of Offshore Incorporations (Cayman) Limited, Scotia Centre, 4th Floor, P.O. Box 2804, George Town, Grand Cayman

KY1-1112, Cayman Islands. Our telephone number at this address is +1 345 949 2648. Our agent for service of process in the United States is Law Debenture Corporate Services Inc., 400 Madison Avenue, 4th Floor, New York, New York 10017.

Initial Public Offering

In June 2013, we completed our initial public offering, in which we offered and sold 19,090,000 ordinary shares in the form of ADSs, raising $75.0 million in proceeds before expenses to us. Our ADSs are listed on the NYSE under the symbol LITB.

ADS Repurchases

On December 16, 2013, we announced the implementation of a share repurchase program of up to $20.0 million worth of our outstanding ADSs each representing two of ordinary shares on the open market at prevailing market prices or in privately negotiated transactions through December 15, 2014. On December 16, 2014, we extended this share repurchase program for an additional 12-month period from December 16, 2014 to December 15, 2015 with all terms and conditions of the share repurchase program remaining unchanged. As of August 31, 2015, we had completed the $20.0 million share repurchase program.

On June 8, 2016, we announced the implementation of a share repurchase program of up to $10.0 million worth of our outstanding ADSs each representing two of ordinary shares on the open market at prevailing market prices or in privately negotiated transactions from June 15, 2016 through June 14, 2017. See Item 16E. Purchases of Equity Securities by the Issuer and Affiliated Purchasers.

Private Placement

In July 2015, AOGANG International (Hong Kong) Corporation Limited, or AOGANG International, a wholly-owned subsidiary of Zhejiang Aokang Shoes Co., Ltd. (SSE: 603001), or AoKang, one of the leading shoes and leather products companies in China, has completed the acquisition of a strategic equity interest in the Company from certain existing shareholders of the Company at $6.30 per ADS.

In March 2016, we completed the issuance of 42,500,000 ordinary shares to Zall Cross-border E-commerce Investment Company Limited, or Zall E-Commerce, an indirect wholly-owned subsidiary of Zall Group, a developer and operator of large-scale consumer-focused product wholesale shopping malls in China, at $1.80 per ordinary share, which amounted to $76.5 million in proceeds. In addition, we have agreed to issue a warrant to Zall E-Commerce pursuant to which Zall E-Commerce may subscribe for up to 7,455,000 ordinary shares of our company, equivalent to 3,727,500 ADSs, accounting for an additional 5% equity interest in our company on a fully diluted basis, at an exercise price of $2.75 per ordinary share, equivalent to $5.50 per ADS, pursuant to the terms and conditions of such warrant. The warrant is exercisable starting from September 30, 2016 and will terminate on March 30, 2018. Furthermore, Zall E-Commerce is granted certain registration and anti-dilution rights under the terms and conditions of the transaction.

B. Business Overview

Overview

LightInTheBox is a global online retail company that delivers products directly to consumers around the world. We offer customers a convenient way to shop for a wide selection of products at attractive prices through *www.lightinthebox.com, www.miniinthebox.com* and our other websites as well as mobile applications, which are available in 23 major languages and cover more than 80.0% of Internet users globally, according to Internet World Stats. Our innovative data-driven business model allows us to offer customized products at scale through optimal merchandising, marketing and fulfillment. We have built an effective business model whereby we source many of our products directly from China-based manufacturers and we work closely with them to re-engineer their manufacturing processes to achieve faster time-to-market with a greater

variety of products. We acquire customers primarily through the Internet and serve our customers primarily from our cost-effective locations in mainland China and Hong Kong.

We target products where consumers value choice or customization, such as apparel and home and garden products. We also offered a wide range of other products in our other general merchandise product category. The products of our core categories generally require design specificity, thus giving us more pricing flexibility and allowing us to capture higher margin potentials. For example, at any time, a customer shopping for a special occasion dress on our site can have her dress made-to-measure, choosing from more than 10,000 distinctive designs. As of December 31, 2016, we had more than 322,000 product listings. In 2016, we added an average of more than 204,000 new product listings each month.

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We serve consumers globally without incurring the costs and complexities associated with establishing a traditional multinational retail infrastructure. Our major markets are Europe and North America. We use global online marketing platforms such as Google and Facebook to reach our consumers, we accept payments through all major credit cards and electronic payment platforms such as PayPal, WorldPay and Global Collect and we deliver our goods through major international couriers, including DHL, UPS and EMS.

In recent years, leveraging our growing operation scale, including our established relationships with major international couriers, we also begun to provide logistics and other value-added services, such as marketing services, primarily to small businesses in China and our suppliers.

We believe that being a China-based company provides important advantages in supply chain management. We strive to source high quality products directly from some of the most competitive manufacturers in the strongest supply ecosystems. By locating our sourcing offices near some of the most competitive factories, we realize cost advantages and inventory efficiency as we create effective supplier competition while maximizing the quality of our products in many cases. Our suppliers benefit from working closely with our in-house manufacturing experts to re-engineer their manufacturing processes to achieve faster time-to-market for our products and enable large scale production of individually customized products. We are also in the process of building our global supply chain and sourcing strategy.

To acquire and retain customers across diverse geographic markets, we have developed proprietary technologies to manage and optimize our marketing operations. In addition, we have established a specialized social marketing team to engage online users. We provide a user-friendly online shopping experience to facilitate purchasing decisions.

We have developed a proprietary technology platform that integrates every aspect of our business operation, including global marketing, online shopping platforms, supply chain management, fulfillment and logistics and customer service. Our founders have extensive experience and expertise in software development. We have made significant investments in software research and development to improve operational efficiency and enable business innovation.

Our Websites and Mobile Applications

We operate our business primarily through *www.lightinthebox.com* and *www.miniinthebox.com* , offering customized apparel, small accessories and gadgets, home and garden, electronics and communication devices and other products. Our *www.lightinthebox.com* website is currently available in 23 major languages.

We have established additional websites for more specific products and geographic regions, including *www.ouku.com* for products targeting our Chinese customer base. All of our websites and mobile applications are supported by a common back-end technology platform, allowing for centralized inventory management across all of our websites.

We have made our websites and mobile applications easily accessible by users on their mobile devices. We believe this provides our customers with greater flexibility and convenience as to when and where they shop and provide us with the ability to attract even more customers. We have launched a dedicated shopping application that works with the iPhone TM , the iPad TM and the Android TM to enhance the mobile shopping

experience of our users. In addition to our LightInTheBox and MiniInTheBox mobile applications, we have also launched our flash sales application called Flash. As the number of customers making purchases through our mobile apps continues to increase, our mobile revenue increased to 38.4% of net revenues from product sales in 2016, compared with 26.8% and 33.5% in 2014 and 2015, respectively.

Our websites and mobile applications offer consumers a rich shopping experience and includes comprehensive information on our entire line of products such as detailed descriptions, rich media presentation, size and color availabilities and customer reviews. We have multilingual copywriter teams to ensure we translate important information on our websites and mobile applications in different languages accurately and in a timely fashion. Users may search and view our products by category, style and other popular features. They may also search by product name, code or keyword. We offer users social media tools on our websites and mobile applications to share information about our products on the world s major social networking sites. We have also established online communities to foster customer peer sharing. Furthermore, we have introduced other functionalities to our sites, such as flash sale featuring our fashion apparel.

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Supplemental Online Outlets

In addition to our own websites and mobile applications, we also experiment with selling through outlets on other high traffic online marketplace platforms such as Amazon.com and eBay.com. These other online outlets provide us with additional channels for the sale of our products and market intelligence to optimize our product offerings.

Our Product Offerings

We primarily offer customers products through our websites and mobile applications. We have historically focused on apparel and electronics and communication devices. In recent years, we have introduced other products, with a particular focus on small accessories and gadgets and home and garden, as well as beauty and sports and outdoor. We intend to continue to expand our product offerings and increase the variety and customization options of the products we offer in each of our categories.

Our product offerings include:

- *Apparel.* This category includes customized, special occasion apparel and fast fashion.

- *Other general merchandise.* This category includes small accessories and gadgets, home and garden, electronics and communication devices and other products.

We have established dedicated retail management teams with strong expertise in their individual categories. We focus on products with strong market demand and large market size, supply chain feasibility, Chinese cost advantages, online marketing efficiency, logistical feasibility and cost saving potentials. After products are selected, we conduct frequent real-time customer behavior analysis and seek customer feedback through surveys to improve and tailor our offerings. This allows us to quickly make adjustments and improvements to our products or the presentation of such products. For wedding apparel, we have established our own design teams. Such internal design expertise allows us to create distinctive product designs and provide design feedback to suppliers as to the latest fashions and trends. Our design teams also assist us with our product selection and product presentation to maximize the appeal of our product offerings.

Net revenues from our product sales accounted for 100.0%, 96.5% and 89.6% of our total net revenues in 2014, 2015 and 2016, respectively.

Our Services Offering

In recent years, leveraging our growing operation scale, including our established relationships with major international couriers, we also begun to provide logistics and other value-added services, such as marketing services, primarily to small businesses in China and our suppliers. Our logistics services include product collection, packaging and labeling, shipment and delivery of products from our warehouses to locations designated by such small business customers. Our other value-added services primarily relates to the provision of marketing services to our suppliers to promote their brands and products on our websites and mobile applications.

Net revenues from services accounted for a very limited portion of our total net revenues in 2014. Net revenues from services accounted for 3.5% and 10.4% of our total net revenues in 2015 and 2016, respectively.

Our Relationship with Suppliers

We source many of our products directly from factories in China. In addition, we source products outside of China, such as from South Korea, Japan, Hong Kong, Australia and New Zealand. We have a comprehensive supplier qualification system and have over 4,800 selected active suppliers in China, accordingly. We are also in the process of building out our global supply chain and sourcing strategy. We select our suppliers based on a range of factors, including product quality, price, reliability, financial strength, reputation, ability to meet our delivery timeline and production capacity, ability to increase their production capacity along with the increase in our business and historical relationship. We employ a bidding process for the selection of our suppliers to encourage competition.

While we do not have manufacturing operations ourselves, we have in-house manufacturing experts who work closely with our suppliers. This provides us with visibility into the manufacturing process, which allows us to efficiently manage capacity and quality and enables continuous improvements and business innovations. Typically we enter into supply framework agreements with our suppliers and specify in each purchase order the product type, unit price, quantity, delivery timeline and other detailed items. As the manufacturing processes of some of our products, such as apparel and certain electronics, require a variety of delicate parts and materials, we usually require our suppliers to procure key materials from our designated raw material suppliers in case of raw material shortages and to ensure prompt fulfillment for popular items. We may also require our suppliers to produce custom fabrics and other materials in accordance with certain design and specification. Our suppliers are liable for problems and costs associated with custom clearance.

We believe that being a China-based company provides important advantages in supply chain management. We have established a supply network that is characterized by on-demand procurement with low lead time. We have established seven sourcing offices in China. We work with some of our suppliers to re-engineer their manufacturing process that enables us to place orders in relatively small batches. This provides us with the advantage to quickly adjust the design of our products, in each batch if needed, based on customer feedback. For example, for our made-to-measure products, such as customized apparel, we place orders with our suppliers only when our customers have placed an order, and such products are delivered to our warehouses by our suppliers within ten to 14 days from the time when we place an order. For non-customized products, we adopt a frequent procurement strategy characterized with short refill cycles from suppliers that are, in most cases, within 48 hours. Our supply chain management system has been efficient in managing inventory while also reducing production waste for our suppliers, which we believe increases the desire for suppliers to work with us.

Starting from the fourth quarter of 2011, we have entered into arrangements with certain suppliers under which the suppliers store their products at our warehouses. Such products are referred to in this annual report as co-location inventory. Such co-location inventory products are delivered to our warehouses by our suppliers at their own costs, and we do not record these products as our inventory until all liabilities and rights of ownership of these products are passed on to us upon the confirmation of orders by our customers. We have the right to ask the suppliers to remove the co-location inventory from our warehouses at any time, generally at the suppliers own costs. However, we may from time to time pay the transportation cost associated with returning such products to suppliers. In addition, certain agreements with our suppliers require them to remove unsold co-location inventory within 90 days after these products are delivered. The costs and expenses incurred related to the storage of co-location inventory in our warehouses, such as rentals, are generally paid by us.

Purchases from our suppliers accounted for 62.0%, 63.0% and 61.3% of our total cost of product sales in 2014, 2015 and 2016, respectively.

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Pricing

In general, we aim to set our products at competitive prices. We price our products to reflect the savings associated with direct sourcing, low inventory levels and optimized logistics. We set the price of our products based on consumer demand and feedback, sourcing costs, delivery costs and existing market prices for similar products. As we perform extensive data analysis on our product presentation and customer purchasing decisions, we believe we can effectively conduct targeted promotional activities, identify optimal pricing points for each product and generate strong product sales and gross-margin performance.

Payment and Order Fulfillment

Payment

Our customers may choose from a wide range of payment methods. For our customers on *www.lightintthebox.com* and other sites targeting customers outside of China, operated by Light In The Box Limited, available payment options include online payment through all major credit and debit cards, including Visa, MasterCard and American Express, and electronic payment platforms such as PayPal, World Pay and Global Collect, money transfer through Western Union and wire transfer. However, available payment options may differ depending on the country or region in which the customers are based.

For customers on our *www.ouku.com* and other sites operated by Lanting Huitong and Shanghai Ouku targeting customers in China, payment options include cash on delivery, online payment, wire transfer and postal remittance. We also allow our customers to pay online with credit cards and debit cards issued by major banks in China, or through popular third-party electronic payment platforms.

Order Fulfillment

We have established strategically located warehouses in Suzhou, Jiangsu Province and Shenzhen, Guangdong Province in China. We also established a warehouse in Warsaw, Poland in March 2014, a warehouse in Hong Kong in July 2014 and a warehouse in Reno, Nevada in the United States in January 2015. In total, our warehouses measure over 50,971 square meters and have the capacity to handle over 30,000 orders per day. As we grow our business, we build incremental capacity to reduce our capital expenditures. Our warehouses are currently leased.

Generally, orders placed by our customers are transmitted via our information technology system to one of our warehouses. As a result of our unique supply network, we have generally maintained a low inventory level and, in many cases, do not keep many products in stock. Rather, we transmit orders to our suppliers for fulfillment only when such orders are received from our customers or on a daily basis in small batches. Products are then delivered from our suppliers to our warehouses for quality inspection before being shipped out to our customers by third-party couriers. We regularly monitor our order fulfillment process and solicit customer feedback to ensure fulfillment accuracy.

We offer a wide range of delivery options to our customers. We work with major international couriers such as DHL, UPS and EMS, for international deliveries. We also work with various local couriers for deliveries in China.

Refund and Exchange

We have implemented refund and exchange policies specific to each of our product categories. Generally, for products sold through our *www.lightinthebox.com, www.miniinthebox.com* and other sites targeting customers outside of China, if the product is returned for quality issues, damage during shipping, failure to conform to specifications, allergic reactions, we generally provide a full refund if the customer submits a return-request form to one of our customer service representatives within 30 days of receiving the product. Customized apparel return requests are subject to additional restrictions due to the personalized nature of such products. Customers in the United States and Europe can return products to our outsourced collection centers in these areas. For products sold through our *www.ouku.com* and other sites targeting customers in China, refunds are generally provided within seven days of purchase for quality issues. Customers in China who choose to make payment on delivery can inspect products and reject the delivery in part or in whole prior to paying for the goods.

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Quality Control

We believe that our ability to offer quality products is essential to our continued growth and success. Therefore, we emphasize quality control and, as of December 31, 2016, we had built a quality control department of more than 40 employees.

As we source all of our products from suppliers, we have implemented a series of quality control measures to ensure that the products they provide meet our specifications and standards. We communicate actively with our suppliers to clarify our requirements, conduct onsite inspections both to ensure compliance with specifications on particular items as well as for regular quality concerns and share customer feedback. We thoroughly examine product prototypes or initial samples before production begins or agreements with the suppliers are enter into. We examine products when they arrive at our warehouses and we thoroughly inspect most of our products just prior to delivery to our customers.

Marketing

We focus our marketing activities on effective customer acquisition through targeted performance marketing. We primarily employ search engine marketing on a cost-per-click basis. Users are shown our advertisements when they conduct searches using designated keywords or phrases. Under our cost-per-click arrangements, we pay a fixed fee for each time a user clicks on our advertisements, with a higher fee for common keywords with a high correlation to purchase intention. Under our cost-per-acquisition arrangements, we pay each time a user purchases a product after clicking on an advertisement. We employ a combination of our own proprietary technology and advanced third-party infrastructure to manage and optimize our cost-per-click advertising and to discover long-tail multilingual keywords that are most likely to offer a positive return on investment.

We display contextual advertising through major search engines   advertising networks on a cost-per-click basis. We measure the cost of customer acquisition and constantly adjust our keyword selection combinations, advertising copies and landing pages to increase the likelihood of customer purchases once they visit our websites and mobile applications. We also engage in an affiliate marketing program where we offer affiliated websites commissions for directing customer traffic to our websites and mobile applications through embedded hyperlinks. As of the date of this annual report, we actively managed millions of keywords in 23 languages and display advertising on over 800,000 publisher sites around the world. Furthermore, we have established a specialized social marketing team to promote our brand and presence across major global social networking platforms through viral marketing campaigns, such as exclusive deals to stimulate customer purchases.

We are also focused on providing our customers with a rich shopping experience, which drives customer recommendations, foster customer sharing and encourages repeat customer visits. We engage in direct marketing campaigns through personalized electronic direct marketing newsletters to our customers. We believe that our data analysis capabilities facilitate repeat purchases as we are able to send targeted notices to customers highlighting products they may find relevant and attractive. In addition, we have established a specialized customer relationship management team to enhance our customer experience.

Customer Service

We believe our rapid growth in past years and success in attracting a growing customer base is partially attributable to our effort to provide excellent customer service. We have a team of highly trained customer service representatives to address customer inquiries, educate potential customers about our products and services and monitor order progress. We also pay close attention to reviews of our business or products on our or third-party websites in order to promptly address customer complaints and to improve our shopping experience and product offerings. Our full-time and part-time customer service representatives are able to provide customer services in 23 languages, up from 16 languages in 2012, and most of these representatives have overseas working experience.

We primarily provide customer services for our *www.lightinthebox.com* , *www.miniinthebox.com* and other sites targeting customers outside of China through electronic communications, including real-time online chat, e-mails and messages posted on our websites and mobile applications or through social media networks. Customer service for our *www.ouku.com* and other sites targeting customers in China are provided through toll-free call centers and electronic communications.

Our websites and mobile applications also offer a variety of self-help features. These features help our customers to track the status of their orders in real time. Customers may also cancel or modify their orders or contact our customer service representatives for exchange or return of products. We collect customer feedback to improve our responses and utilize such feedback to update our knowledge base to better address customers needs.

For discussion as to our product exchange and return policy, see Payment and Order Fulfillment Refund and Exchange.

Technology

We have focused on and will continue to invest in our information technology infrastructure and applications. We have built a proprietary modularized and scalable technology infrastructure, which enables us to quickly expand system capacity and add new features and functionalities in response to our business needs and evolving customer demand without affecting our existing operations or incurring significant costs.

Our systems are mainly composed of front-end and back-end modules with different functions. Each module operates independently and is not affected by the performance of other modules. The following describes the functionality of our front-end and back-end modules:

- *Front-end Modules* . Our front-end modules support the operation of our user-interface websites, including user account management, website homepages, search functions, category browsing, product display pages, online shopping carts, checkout and order management functions.

- *Back-end Modules* . Our back-end modules support our business operations, including our marketing system, order processing system, inventory management system, sourcing system (which is connected to systems of many of our suppliers for order placement and tracking), product fulfillment system (which is tied to our warehouses), product recommendation system, e-mail delivery system and customer support system. Many of our back-end systems work with each other and our financial operations systems and can generate up-to-date inventory reports and automatically place customized orders with our manufacturers.

A critical component of our business model is our data analysis capabilities. We have a dedicated data analysis team to track, analyze and forecast customer purchase and browsing behaviors. This enables us to anticipate market demand, arrange for production, rearrange website

layouts and product placement, product presentation and supports our supply network. Our systems are integrated to allow a seamless communication of data regarding our customers, their orders, product availability information and logistics information.

Our open application programming interface approach allows us to integrate and work with third- party websites including social network sites, electronic payment platforms, other online distribution outlets and analytic systems. We have also adopted rigorous security policies and measures, including our dual-key and server-specific encryption technology, to protect customer privacy. Customers are protected by their own unique passwords and by our advanced data security software.

Competition

The retail market for our products is intensely competitive. Consumers have many product choices online and offline offered by global, regional and local retailers. Our current or potential competitors include online retailers such as other China-based global online retail companies, retail chains, specialty retailers and sellers on online marketplaces. Each of our competitors has unique strengths that depend on their demographic, product and geographic focus. We may also in the future face competition from new entrants, consolidations of existing competitors or companies created through spin-offs of our larger competitors. For information in relation to the competitive challenges that we face, see Item 3. Key Information D. Risk Factors Risks Related to Our Business and Industry The online retail industry is intensely competitive and we may not compete successfully against new and existing competitors, which may materially and adversely affect our results of operations.

We compete on the basis of characteristics such as sourcing products efficiently, technology innovation, pricing our products competitively, maintaining the quality of our products and services, anticipating and responding quickly to changing consumer demands, conducting strong and effective marketing activities and maintaining favorable brand recognition. We believe that our primary competitive advantages are our technology-enabled infrastructure, our differentiated product offerings, direct sourcing from cost competitive and flexible suppliers in China, strong online marketing capabilities, favorable prices, effective customer service, and a strong management team.

Intellectual Property

We rely on a combination of trademark, trade secret, patent and other intellectual property laws as well as confidentiality agreements with our employees, manufacturers and others to protect our intellectual property. We have registered domain names for all of our websites, including *www.lightinthebox.com, www.ouku.com* and *www.miniinthebox.com* and trademarks and service marks in China, Hong Kong and the European Union, including for *Lightinthebox* and *MiniInTheBox*. We also have 19 registered computer software copyrights in China and one registered computer software copyright in the United States. In addition, we have filed additional trademark applications in China, Hong Kong, Japan, Korea, Brazil, Russia, Austria, the European Union and the United States, as well as patent applications in China and the United States.

In addition to the protection of our intellectual property, we are also focused on ensuring that our product offerings do not infringe the intellectual property of others. We have adopted internal policies and guidelines during product design and procurement process to make sure our suppliers and products we offer do not infringe on third-party intellectual property rights. All our supplier agreements contain provisions to safeguard against potential intellectual property infringement by our suppliers and impose severe penalties in the event of any infringement. We will also refuse to work with or terminate our relationship with suppliers in the event of intellectual property right violations. In addition, we have also engaged third-party advisors to assist us in ensuring compliance with third-party intellectual property rights.

Despite our best efforts, however, we cannot be certain that third parties will not infringe or misappropriate our intellectual property rights and that products sold on our websites and mobile applications do not infringe or misappropriate the intellectual property rights of others. For information in relation to the challenges we face protecting our intellectual property, see Item 3. Key Information D. Risk Factors Risks Related to Our Business and Industry We may not be able to prevent unauthorized use of our intellectual property, which could harm our business and competitive position. For information in relation to the challenges we face in relation to preventing our infringement of the intellectual property rights of others, see Item 3. Key Information D. Risk Factors Risks Related to Our Business and Industry Products manufactured by our suppliers may be defective or inferior in quality or infringe on the intellectual property rights of others, which may materially and adversely affect our business.

Seasonality

We experience seasonality in our business, reflecting seasonal fluctuations in online and offline retail patterns in general and for our products. For example, product sales may be higher in the fourth quarter of a calendar year due to the Christmas holidays. Our product mix may experience quarterly shifts which may cause our margins to fluctuate from quarter to quarter. See Item 3. Key Information D. Risk Factors Risks Related to Our Business and Industry Our results of operations are subject to quarterly fluctuations due to a number of factors that could adversely affect our business and the trading price of the ADSs.

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Insurance

We participate in government sponsored social security programs including pension, unemployment insurance, childbirth insurance, work-related injury insurance, medical insurance and housing fund. We currently have limited insurance covering certain of our warehouses but do not maintain insurance for all of our properties. In addition, as is typical in China, we do not maintain business interruption insurance, or general third-party liability insurance, general product liability insurance, or key-man life insurance. See Item 3. Key Information D. Risk Factors Risks Related to Our Business and Industry We do not have any business liability, disruption or litigation insurance and any business disruption or litigation we experience might result in our incurring substantial costs and diversion of resources.

Regulation

We sell our products to customers around the world, and as such we are subject to a number of foreign and domestic laws and regulations that affect companies conducting global online retail businesses, many of which are still evolving and could be interpreted in ways that could harm our business. For example, we are subject to laws protecting the privacy of customer non-public information and regulations prohibiting unfair and deceptive trade practices. Other laws in which we may be subject include issues such as user privacy, the tracking of consumer activities, marketing e-mails and communications, other advertising and promotional practices, content and quality of products and services, sales and other taxes, import and export laws, electronic contracts and other communications and mandatory data retention.

For example, tax authorities in a number of states in the United States are currently reviewing the appropriate tax treatment of companies engaged in online commerce, and new state tax regulations may subject us to additional state sales and income taxes. New legislation or regulations, the application of laws and regulations from jurisdictions whose laws do not currently apply to our business or the application of existing laws and regulations to the Internet and commercial online services could result in significant additional taxes or regulatory restrictions on our business.

Many states in the United States have passed laws requiring notification to subscribers when there is a security breach of personal data. There are also a number of legislative proposals pending before Congress, various state legislative bodies and foreign governments concerning data protection. In addition, data protection laws in Europe and other jurisdictions outside the United States may be more restrictive, and the interpretation and application of these laws are still uncertain. It is possible that these laws may be interpreted and applied in a manner that is inconsistent with our data practices. If so, in addition to the possibility of fines, this could result in an order requiring that we change our data practices, which could have an adverse effect on our business. Complying with these various laws could cause us to incur substantial costs or require us to change our business practices in a manner adverse to our business.

Although our products are sold all over the world, our operations are based primarily in China, and as such, we are primarily governed by and especially sensitive to the laws and regulations of China, including the following:

Regulations Relating to Cross-border Trading

The Customs Law, effective as of July 1, 1987 and amended on July 8, 2000, June 29, 2013 December 28, 2013 and November 17, 2016, divides imported and exported items into goods and articles based upon the nature and purpose of such items. Under the Customs Law, goods and articles are not defined. However, this concept is clarified in the Rules for the Implementation of Administrative Punishments Under the Customs Law, effective as of November 1, 2004. These Rules describes articles as postal items and travelers luggage that are brought in and out of the PRC on an individual s person or luggage. When the quantity of articles is higher than a reasonable amount for personal use, it will be regarded as goods . Personal use means that the traveler or consignee will use the items themselves or give the items as gifts, rather than selling or renting the items. Reasonable amount means the regular amount determined in accordance with the traveler or consignee s situation, purpose of travel and duration of stay. Product samples are also categorized as goods , but customs declaration, clearance and inspection procedures for the export of product samples are handled differently from the export of other goods .

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The Foreign Trade Law, effective as of July 1, 2004 and amended on November 17, 2016, governs international trade in services and the import and export of goods and technologies. Under this law, goods and technologies are categorized as (i) permitted, which may be freely imported and exported, (ii) restricted, which require advance approval or (iii) prohibited, which may not be imported or exported at all. Currently, all merchandise we export is categorized as permitted. Furthermore, an import and export trader , or any company or individual engaging in the import or export of goods or technologies, must register with the administrative department of foreign trade under the State Council or any of its authorized bodies in order to be qualified as a foreign trade business operator. According to current foreign trade laws, the Ministry of Commerce and its competent local branches are the authorized bodies to conduct qualification filings and registrations for foreign trade business operators.

The Customs Law requires that importers and exporters make true declarations of their goods and technologies to customs. The Imported and Exported Merchandise Inspection Law, issued February 21, 1989 and amended on June 29, 2013, also requires that certain items listed in the Catalogue of Import and Export Commodities for Inspection, or the Customers Catalogue, must be inspected by a commodity inspection organization authorized by the State Administration for Commodity Inspection before they can be exported. For import and export commodities not listed in the Customers Catalogue, the commodity inspection authorities may conduct random inspections pursuant to the Measures for the Administration of Random Inspection of Import and Export Commodities, issued as of December 31, 2002. Further, the Ministry of Commerce and General Administration of Customs jointly adopted a mandatory licensing system for the export of certain merchandise, which exporters must comply with depending on the commodities they export.

The customs declaration, clearance and inspection procedures for goods and articles are different. The declaration of import or export of goods may be made by the consignees or consigners themselves or by customs brokers that have registered with the permission of the customs. The consignees, consigners or customs brokers shall make true declarations and submit the import or export license for restricted goods and relevant documentation to the customs for inspection. Where the commodities are imported or exported by means of express delivery, the consignees or consignor shall entrust an entry-exit express delivery enterprise with the inspection declaration, pursuant to the Regulations on the Implementation of the Law of the People s Republic of China on Import and Export Commodity Inspection, effective as December 1, 2005 and most recently amended on February 6, 2016. In addition, a new clearance system for express delivery consignments was established on March 24, 2016, allowing express delivery operators to declare goods valued no more than RMB5,000 online. The Imported and Exported Merchandise Inspection Law also requires that certain goods must be inspected by a commodity inspection organization before they can be exported, while other exported articles are generally exempted from inspection unless otherwise required by law.

We work with third-party couriers to ship the merchandise purchased by our global customers on a parcel-by-parcel basis and to go through customs declaration, clearance and inspection procedures for the export of these merchandise. The customs declaration, clearance and inspection procedures for the merchandise which are packaged and shipped in parcels are handled in accordance with procedures for articles or product samples. If the PRC government determines that our custom declaration practice do not comply with applicable laws and regulations and the merchandise we sell to our global customers shall be exported as goods instead of articles or product samples, it may take regulatory or enforcement actions against us. See Item 3. Key Information D. Risk Factors Risks Related to Doing Business in China We may be adversely affected by the uncertainties and changes in the PRC regulations and policies of cross-border business activities.

Corporate Laws and Industry Catalogue Relating to Foreign Investment

The establishment, operation and management of corporate entities in China are governed by the Company Law of the PRC, or the Company Law, effective in 1994 and as amended in 1999, 2004, 2005, and 2013 respectively. The Company Law is applicable to our PRC subsidiary, our VIEs and Shanghai Ouku unless the PRC laws on foreign investment have stipulated otherwise.

The establishment, approval, filing, registered capital requirement and day-to-day operational matters of wholly foreign owned enterprises, such as our PRC subsidiary, Lanting Jishi, are regulated by the Wholly Foreign owned Enterprise Law of the PRC, effective in 1986 and as amended in 2000 and 2016, and the Implementation Rules of the Wholly Foreign Owned Enterprise Law of the PRC, effective in 1990, as amended in 2001 and 2014. Under those rules, in those cases where the establishment of a given wholly foreign-owned enterprise does not involve any special restriction under applicable PRC regulations, the establishment, breakup, merger or any other major change to such wholly foreign-owned enterprise will be subject to record-filing requirements.

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Investment activities in the PRC by foreign investors are principally governed by the Guidance Catalogue of Industries for Foreign Investment, or the Catalogue, which was promulgated and is amended from time to time by the Ministry of Commerce and the National Development and Reform Commission. The Catalogue divides industries into three categories: encouraged, restricted and prohibited. Industries not listed in the Catalogue are generally open to foreign investment unless specifically restricted by other PRC regulations.

Establishment of wholly foreign owned enterprises is generally permitted in encouraged industries. Some restricted industries are limited to equity or contractual joint ventures, while in some cases Chinese partners are required to hold the majority interests in such joint ventures. In addition, restricted category projects are also subject to higher-level government approvals. Foreign investors are not allowed to invest in industries in the prohibited category.

Regulations Relating to Telecommunications Services

The Telecommunications Regulations were promulgated by the State Council in 2000 and revised in 2014 and 2016, respectively. The Telecom Regulations draw a distinction between basic telecommunication services and value-added telecommunication services. On December 25, 2015, the Ministry of Industry and Information Technology (currently the MIIT)published the Classification Catalogue of Telecommunications Services (the 2015 Catalogue), which took effect on March 1, 2016. The first catalogue was published in September 2000 and was subsequently amended in 2001 and 2003, respectively. Under the 2015 Catalogue, value-added telecommunication services was further classified into two sub-categories and ten items. Internet content provision services, or ICP services, is a subcategory of value-added telecommunications businesses. Under the Telecom Regulations, commercial operators of value-added telecommunications services must first obtain an operating license from the MIIT or its provincial level counterparts.

On September 25, 2000, the State Council issued the Administrative Measures on Internet Information Services, or the Internet Measures, which was subsequently amended on January 9, 2011. According to the Internet Measures, commercial ICP service operators must obtain a value-added telecommunications license for Internet information service or an ICP license from the relevant government authorities before engaging in any commercial ICP operations within the PRC.

On December 26, 2001, the MIIT promulgated the Administrative Measures on Telecommunications Business Operating License, or the Telecom License Measures. On March 1, 2009, the MIIT issued the revised Telecom License Measures, which took effect on April 10, 2009. The Telecom License Measures set forth the types of licenses required to operate value-added telecommunications services and the qualifications and procedures for obtaining such licenses. For example, an ICP operator providing value-added services in multiple provinces is required to obtain an inter-regional license, whereas an ICP operator providing the same services in one province is required to obtain a local license.

To comply with these PRC laws and regulations, Lanting Huitong, as our ICP operator, holds an ICP license.

Regulations Relating to Foreign Investment in Value-Added Telecommunications Industry

According to the Administrative Rules for Foreign Investment in Telecommunications Enterprises issued by the State Council effective in January 2002, as amended in September 2008 and 2016, respectively, a foreign investor may hold no more than a 50% equity interest in a value-added telecommunications services provider in China and such foreign investor must have experience in providing value-added telecommunications services overseas and maintain a good track record.

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The Circular on Strengthening the Administration of Foreign Investment in and Operation of Value-added Telecommunications Business, or the Circular, issued by the former Ministry of Information Industry in July 2006, reiterated the regulations on foreign investment in telecommunications businesses, which require foreign investors to set up FIEs and obtain an ICP license to conduct any commercial ICP business in China. Under the Circular, a domestic company that holds an ICP license is prohibited from leasing, transferring or selling the license to foreign investors in any form and from providing any assistance, including providing resources, sites or facilities, to foreign investors that conduct value-added telecommunications business illegally in China. Furthermore, certain relevant assets, such as the relevant trademarks and domain names that are used in the value-added telecommunications business must be owned by the local ICP license holder or its shareholders. The Circular further requires each ICP license holder to have the necessary facilities for its approved business operations and to maintain such facilities in the regions covered by its license. In addition, all value-added telecommunications service providers are required to maintain network and information security in accordance with the standards set forth under relevant PRC regulations. If an ICP license holder fails to comply with the requirements in the Circular and also fails to remedy such non-compliance within a specified period of time, the MIIT or its local counterparts have the discretion to take administrative measures against such license holder, including revoking its ICP license.

In March 2015, the National Development and Reform Commission and the Ministry of Commerce issued the updated Catalogue, which further relaxed market access restrictions. Among these changes, foreign investors will now be allowed to own up to 100% of the equity interests in an e-commerce business. The Catalogue became effective on April 10, 2015. However, there are still uncertainties as to how the Catalogue will be enforced in regards to e-commerce business, especially through the MIIT which has authority over the Internet industry.

Regulations Relating to Internet Information Services and Content of Internet Information

On September 25, 2000, the State Council issued the Administrative Measures on Internet Information Services, or the Internet Measures, to regulate the provision of information services to online users through the Internet. According to the Internet Measures, entities engaged in the provision of Internet information services within the PRC should obtain either (i) an Internet Content Provider license issued by the MIIT or its local bureau (ICP License), if the services in question are regarded as commercial Internet information services ; or (2) an ICP filing with the local MIIT bureau (ICP Filing), if the services in question are regarded to as non-commercial services . The former refers to information, web page creation and other services provided to Internet users via the Internet for consideration , while the latter refers to services that provide information of a publicly available and accessible nature to Internet users via the Internet for gratis . Operators providing commercial Internet information services shall obtain specific approvals before providing BBS services and the operators providing non-commercial Internet information services shall obtain specific filings before providing BBS services. If an Internet information service provider fails to obtain an ICP license or ICP filing or fails to obtain a specific approval or filing for its BBS services, the relevant local branch of the MIIT may levy fines, confiscate its income or even block its website. The concepts of commercial and non-commercial Internet information services are stipulated generally and hence leave much room for interpretation by the local MIIT bureau in its approval practice. According to the practice of Shanghai MIIT branch which applies the ICP filing system to online e-commerce activity (rather than ICP license), Shanghai Ouku has made ICP filings for its website. Shanghai Ouku has not obtained specific filings for BBS on its website.

The Internet Measures further specify that Internet information services regarding, among others, news, publication, education, medical and health care, pharmacy and medical appliances are required to be examined, approved and regulated by the relevant authorities. Internet content providers are prohibited from providing services beyond that included in the scope of their business license or other required licenses or permits. Furthermore, the Internet Measures clearly specify a list of prohibited content. Internet content providers must monitor and control the information posted on their websites. If any prohibited content is found, they must remove the offending content immediately, keep a record and report to the relevant authorities.

On February 4, 2015, the China Internet Network Information Center promulgated the Administrative Provisions on Account Names of Internet Users, or the Account Names Provisions, which will become effective as of March 1, 2015. The Account Name Provisions require all Internet

information service provider users to authenticate their real identity information for registration of accounts and to commit to complying with the seven basic requirements , including observing the laws and regulations, upholding the socialist regime, protecting state interests, as well as ensuring the authenticity of any information they provide. Relevant Internet information service providers are responsible for protecting users privacy, the consistency between user information, such as account names, avatars, and the requirements contemplated in the Account Names Provisions, making reports to the competent authorities regarding any violation of the Account Names Provisions, and taking appropriate measures to stop any such violations, such as, notifying users to make corrections within a specified time and suspending or closing accounts in the event of continued noncompliance by users.

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Regulation Relating to E-Commerce

China s e-commerce industry is at an early stage of development and there are few PRC laws or regulations specifically regulating the e-commerce industry. In January 2014, the SAIC issued the Administrative Measures on Online Trading, or the Administrative Measures. The Administrative Measures regulate online trading, including selling items and providing services through the Internet. In addition to basic requirements that online sellers and service provider, or together the Operator, should abide by the requirements of the PRC Consumer Rights and Interests Protection Law and similar rules, the Administrative Measures emphasize that an Operator is responsible for personal data protection. In this respect, Operators are obliged to (i) seek consumers prior consent for collecting and using their personal data, (ii) keep the collected data confidential and secured, and (iii) take effective measures to remedy any leakage or loss of personal data. In addition, the Administrative Measures set specific requirements for operators of third party platforms that provide a web space for parties to transact business. These requirements include authenticating the Operator s identification, signing a contract with the Operator for the use of the platform, setting rules for online trading, security and dispute resolution, cooperation with the local administrations of industry and commerce, taking measures to protect trademark rights and corporate name rights, distinguishing its own products or service from those of other Operators, and keep online trading records for at least two years.

On December 24, 2014, the MOFCOM issue the Provisions on the Procedures for Formulating Transaction Rules of Third-party Platforms for Internet Retail (for Trial Implementation), or the Procedures Provisions, effective as of April 1, 2015. The Procedures Provisions were promulgated to promote the healthy development of Internet retail, protect the legitimate rights and interests of various parties involved in Internet retail activities based on third-party platforms, safeguard the public interest, and strengthen public information services. It specifies the duties of operators of third-party platforms for Internet retail, which are to make relevant transactions rules public and recorded, solicit public opinions when such operators formulate or revise their transaction rules, adapt reasonable transitional measures if the transaction rules that are formulated, revised or enforced by them have a material impact on Internet retail operators and consumers, and similar measures. In addition, the Procedure Provisions also give the power to the local competent commerce authorities to impose penalties on operators where there is a violation.

Under prior laws, foreign investors outside of the China (Shanghai) Pilot Free Trade Zone (subject to certain conditions) are not allowed to own more than 50% of the equity interests in a value-added telecommunications service provider, and any such foreign investor must have experience in providing value-added telecommunications services overseas and maintain a good track record. In March 2015, the National Development and Reform Commission and the Ministry of Commerce issued the updated Catalogue, which further relaxed market access restrictions. Among these changes, foreign investors will now be allowed to own up to 100% of the equity interests in an e-commerce business. However, such foreign investor must have experience in providing value-added telecommunications services overseas and maintain a good track record.The Catalogue became effective on April 10, 2015.

The Administrative Measures, the Procedures Provisions and the Catalogue are new and there are still uncertainties as to their interpretation and implementation.

Lanting Huitong and its subsidiary, Shanghai Ouku, manage www.ouku.com and other websites targeting consumers in China. In the event of any clarifications or interpretations that may be issued in the future regarding the Administrative Measures, the Procedures Provisions and/or the Catalogue, we might need to adjust our operational or contracting practices accordingly.

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Regulations Relating to Privacy Protection

In recent years, the PRC government authorities have enacted legislation on Internet use to protect personal information from any unauthorized disclosure. Current PRC laws do not prohibit ICP operators from collecting and using personal information from their users with consent. However, the Internet Measures prohibit an ICP operator from insulting or slandering a third party or infringing the lawful rights and interests of a third party. Pursuant to the BBS Measures, ICP operators that provide electronic messaging services must keep users personal information confidential and must not disclose such personal information to any third party without their consent or unless required by law. The regulations further authorize the relevant telecommunications authorities to order ICP operators to rectify their unauthorized disclosure. ICP operators are subject to legal liability if the unauthorized disclosure results in damages or losses to users. The PRC government, however, has the power and authority to order ICP operators to turn over personal information if an Internet user posts any prohibited content or engages in illegal activities on the Internet. On December 29, 2011, the MIIT promulgated the Several Provisions on Regulating the Market Order of Internet Information Services, effective as of March 15, 2012. It stipulates that ICP operators may not, without a user s consent, collect the user s information that can be used alone or in combination with other information to identify the user and may not provide any such information to third parties without the user s prior consent. ICP operators may only collect users personal information that is necessary to provide their services and must expressly inform the users of the method, content and purpose of the collection and using of such personal information. In addition, an ICP operator may only use users personal information for the stated purposes under the ICP operator s scope of service. ICP operators are also required to ensure the proper security of users personal information, and take immediate remedial measures if users personal information is suspected to have been inappropriately disclosed. If the consequences of any such disclosure are expected to be serious, ICP operators must immediately report the incident to the telecommunications regulatory authority and cooperate with the authorities in their investigations. On December 28, 2012, the Standing Committee of the National People s Congress of the PRC issued the Decision on Strengthening the Protection of Online Information. Most requirements under this decision relevant to ICP operators are consistent with the requirements already established under the MIIT provisions discussed above, but are often stricter and broader. Under this decision, ICP operators are required to take such technical and other measures necessary to safeguard the information against inappropriate disclosure. To further implement this decision and relevant rules, MIIT issued the Regulation of Protection of Telecommunication and Internet User Information on July 16, 2013, which became effective on September 1, 2013.

On November 7, 2016, the Standing Committee of the National People s Congress issued the Cyber Security Law, which will come into effect on June 1, 2017. The Cyber Security Law imposes certain data protection obligations on network operators, including that network operators may not disclose, tamper with, or damage users personal information that they have collected, and are obligated to delete unlawfully collected information and to amend incorrect information. Moreover, Internet operators may not provide users personal information to others without consent. Exempted from these rules is information irreversibly processed to preclude identification of specific individuals. Also, the Cyber Security Law imposes breach notification requirements that will apply to breaches involving personal information.

We believe that we are currently in compliance with these regulations in all material aspects.

Regulations on Intellectual Property Rights

China has adopted legislation governing intellectual property rights, including trademarks, patents and copyrights. China is a signatory to the major international conventions on intellectual property rights and became a member of the Agreement on Trade Related Aspects of Intellectual Property Rights upon its accession to the World Trade Organization in December 2001.

Patent

The National People s Congress adopted the Patent Law in 1984, which was subsequently amended in 1992, 2000 and 2008. The purpose of the Patent Law is to protect lawful interests of patent holders, encourage invention, foster applications of invention, enhance innovative capabilities and promote the development of science and technology. To be patentable, invention or utility models must meet three conditions: novelty, inventiveness and practical applicability. Patents cannot be granted for scientific discoveries, rules and methods for intellectual activities, methods used to diagnose or treat diseases, animal and plant breeds, substances obtained by means of nuclear transformation or a design which has major marking effect on the patterns or colors of graphic print products or a combination of both patterns and colors. The Patent Office under the State Intellectual Property Office is responsible for administering patents in the PRC. A patent is valid for a term of 20 years in the case of an invention and a term of ten years in the case of utility models and designs, each starting from application date. A third-party user must obtain consent or a proper license from the patent owner to use the patent. Otherwise, the use constitutes an infringement of patent rights.

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China follows a first to file principle for patents. When more than one person files a patent application for the same invention, the patent will be granted to the person who first filed the application. In addition, the PRC requires absolute novelty in order for an invention to be patentable. Pursuant to this requirement, generally, with limited exceptions, any prior written or oral publication in or outside the PRC, demonstration or use in the PRC before the patent application filing prevents an invention from being patented in the PRC. Patents issued in the PRC are not enforceable in Hong Kong, Taiwan or Macau, each of which has an independent patent system. The fact that a patent application is pending is no guarantee that a patent will be granted and, even if granted, the scope of a patent may not be as broad as that of the initial application.

When a patent infringement dispute arises, the patent holder or an interested party who believes the patent is being infringed may either file a civil lawsuit or file a complaint with the relevant authorities in charge of the patent administration. A PRC court may grant the patent holder s or the interested party s request for a preliminary injunction before the legal proceeding. Pursuant to the Patent Law, an infringer shall be subject to various civil liabilities, which include ceasing the infringement and compensating the actual loss suffered by patent owners. If it is difficult to calculate the actual loss suffered by the patent owner, the illegal income received by the infringer as a result of the infringement or if it is difficult to calculate the illegal income, a reasonable amount calculated with reference to the patent royalties shall be deemed as the actual loss. The compensation amount shall also include the reasonable expenses incurred by the patent owner for stopping the infringement. If damages cannot be established by any of the above methods the court can decide the amount of the actual loss up to RMB1,000,000. In addition, an infringer who counterfeits patents of third parties shall be subject to administrative penalties or criminal liabilities if applicable. Typically, a patent holder in the PRC has the burden of proving that the patent is being infringed. However, if the holder of a production process patent alleges infringement of such patent, the alleged infringing party which produces the same kind of products has the burden of proving that there has been no infringement.

We have applied for two patent registrations in China, one of which is now undergoing substantive examination and the other one was successfully registered.

Copyright

Copyrights are protected by the Copyright Law of the PRC which was promulgated in 1990 and amended in 2001 and February 2010 and the Regulation for the Implementation of the Copyright Law of the PRC which came into effect in September 2002 and was amended in January 2011. The amended Copyright Law extends copyright protection to Internet activities, products disseminated over the Internet and software products. In addition, there is a voluntary registration system administered by local Copyright Bureaus and the China Copyright Protection Center. The amended Copyright Law also requires registration of a copyright pledge.

Copyrights shall vest on the authors, unless otherwise provided under the laws. If a work constitutes work for hire , the employer, instead of the employee, is considered the legal author of the work and will enjoy the copyrights of such work for hire other than rights of authorship. Works for hire include, (1) drawings of engineering designs and product designs, maps, computer software and other categories, which are created mainly with the materials and technical resources of the legal entity or organization with responsibilities being assumed by such legal entity or organization; (2) those works the copyrights of which are, in accordance with the laws or administrative regulations or under contractual arrangements, enjoyed by a legal entity or organization. The actual creator may enjoy the rights of authorship of such work for hire. A copyright owner may transfer its copyrights to others or permit others to use its copyrighted works. Use of copyrighted works of others generally requires a licensing contract with the copyright owner. The protection period for copyrights in the PRC varies, with 50 years as the minimum. The protection period for a work for hire where a legal entity or organization owns the copyright (except for the right of authorship) is 50 years, expiring on December 31 of the fiftieth year after the first publication of such work.

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In China, holders of computer software copyrights enjoy protections under the Copyright Law. Various regulations relating to the protection of software copyrights in China have promulgated. Under these regulations, computer software that is independently developed and exists in a physical form is protected, and software copyright owners may license or transfer their software copyrights to others. Registration of software copyrights, exclusive licensing and transfer contracts with the Copyright Protection Center of China or its local branches is encouraged. Such registration is not mandatory under Chinese law, but can enhance the protections available to the registered copyrights holders.

Where copyright or a copyright-related right is infringed, the infringer shall make compensation according to the actual losses incurred by the right owner. Where the actual losses are difficult to calculate, the compensation may be paid according to the illegal incomes obtained by the infringer. The compensation amount shall also include the reasonable expenses incurred by the right owner for preventing the infringement. Where neither the actual losses incurred by the right owner nor the illegal gains obtained by the infringer is determinable, the court may render a ruling to award compensation in an amount not more than RMB500,000.

We have 19 registered computer software copyrights in China.

Trademark

Trademarks are protected by the PRC Trademark Law adopted in 1982 and subsequently amended in 1993, 2001 and 2013 as well as the Implementation Regulation of the PRC Trademark Law adopted by the State Council in 2002. The Trademark Office under the SAIC handles trademark registrations and grants a term of ten years to registered trademarks and another ten years if requested upon expiry of the first or any renewed ten year term. Trademark license agreements must be filed with the Trademark Office for record. The PRC Trademark Law has adopted a first-to-file principle with respect to trademark registration. Where a trademark for which a registration has been made is identical or similar to another trademark which has already been registered or been subject to a preliminary examination and approval for use on the same kind of or similar commodities or services, the application for registration of such trademark may be rejected. Any person applying for the registration of a trademark may not prejudice the existing right first obtained by others, nor may any person register in advance a trademark that has already been used by another party and has already gained a sufficient degree of reputation through such party s use. Trademark license agreements must be filed with the Trademark Office or its regional offices.

Under the Trademark Law, any of the following acts is deemed as an infringement to the right to exclusive use of a registered trademark: (i) using a trademark identical to the registered trademark for the same kind of commodities without a license from the registrant of that trademark; (ii) using a trademark that is similar to a registered trademark for the same goods, or using a trademark that is identical or similar to a registered trademark for similar goods in a way that could be confusing, without a license from the registrant of that trademark ; (iii) selling commodities that infringe upon the right to exclusive use of a registered trademark; (iv) forging or manufacturing without authorization the marks of a registered trademark of another, or selling the marks of a registered trademark that has been forged or manufactured without authorization; (v) changing a registered trademark and putting commodities with the changed trademark into the market without the consent of the registrant of that trademark; (vi) providing conveniences to intentionally facilitate trademark infringement; or (vii) causing other damage to the right to exclusive use of a registered trademark of another person. In the event of any of the foregoing acts, the infringer may be fined, and ordered to stop the infringement acts immediately and pay the infringed party compensation. The compensation shall be equal to the amount of (i) the losses suffered by the infringed party ; (ii) the benefits gained by the infringing party if the losses suffered by the infringed party are difficult to determine, or (iii) a multiple of the royalty for a relevant trademark license if both of the foregoing are difficult to determine, including any reasonable expenses incurred by the infringed party in stopping the infringement. For seriously malicious infringement, the amount of compensation may be one to three times the foregoing amounts. If it is difficult to determine the amount of the benefits gained by the infringing party, the losses suffered by the infringed party or the relevant royalty for a trademark license , the court may render a judgment awarding damages not more than RMB 3.0 million.

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Selling goods without awareness of such goods infringement of the exclusive right to use a trademark shall be exempted from liability for compensation insofar as the seller is able to prove that the goods were lawfully obtained and can indicate the supplier s identity.

We have registered our logos as trademarks in China, including Lightinthebox and ouku.

Domain Names

In September 2002, China Internet Network Information Center, or the CNNIC, issued the Implementing Rules for Domain Name Registration setting forth detailed rules for registration of domain names. On November 5, 2004, Ministry of Industry and Information Technology of the People s Republic of China, or the MIIT, promulgated the Measures for Administration of Internet Domain Names for the Chinese Internet of China, or Domain Name Measures. The Domain Name Measures regulate the registration of domain names, such as the first tier domain name .cn. In 2009, China Internet Network Information Center, or the CNNIC, issued the Implementing Rules for Domain Name Registration setting forth detailed rules for registration of domain names, which was amended in 2012. In September 2002, CNNIC issued the Measures on Domain Name Disputes Resolution and its procedure rules, or Domain Name Disputes Resolutions Measures and Procedure Rules of Domain Name Disputes Resolutions Measures, both of which were amended in 2006 and further amended in 2012. Pursuant to Domain Name Disputes Resolutions Measures, which CNNIC can authorize a domain name dispute resolution institution to decide disputes. These regulations require owners of Internet domain names to register their domain names with qualified domain name registrars approved by the MIIT and obtain registration certificates from such registration agencies. A registered domain name owner has the exclusive right to use its domain name. Unregistered domain names may not receive proper legal protections and may be misappropriated by unauthorized third parties.

We and our VIEs have registered domain names for all of our websites, including *www.lightinthebox.com , www.ouku.com and www.miniinthebox.com.*

Regulations Relating to Foreign Currency Exchange

Foreign Exchange Relating to Export Businesses

Foreign exchange activities relating to import and export trading in China are primarily governed by the following regulations:

- the Foreign Exchange Administration Rules (2008), or the Exchange Rules;
- the Administration Rules for the Settlement, Sale and Payment of Foreign Exchange (1996), or the Administration Rules; and

- Circular of the State Administration of Foreign Exchange on Standardizing the Verification of Electronic Receipt and Payment Documents for Trade in Goods.

These foreign exchange regulations, along with certain other ancillary notices issued by the SAFE, lay out the legal framework for the administration of foreign exchange for the export of commodities in international trade. Under these foreign exchange regulations, the exporter, in order to receive the proceeds of the export in foreign exchange and settle the same into Renminbi, must apply with the local branch of the SAFE for a certificate of verification and cancellation of export proceeds in foreign exchange unless otherwise provided under the applicable laws and regulations The exporter must also apply with the competent tax authorities for a tax exemption or refund where a tax exemption refund is applicable.

We source many of our products from suppliers in the PRC. Our payments are in most cases made to the suppliers entities located in Hong Kong and in some cases are made to sourcing agents located in Hong Kong for further settlement with our suppliers. Our payments are made directly to such Hong Kong entities and thus are not subject to the PRC foreign exchange laws and regulations. Following receipt of the payment in foreign exchange either from the agents to the PRC suppliers or from suppliers own entities located in Hong Kong to the suppliers entities in mainland China, the PRC suppliers shall go through the relevant procedures with the local branch of the SAFE as mentioned above to settle the foreign exchange into Renminbi. However, we cannot assure you that all our sourcing agents or the PRC suppliers will fully comply with these foreign exchange laws and regulations.

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Foreign Exchange Relating to FIEs

Under current Chinese regulations, Renminbi are freely convertible for trade and service-related transactions denominated in foreign currency, but not for direct investment, loans or investments in securities outside China without the prior approval of the SAFE or its local branches.

FIEs in China may execute foreign exchange transactions without the SAFE approval for trade and service-related transactions denominated in foreign currency by providing commercial documents evidencing these transactions. They may also retain foreign currency, subject to a cap approved by the SAFE, to satisfy foreign currency-denominated liabilities or to pay dividends. Foreign exchange transactions related to direct investment, loans and investment in securities outside China are still subject to limitations and require approval from the SAFE.

On March 30, 2015, SAFE issued the SAFE Circular 19, which became effective on June 1, 2015. Pursuant to SAFE Circular 19, foreign-invested enterprises may either continue to follow the current payment-based foreign currency settlement system or choose to follow the conversion-at-will system for foreign currency settlement. Where a foreign-invested enterprise follows the conversion-at-will system for foreign currency settlement, it may convert part or all of the amount of the foreign currency in its capital account into Renminbi at any time. The converted Renminbi will be kept in a designated account labeled as settled but pending payment, and if the foreign-invested enterprise needs to make payment from such designated account, it still needs to go through the review process with its bank and provide necessary supporting documents. SAFE Circular 19, therefore, has substantially lifted the restrictions on the usage by a foreign-invested enterprise of its Renminbi registered capital converted from foreign currencies. As SAFE Circular 19 was promulgated recently, there remains substantial uncertainties with respect to the interpretation and implementation of this circular by relevant authorities.

Regulations on Dividend Distributions

The principal regulations governing dividend distributions of wholly foreign owned companies in China include:

- the Companies Law (2013);
- the Wholly Foreign Owned Enterprise Law (2016); and
- the Wholly Foreign Owned Enterprise Law Implementing Rules (2014).

Under these regulations, wholly foreign owned companies in China may pay dividends only out of their accumulated profits, if any, as determined in accordance with PRC accounting standards and regulations. In addition, wholly foreign owned companies are required to set aside at least 10% of their respective accumulated profits each year, if any, to fund certain reserve funds, until the aggregate amount of these funds reaches 50% of the company s registered capital. Wholly foreign owned companies may, at their discretion, allocate a portion of their after-tax

profits based on PRC accounting standards to staff welfare and bonus funds. These reserve funds and staff welfare and bonus funds are not distributable as cash dividends.

Regulations on Tax

PRC Enterprise Income Tax

The PRC enterprise income tax is calculated based on the taxable income determined under the applicable Enterprise Income Tax Law and its implementation rules. On March 16, 2007, the National People s Congress of China enacted the New EIT Law, which became effective on January 1, 2008. On December 6, 2007, the State Council promulgated the implementation rules to the New EIT Law, which also became effective on January 1, 2008. On December 26, 2007, the State Council issued the Notice on Implementation of Enterprise Income Tax Transition Preferential Policy under the New EIT Law, or the Transition Preferential Policy Circular, which became effective simultaneously with the New EIT Law. The New EIT Law imposes a uniform enterprise income tax rate of 25% on all resident enterprises in China, including FIEs and domestic enterprises, unless they qualify for certain exceptions, and terminates most of the tax exemptions, reductions and preferential treatments available under the old Enterprise Income Tax Law and regulations. Under the New EIT Law and the Transition Preferential Policy Circular, qualified enterprises established before March 16, 2007 that already enjoyed preferential tax treatments will continue to enjoy them (i) in the case of preferential tax rates, for a maximum of five years starting from January 1, 2008 and during the five-year period, the tax rate will gradually increase from their current preferential tax rate to 25%, or (ii) in the case of preferential tax exemption or reduction for a specified term, until the expiration of such term. For enterprises that are not profitable enough to enjoy the preferential tax exemption or reduction referred to in (ii) above, the preferential duration shall commence from 2008.

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Prior to the effectiveness of the New EIT Law on January 1, 2008, domestic companies were generally subject to an enterprise income tax at a statutory rate of 33%.

The New EIT Law and its implementation rules permit high and new technology enterprises strongly supported by the state holding independent ownership of core intellectual property and meeting certain other criteria, as stipulated in the implementation rules and other regulations, to enjoy a reduced enterprise income tax rate of 15%. The State Administration of Taxation, the Ministry of Science and Technology and the Ministry of Finance jointly issued the Administrative Rules for the Certification of High and New Technology Enterprises delineating the specific criteria and procedures for the certification of high and new technology enterprises on April 14, 2008. The New EIT Law and its implementation rules also provide that software enterprises enjoy a two-year income tax exemption starting from the first profit making year, followed by a reduced tax rate of 12.5% for the subsequent three years.

Uncertainties exist with respect to how the New EIT Law applies to our tax residency status. Under the New EIT Law, an enterprise established outside of the PRC with de facto management bodies within the PRC is considered a resident enterprise, which means that it can be treated in a manner similar to a Chinese enterprise for enterprise income tax purposes, although the dividends paid to one resident enterprise from another may qualify as tax-exempt income. Though the implementation rules of the New EIT Law define 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 only detailed guidance currently available for the definition of de facto management body as well as the determination of an offshore incorporated PRC tax resident and its administration are set forth in Circular 82 and Bulletin No. 45 issued by the SAT, which provide guidance on the administration as well as determination of the tax residency status of a Chinese-controlled offshore-incorporated enterprise, defined as an enterprise that is incorporated under the law of a foreign country or territory and that has a PRC company or PRC corporate group as its primary controlling shareholder. Although we do not have a PRC enterprise or enterprise group as our primary controlling shareholder and are therefore not a Chinese- controlled offshore-incorporated enterprise within the meaning of Circular 82, in the absence of guidance specifically applicable to us, we have applied the guidance set forth in Circular 82 to evaluate the tax residency status of our legal entities organized outside the PRC.

According to Circular 82, a Chinese-controlled offshore-incorporated enterprise will be regarded as a PRC tax resident by virtue of having de facto management body in China and will be subject to PRC enterprise income tax on its global income only if all of the following conditions set forth in Circular 82 are met:

- the primary location of the day-to-day operational management is in the PRC;
- decisions relating to the enterprise s financial and human resource matters are made or are subject to approval by organizations or personnel in the PRC;
- the enterprise s primary assets, accounting books and records, company seals and board and shareholder resolutions are located or maintained in the PRC; and
- 50% or more of voting board members or senior executives habitually reside in the PRC.

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In addition, Bulletin No. 45 provided clarification on the resident status determination, post-determination administration, and competent tax authorities. It also specifies that when provided with a copy of a PRC resident determination certificate from a resident Chinese-controlled offshore- incorporated enterprise, the payer should not withhold 10% income tax when paying certain PRC- sourced income such as dividends, interest and royalties to the Chinese-controlled offshore- incorporated enterprise.

Although both the circular and the bulletin only apply to offshore enterprises controlled by PRC enterprises and not those by PRC individuals, the determination criteria set forth in the circular and administration clarification made in 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 the administration measures should be implemented, regardless of whether they are controlled by PRC enterprises or PRC individuals.

We do not believe that we meet all of the conditions above. We are a company incorporated outside the PRC. As a holding company, our key assets and records, including the resolutions of our board of directors and the resolutions of their respective shareholders, are located and maintained outside the PRC. In addition, we are not aware of any offshore holding companies with a corporate structure similar to ours that has been deemed a PRC resident enterprise by the PRC tax authorities. Therefore, we believe that we should not be treated as a resident enterprise for PRC tax purposes if the criteria for de facto management body as set forth in the Circular 82 were deemed applicable to us. However, as the tax residency status of an enterprise is subject to determination by the PRC tax authorities and uncertainties remain with respect to the interpretation of the term de facto management body as applicable to our offshore entities, we will continue to monitor our tax status. See Item 3. Key Information D. Risk Factors Risks Related to Doing Business in China We may be deemed a PRC resident enterprise under the New EIT Law and be subject to PRC taxation on our income.

Although we believe we are not a PRC resident enterprise for enterprise income tax purposes, substantial uncertainty regarding our status still exists. In the event that our company or our Hong Kong subsidiary is considered to be a PRC resident enterprise, (1) our company or our Hong Kong subsidiary would be subject to the PRC enterprise income tax at the rate of 25% on worldwide income; and (2) dividend income that our Hong Kong subsidiary receives from our PRC subsidiary, however, may be exempt from the PRC withholding tax since such income is exempted under the New EIT Law for PRC resident enterprise recipients. See Item 3. Key Information D. Risk Factors Risks Related to Doing Business in China We may rely on dividends and other cash distributions on equity paid by our subsidiaries to fund future cash and financing requirements we may have, and any limitation on the ability of our subsidiaries to make payments to us could have a material adverse effect on our ability to conduct our businesses.

Pursuant to the Notice on Strengthening Administration of Enterprise Income Tax for Share Transfers by Non-PRC Resident Enterprises, or SAT Circular 698, issued by the State Administration of Taxation in 2009 with retroactive effect from January 1, 2008, if a non-resident enterprise transfers the equity interests of a PRC resident enterprise indirectly by disposing of the equity interests of an overseas holding company without a reasonable commercial purpose then it may be subject to PRC withholding tax at a rate of up to 10% from gains derived from this indirect transfer.

Although the SAT issued the Notice on Several Issues on the Administration of Enterprise Income Tax of Non-PRC Resident Enterprises in 2011, or SAT Circular 24, to provide further clarification on how SAT Circular 698 and its relevant provisions should be implemented, there remain uncertainties as to how reasonable commercial purpose is defined or determined or whether transactions conducted as part of an internal restructuring may be immune to re-characterization. On February 3, 2015, the SAT issued SAT Notice on the Collection of Corporate Income Tax by Indirect Transfer of Assets by Non-Resident Companies, or SAT Circular 7, which attempts to clarify the meaning of reasonable commercial purpose and abolishes certain clauses of both Circular 698 and Circular 24. SAT Circular 7 also expanded the concept of indirect transfer from equity interests to movable and immovable property in China and provides safe harbor rules for the public trading of shares in a listed company holding taxable China assets and for indirect transfers resulting from a corporate restructuring. Further, SAT Circular 7 replaces the compulsory reporting requirement set forth in SAT Circular 698 with a voluntary reporting regime. SAT Circular 7 provides that, where an

indirect transfer occurs, both parties to the indirect transfer must submit the relevant documents to the competent tax authority for tax filing purposes, and enterprise income tax will be payable after the share transfer agreement comes into effect and the registration of the share transfers is completed. Indirect transfers occurring before SAT Circular 7 but for which tax matters have not been resolved will be governed by SAT Circular 7. SAT Circular 7 is new and there are still uncertainties as to its interpretation and implementation. It brings challenges to both the foreign transferor and transferee of the indirect transfer as they are required to make self-assessment on whether the transaction should be subject to PRC tax and to file or withhold the PRC tax accordingly. Further, the PRC tax authorities have discretion under SAT Circular 698 and SAT Circular 7 to make adjustments to the taxable capital gains based on the difference between the fair value of the equity interests transferred and the cost of investment.

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Value Added Tax

Our PRC subsidiary, VIEs and Shanghai Ouku are subject to value added tax, or VAT, at a rate of 17% on revenue from sale of products in the PRC and is entitled to a refund for VAT already paid or borne on the goods purchased by it and utilized in the production of goods that have generated gross sales proceeds.

Dividends Withholding Tax

Under the old Enterprise Income Tax Law effective prior to January 1, 2008, dividends paid to foreign investors by FIEs would be exempt from PRC withholding tax. We are a Cayman Islands holding company and substantially all of our income may come from dividends we receive from our subsidiary, Light In The Box Limited, a Hong Kong registered company and its PRC subsidiary and VIEs. Approximately 0.1% of our total net revenues in 2016 was generated from product sales via our websites and third-party online marketplace platforms targeting consumers in China. Pursuant to the New EIT Law and its implementation rules, dividends generated after January 1, 2008 and distributed to us by Lanting Jishi, our PRC subsidiary directly held by Light In The Box Limited, may be subject to withholding tax at a rate of up to 10%. Pursuant to the Double Taxation Avoidance Arrangement, dividends that Light in The Box Limited receives from Lanting Jishi may be subject to withholding tax at a rate of 5%, provided that the conditions and requirements under the Double Taxation Avoidance Arrangement have been satisfied, and subject to the assessment and approval of our relevant local tax authority.

Regulations on Offshore Investment by PRC Residents

On July 4, 2014, the SAFE promulgated the Notice on Relevant Issues Concerning Foreign Exchange Control of Domestic Residents Overseas Investment and Financing and Roundtrip Investment through Offshore Special Purpose Vehicles, or SAFE Circular 37, which replaced the former Notice on Relevant Issues Concerning Foreign Exchange Administration for PRC Residents to Engage in Financing and Inbound Investment via Overseas Special Purpose Vehicles, or SAFE Circular 75, promulgated by the SAFE in 2005.

SAFE Circular 37 requires PRC residents to register with local branches of SAFE in connection with their direct establishment or indirect control of an offshore entity, for the purpose of overseas investment and financing, with such PRC residents legally owned assets or equity interests in domestic enterprises or offshore assets or interests, which is referred to in SAFE Circular 37 as a special purpose vehicle. SAFE Circular 37 further requires amendment to the registration in the event of any significant changes with respect to the special purpose vehicle, such as an increase or decrease of capital contributed by PRC residents, share transfer or exchange, merger, division or other material events. In the event that a PRC resident holding interests in a special purpose vehicle fails to complete the required SAFE registration, the PRC subsidiaries of that special purpose vehicle may be prohibited from making profit distributions to the offshore parent and from carrying out subsequent cross-border foreign exchange activities, and the special purpose vehicle may be restricted in its ability to contribute additional capital into its PRC subsidiaries. Furthermore, failure to comply with the various SAFE registration requirements described above could result in liability under PRC law for evasion of foreign exchange controls. See Item 3. Key Information D. Risk Factors Risks Related to Doing Business in China PRC regulations relating to the establishment of offshore special purpose companies by PRC domestic residents and registration requirements for employee stock ownership plans or share option plans may subject our PRC resident beneficial owners or the plan participants to personal liability, limit our ability to inject capital into our PRC subsidiary, limit our PRC subsidiary s ability to increase its registered capital or distribute profits to us, or may otherwise adversely affect us.

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In addition, PRC subsidiaries of an offshore special purpose company are required to coordinate and supervise the filing of foreign exchange registrations by the offshore holding company s shareholders who are PRC residents in a timely manner. If these shareholders fail to comply, the PRC subsidiaries of the offshore parent company may be prohibited from distributing their profits and proceeds from any reduction in capital, share transfer or liquidation to their offshore parent company and the offshore parent company may be restricted in its ability to contribute additional capital into its PRC subsidiaries. Moreover, failure to comply with the above foreign exchange registration requirements could result in liabilities for such PRC subsidiaries under PRC laws for evasion of foreign exchange restrictions, including (i) requirement by the SAFE to return the foreign exchange remitted overseas within a period specified by the SAFE, with a fine of up to 30% of the total amount of foreign exchange remitted overseas and deemed evasive and (ii) in circumstances involving serious violations, a fine of no less than 30% of and up to the total amount of remitted foreign exchange deemed evasive. Furthermore, the persons-in-charge and other persons at such PRC subsidiaries who are held directly liable for the violations may be subject to administrative sanctions.

Regulations on Employee Stock Option Plans

In December 2006, the People s Bank of China promulgated the Administrative Measures of Foreign Exchange Matters for Individuals, setting forth the respective requirements for foreign exchange transactions by individuals (both PRC and non-PRC citizens) under either the current account and the capital account. In January 2007, the SAFE issued implementing rules for the Administrative Measures of Foreign Exchange Matters for Individuals, which, among other things, specified the approval requirements for certain capital account transactions, such as a PRC citizen s participation in employee stock ownership plans or share option plans of overseas listed companies. On March 28, 2007, the SAFE promulgated the Stock Option Rules. In February 2012, the SAFE promulgated the Stock Option Notice. This Stock Option Notice replaced the previous Stock Option Rules. The Stock Option Notice simplifies the requirements and procedures for the registration of stock incentive plan participant, especially in respect of the required application documents and the absence of strict requirements on offshore and onshore custodian banks, as were stipulated in the Stock Option Rules. The purpose of the Stock Option Notice is to regulate the foreign exchange administration of PRC resident individuals who participate in employee stock incentive plans of overseas listed companies.

According to the Stock Option Notice, if a PRC resident individual participates in stock incentive plans of an overseas listed company, which includes employee stock ownership plan share option plan and other incentive plans permitted by relevant laws and regulations, a PRC domestic qualified agent or the PRC subsidiary of such overseas listed company must, among other things, file, on behalf of such resident, an application with the SAFE or its local counterpart to obtain approval for an annual allowance with respect to the purchase of foreign exchange in connection with stock holding or share option exercises as PRC resident individuals may not directly use overseas funds to purchase shares or exercise share options. With the approval from the SAFE or its local counterpart, the PRC domestic qualified agent or the PRC subsidiary shall open a special foreign exchange account at a PRC domestic bank to hold the funds required in connection with the stock purchase or option exercise, any returned principal or profits upon sales of shares, any dividends issued on the stock and any other income or expenditures approved by the SAFE or its local counterpart. In addition, within three months after any substantial changes to any such stock incentive plan, including, for example, any changes due to a merger or acquisition or changes to the domestic or overseas custodian agent, the domestic agent must update the registration with SAFE.

Under the Foreign Currency Administration Rules (1996), as amended in 2008, the foreign exchange proceeds of domestic entities and individuals can be remitted into China or deposited abroad, subject to the terms and conditions to be issued by the SAFE. However, to date, the SAFE has not issued any implementing rules in respect of depositing the foreign exchange proceeds abroad. Currently, the foreign exchange proceeds from the sales of shares 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 share options are exercised on a noncash basis, the PRC domestic individuals are required to remit the proceeds to special foreign exchange accounts.

Furthermore, a notice concerning the individual income tax on earnings from employee stock options jointly issued by the Ministry of Finance and the SAT, and its implementing rules, provide that domestic companies that implement employee share option programs shall (1) file the employee share option plans and other relevant documents to the local tax authorities having jurisdiction over them before implementing such employee share option plans; (2) file share option exercise notices and other relevant documents with the local tax authorities having jurisdiction over them before exercise by the employees of the share options and clarify whether the shares issuable under the employee share options mentioned in the notice are the shares of publicly listed companies; and (3) withhold taxes from the PRC employees in connection with the PRC individual income tax.

On October 27, 2008, our board of directors adopted the Amended and Reinstated 2008 Share Incentive Plan, pursuant to which we may issue employee stock options to our qualified employees and directors on a regular basis. We and our PRC employees who have participated in the Amended and Reinstated 2008 Share Incentive Plan are subject to the Stock Option Rules as our company is an overseas listed company. However, we cannot assure you that our PRC individual beneficiary owners and the stock options holders can successfully register with the SAFE in full compliance with Stock Option Rules. See Item 3. Key Information D. Risk Factors Risks Related to Doing Business in China PRC regulations relating to the establishment of offshore special purpose companies by PRC domestic residents and registration requirements for employee stock ownership plans or share option plans may subject our PRC resident beneficial owners or the plan participants to personal liability, limit our ability to inject capital into our PRC subsidiary, limit our PRC subsidiary ability to increase their registered capital or distribute profits to us, or may otherwise adversely affect us.

Labor Laws and Social Insurance

Pursuant to the PRC Labor Law and the PRC Labor Contract Law, employers must execute written labor contracts with full-time employees in order to establish an employment relationship. All employers must compensate their employees equal to at least the local minimum wage standards. All employers are required to establish a system for labor safety and sanitation, strictly abide by state rules and standards and provide employees with appropriate workplace safety training. Violations of the PRC Labor Contract Law and the PRC Labor Law may result fines or other administrative sanctions or, in the case of serious violations, criminal liability.

In addition, employers in China are obliged to provide employees with welfare schemes covering pension insurance, unemployment insurance, maternity insurance, work-related injury insurance, medical insurance and housing funds.

Regulations on Overseas Listing

In 2006, six PRC regulatory agencies jointly adopted the Regulations on Mergers and Acquisitions of Domestic Enterprises by Foreign Investors, or the M&A Rules. This rule requires that, if an overseas company established or controlled by PRC domestic companies or citizens intends to acquire equity interests or assets of any other PRC domestic company affiliated with the PRC domestic companies or citizens, such acquisition must be submitted to the Ministry of Commerce, rather than local regulators, for approval. In addition, this regulation requires that an overseas special purpose vehicle, or SPV, formed for overseas listing purposes and controlled by PRC companies or individuals, to obtain the approval of CSRC prior to publicly listing their securities on an overseas stock exchange.

While the application of the new regulations remain unclear, based on their understanding of current PRC laws, regulations and new procedures announced on September 21, 2006, our PRC counsel, TransAsia Lawyers, has advised us that:

- the CSRC currently has not issued any definitive rule or interpretation concerning whether offerings like ours are subject to this regulation;

- we established our PRC subsidiary by means of direct investment other than by merger or acquisition of the equity or assets of PRC domestic companies; and

- no provision in this regulation clearly classified contractual arrangements as a type of transaction subject to its regulation.

See Item 3. Key Information D. Risk Factors Risks Related to Doing Business in China Failure to obtain prior approval required under the M&A Rules and/or any other regulations promulgated by relevant PRC regulatory agencies in the future could have a material adverse effect on our business, financial condition and results of operations as well as the trading price of the ADSs.

Regulations on Concentration in Merger and Acquisition Transactions

The M&A Rules also establish procedures and requirements that could make some merger and acquisitions of Chinese companies by foreign investors more time-consuming and complex. These rules require, among other things, that the Ministry of Commerce be notified in advance of any change-of-control transaction in which a foreign investor will take control of a PRC domestic enterprise or a foreign company with substantial PRC operations, if certain thresholds under the Provisions on Thresholds for Prior Notification of Concentrations of Undertakings issued by the State Council on August 3, 2008 are triggered.

According to the Implementing Rules Concerning Security Review on the Mergers and Acquisitions by Foreign Investors of Domestic Enterprises issued by the Ministry of Commerce in August 2011, mergers and acquisitions by foreign investors involved in an industry related to national security are subject to strict review by the Ministry of Commerce. These rules also prohibit any transactions attempting to bypass such security review, including controlling entities through contractual arrangements.

C. Organizational Structure

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

(1) Such arrangements include exclusive technical and consulting service agreements, business operation agreements, equity disposal agreements, share pledge agreements, powers of attorney, spousal consent letters (applicable only to Lanting Huitong) and a loan agreement (applicable only to Lanting Gaochuang).

(2) Include five subsidiaries each of which is a limited liability company incorporated in Hong Kong that are primarily engaged or expected to be engaged in the wholesale distribution of products. These five subsidiaries are Light Square, Light Hill, Light Linnet, Light Xiao and Fashion Easy-go. Light In The Box Limited is the beneficial owner of each of these companies. The entire share capital of each of these subsidiaries are registered in the name of our employees who hold such shares on trust for the benefit of Light In The Box Limited pursuant to the respective declaration of trust executed on various dates in June and July of 2016. As of the date of this annual report, the business operations of each of Light Hill, Light Linnet, Light Xiao and Fashion Easy-go remain inactive.

(3) Mr. Quji (Alan) Guo holds the other 51% of the equity interest in Lanting Gaochuang.

(4) The shareholders of Lanting Huitong are Mr. Quji (Alan) Guo, our co-founder, chairman and chief executive officer, Mr. Liang Zhang, our co-founder and executive vice president, and Mr. Xin (Kevin) Wen, our co-founder and advisory consultant. In April 2014, one of our co-founders, Mr. Jun Liu has entered into an equity transfer agreement to transfer his shares of Lanting Huitong to Mr. Quji (Alan) Guo, Mr. Xin (Kevin) Wen and Mr. Liang Zhang. We have completed the registration of this transfer with the local branch of the SAIC.

Contractual Arrangements Among Lanting Jishi, our VIEs and the Respective Shareholders of our VIEs

Foreign ownership of Internet-based businesses is subject to significant restrictions under current PRC laws and regulations. The PRC government regulates Internet access and the distribution of online information through strict business licensing requirements and other government regulations. Under prior laws, foreign investors outside of the China (Shanghai) Pilot Free Trade Zone (subject to certain conditions) are not allowed to own more than 50% of the equity interests in a value-added telecommunications service provider, and any such foreign investor must have experience in providing value-added telecommunications services overseas and maintain a good track record. In March 2015, the National Development and Reform Commission and the Ministry of Commerce issued the updated Catalogue, which further relaxed market access restrictions. Among these changes, foreign investors will now be allowed to own up to 100% of the equity interests in an e-commerce business. However, such foreign investor must have experience in providing value-added telecommunications services overseas and maintain a good track record. We are a Cayman Islands company and our wholly owned PRC subsidiary, Lanting Jishi, is a wholly foreign owned enterprise and is restricted from holding the relevant licenses that are essential to the operations of our PRC business. Accordingly, we conduct the operation of our domestic websites in China primarily through Lanting Huitong, which we control through a series of contractual arrangements, and its subsidiary, Shanghai Ouku. The registered shareholders of Lanting Huitong are our co-founders, including Mr. Quji (Alan) Guo, Mr. Xin (Kevin) Wen and Mr. Liang Zhang. In April 2014, one of our co-founders, Mr. Jun Liu has entered into an equity transfer agreement to transfer his shares of Lanting Huitong to Mr. Quji (Alan) Guo, Mr. Xin (Kevin) Wen and Mr. Liang Zhang. We have completed the registration of this transfer with the local branch of the SAIC and Mr. Quji (Alan) Guo, Mr. Xin (Kevin) Wen and Mr. Liang Zhang currently hold 42.14%, 28.93% and 28.93% of the equity interests of Lanting Huitong, respectively.

We conduct certain research and development functions through Lanting Gaochuang, which we control through similar contractual arrangements. Mr. Quji (Alan) Guo and Lanting Huitong hold 51% and 49% of Lanting Gaochuang, respectively. Lanting Gaochuang s ownership structure enables it to join a special economic zone within the Wangjing Hi-Tech Industry Zone, the China Beijing Wangjing Overseas Students Pioneer Park, or the Wangjing Pioneer Park, which is reserved for domestic enterprises that are held by Chinese nationals who have previously studied overseas. As Lanting Gaochuang is majority-owned by Mr. Guo, a Chinese national who has studied overseas, Lanting Gaochuang enjoys certain benefits provided by the Wangjing Pioneer Park, which include reduced rents and other benefits aimed to encourage the development of technically innovative companies. In addition, Lanting Gaochuang was qualified as a software enterprise in 2012, 2013 and 2014 which entitles it to certain tax benefits. See Item 4. Information on the Company B. Business Overview Regulation Regulations on Tax PRC Enterprise Income Tax for more information regarding tax benefits provided to software enterprises.

Through contractual arrangements with our VIEs and their respective shareholders, we receive substantially all of the economic benefits of our VIEs as their primary beneficiary. The financial results of our VIEs are consolidated into our financial statements despite the lack of our equity interest in them. We did not derive consolidated net revenues from Lanting Huitong and Shanghai Ouku from 2014 to 2016. We have not derived any consolidated net revenues from Lanting Gaochuang since its inception in December 2011, and we do not expect to derive any significant contributions to our consolidated net revenues from Lanting Gaochuang going forward, if at all. We believe the consolidation is necessary to fairly present the financial position and results of operations of our company because of the existence of a parent-subsidiary relationship through contractual arrangements, which enables us to:

- exercise effective control over our VIEs;
- receive substantially all of the economic benefits from our VIEs; and
- have an exclusive option to purchase all or part of the equity interest in our VIEs when and to the extent permitted by PRC law.

The following is a summary of the currently effective contractual arrangements among Lanting Jishi, our VIEs, and the shareholders of our VIEs:

Agreements that provide Lanting Jishi effective control over the VIEs

Powers of attorney: Each registered shareholder of our VIEs has executed a power of attorney appointing Lanting Jishi to be his or her attorney, and irrevocably authorizing them to vote on his or her behalf on all of the matters concerning our VIEs that may require shareholders approval, including nominating and electing directors, general managers and other executive officers. The powers of attorney will be valid as long as the registered shareholders remain as shareholders of our VIEs.

Equity disposal agreements: Under the Equity Disposal Agreements entered into among Lanting Jishi, our VIEs, and the shareholders of our VIEs, Lanting Jishi or its designated party has exclusive options to purchase, when and to the extent permitted under PRC law, all or part of the equity interest in our VIEs. The exercise price for the options to purchase all or part of the equity interest will be the minimum amount of consideration permissible under the then applicable PRC law. The agreements will be valid until Lanting Jishi or its designated party purchases all the shares from shareholders of our VIEs.

Spousal consent letters: Under the spousal consent letters, the spouses of certain shareholders of Lanting Huitong acknowledged that a certain percentage of the equity interest in Lanting Huitong held by and registered in the name of their respective spouse will be disposed of pursuant to the equity disposal agreement and share pledge agreement. These spouses understand that such equity interest is held by their respective spouse on behalf of Lanting Jishi, and they will not take any action to interfere with the disposition of such equity interests, including, without limitation, claiming that such equity interest constitute communal property of marriage. The spousal consent letters will be valid until the liquidation of Lanting Huitong, unless terminated earlier at Lanting Jishi s sole discretion.

Loan agreement: Under the loan agreement entered into in December 2011 between Lanting Jishi and Mr. Quji (Alan) Guo, Lanting Jishi extended a loan in the amount of RMB255,000 ($40,492) to Mr. Guo for his contribution of 51% of the registered capital of Lanting Gaochuang. Under this agreement, Mr. Guo agreed that without prior written consent from Lanting Jishi, Lanting Gaochuang may not enter into any transaction that could materially affect its assets, liabilities, interests or operations, and there will be no earnings distribution in any form by Lanting Gaochuang before such loan has been repaid. Mr. Guo also agreed that at the request of Lanting Jishi, all or part of the equity interests held in Lanting Gaochuang shall be promptly and unconditionally transferred to Lanting Jishi or a designated third party in accordance with PRC law. This loan can only be repaid by transferring all of Mr. Guo s equity interest in Lanting Gaochuang to Lanting Jishi or a third party designated by Lanting Jishi, and submitting all proceeds from such transaction to Lanting Jishi. The loan agreement has a term of ten years and will be extended automatically, unless indicated otherwise by Lanting Jishi in writing three months prior to the expiration date.

Agreements that transfer economic benefits to Lanting Jishi Business operation agreements: Under the Business Operation Agreements entered into among Lanting Jishi, our VIEs, and the shareholders of our VIEs, the registered shareholders of our VIEs and our VIEs agreed that our VIEs may not enter into any transaction that could materially affect their assets, liabilities, interests or operations without prior written consent from Lanting Jishi or other party designated by Lanting Jishi, including entry into any loan or other debtor-creditor relationship with any third party or the making of any equity investment in any third party, the sale or purchase of any asset or right to or from any third party or creation of guarantees or any other security on any of its assets in favor of any third party, or creation of any other obligation on any of its assets. In addition, directors, supervisors, chairman, general managers, financial controllers or other senior managers of our VIEs must be Lanting Jishi s nominees. Furthermore, our VIEs and their registered shareholders have agreed to accept and stringently implement proposals set forth by Lanting Jishi regarding employment and business and financial management. Lanting Jishi is entitled to any dividends declared by our VIEs. The business operation agreements will be valid until the liquidation of our VIEs, unless terminated earlier at Lanting Jishi s sole discretion.

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Exclusive technical support and consulting service agreements: Under the Exclusive Technical Support and Consulting Service Agreements entered into between Lanting Jishi and our VIEs, Lanting Jishi agreed to provide our VIEs with technology support and consulting services, including the maintenance of computer rooms and websites, the provision of technology platforms required for operations, provision and maintenance of office networks, the conception, configuration, design, updating and maintenance of web pages, the maintenance of customer service platforms, employee training, advertisements, publicity and promotions, and provision of logistics support for product sales and services. Our VIEs agreed to pay a service fee equal to substantially all of their net income, an amount equivalent to the amount of the respective VIEs operating revenue for the then current quarter after the deduction of: (1) working capital necessary for the maintaining of the daily operations of the respective VIEs; and (2) the amount of cash required for the respective VIEs capital expenditures. The exclusive technical support and consulting service agreements will be valid until the liquidation of our VIEs, unless terminated earlier at Lanting Jishi s sole discretion.

Share pledge agreements: Under the Share Pledge Agreements entered into among Lanting Jishi, our VIEs, and the shareholders of our VIEs, the registered shareholders of our VIEs pledged all of their respective equity interest in favor of Lanting Jishi to secure our VIEs and their shareholders obligations under the various contractual agreements, including the business operation agreements and the exclusive technical support and consulting service agreements described above. If our VIEs or any of their respective registered shareholders breach any of their respective contractual obligations under these agreements, Lanting Jishi, as pledgee, will be entitled to certain rights, including the right to sell the pledged equity interest. The registered shareholders of our VIEs agreed not to transfer, sell, pledge, dispose of or otherwise create any new encumbrance on their respective equity interest in our VIEs, without Lanting Jishi s prior written consent. Unless terminated at Lanting Jishi s sole discretion, the share pledge agreements will be valid until our VIEs and their shareholders fulfill all contractual obligations under the business operation agreements, the exclusive technical support and consulting service agreements and the equity disposal agreements. Our PRC counsel, TransAsia Lawyers, has advised us that the pledges on the equity interest of our VIEs were created and are effective as such pledges have already been registered with the relevant local branch of the SAIC in accordance with the PRC Property Rights Law.

Arrangements between our Hong Kong subsidiary, Lanting Jishi and Lanting Huitong

Our Hong Kong subsidiary, Light In The Box Limited, and its PRC subsidiary, Lanting Jishi, have entered into and performed several business information and logistics services agreements, pursuant to which our Hong Kong subsidiary paid service fees to our PRC subsidiary for certain information and logistics services. In addition, our Hong Kong subsidiary and our VIE, Lanting Huitong, entered into and performed a consulting service agreement and several software development service agreements, pursuant to which our Hong Kong subsidiary paid service fees to Lanting Huitong for the consulting and software development services.

D. Property, Plant and Equipment

We currently lease all properties for our operations. Our corporate headquarters are located in Beijing, China. We have established sourcing offices in Beijing, Shenzhen, Guangdong Province, Shanghai, Suzhou, Jiangsu Province, Guangzhou, Guangdong Province, Hangzhou, Zhejiang Province and Yiwu, Zhejiang Province. In addition, we have an overseas office in Seattle, Washington in the United States. We maintain warehouses in Suzhou, Jiangsu Province and Shenzhen, Guangdong Province in China, and had established warehouses in Warsaw, Poland, Hong Kong and Reno, Nevada in the United States. We have also established one photo studio in Beijing. The following table sets forth a summary of our leased properties as of the date of this annual report:

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Location	size (in square meters)	Usage of Property
Beijing	3,837	Office space, data center, sourcing office and photo studio
Shenzhen, Guangdong Province	29,957	Warehouses, sourcing office and office space
Suzhou, Jiangsu Province	20,074	Warehouse and sourcing office
Shanghai	967	Sourcing office and office space
Guangzhou, Guangdong Province	224.5	Sourcing office
Yiwu, Zhejiang Province	122	Sourcing office
Hangzhou, Zhejiang Province	145	Sourcing office
Chengdu, Sichuan Province	531	Office space, data center
Hong Kong	500	Warehouse
Warsaw, Poland	5,271	Warehouse
Amsterdam, Netherlands	32	Office space
Reno, Nevada, United States	2,415	Warehouse
Seattle, Washington, United States	604	Office space

We believe that our existing facilities are adequate for our current business operations and we will be able to enter into lease arrangements on commercially reasonable terms for future expansion.

ITEM 4A. UNRESOLVED STAFF COMMENTS

None.

ITEM 5. OPERATING AND FINANCIAL REVIEW AND PROSPECTS

You should read the following discussion and analysis of our financial condition and results of operations in conjunction with our audited consolidated financial statements and the related notes included elsewhere in this annual report. This discussion contains forward-looking statements that involve risks and uncertainties. Our actual results and the timing of selected events could differ materially from those anticipated in these forward-looking statements as a result of various factors, including those set forth under Item 3. Key Information D. Risk Factors and elsewhere in this annual report.

A. Operating Results

Overview

LightInTheBox is a global online retail company that delivers products directly to consumers around the world. We offer customers a convenient way to shop for a wide selection of products at attractive prices through *www.lightinthebox.com* , *www.miniinthebox.com* and our other websites as well as mobile applications, which are available in 23 major languages and cover more than 80.0% of Internet users globally, according to

Internet World Stats. Our innovative data-driven business model allows us to offer customized products at scale through optimal merchandising, marketing and fulfillment. We have built an effective business model whereby we source many of our products directly from China-based manufacturers and we work closely with them to re-engineer their manufacturing processes to achieve faster time-to-market with a greater variety of products. We acquire customers primarily through the Internet and serve our customers primarily from our cost-effective locations in mainland China and Hong Kong.

Since the launch of *www.lightinthebox.com* in 2007, we have focused on offering products where consumers value increased choice or customization, such as apparel. In 2016, the sale of products from this core product category accounted for 34.1% of our net revenues from product sales. In addition, we also offered a wide range of other products. The products of our core categories generally require design specificity, thus giving us more pricing flexibility and allowing us to capture higher margin potentials. We will continue to focus on expanding our product selections and categories. In recent years, leveraging our growing operation scale, including our established relationships with major international couriers, we also begun to provide logistics and other value-added services, such as marketing services, primarily to small businesses in China and our suppliers.

We have developed a large global customer base since we launched our first website. Our number of customers was approximately 4.9 million in 2016.

We primarily operate our business from mainland China and Hong Kong but have delivered our products to consumers in over 200 countries and territories. In 2016, we derived 49.6% and 26.6% of our total net revenues from Europe and North America, respectively. We established our first warehouse in 2008 in Shenzhen, Guangdong Province. In 2009 and 2013, we established two additional warehouses in Suzhou, Jiangsu Province, and Shenzhen, Guangdong Province, respectively. In March 2014, July 2014 and January 2015, we established our overseas warehouses in Warsaw, Poland, Hong Kong and Reno, Nevada in the United States, respectively. We have also established seven sourcing offices in China located near our suppliers. In addition, we have established LITB, Inc. to serve as our representative office in the United States for marketing and software development and technology support. In September 2014, we have established LITB Netherlands B.V. to serve as our representative office in the Netherlands for marketing in Europe.

Our total net revenues were $382.4 million, $323.8 million and $292.5 million in 2014, 2015 and 2016, respectively. We experienced a net loss of $30.0 million, $39.4 million and $8.7 million in 2014, 2015 and 2016, respectively. We used cash in operating activities of $6.9 million, $37.9 million and $15.3 million in 2014, 2015 and 2016, respectively.

In 2017, we will continue to invest for long-term growth. We expect to continue to expand our product selection and supplier network; broaden the geographical reach of our websites and mobile applications by enhancing our marketing efforts and mobile penetration. Furthermore, we will continue to invest in upgrading our technology and network infrastructure to handle increased traffic and improve our consumer shopping experience. Whilst we still leverage our financial resources to achieve our long-term growth, we anticipate that we may continue to incur losses from operations and net losses in the near future as we grow our business, and it may be difficult for us to make accurate predictions of our future results of operations. See Item 3. Key Information D. Risk Factors Risks Related to Our Business and Industry We have incurred net losses since our inception and experienced negative cash flow from operating activities in the past. We may continue to incur net losses and experience negative cash flow from operating activities and, as a result, we may need to obtain additional capital in the future and Item 3. Key Information D. Risk Factors Risks Related to Our Business and Industry Our limited operating history may make our growth and future prospects uncertain and difficult to evaluate.

Factors Affecting Our Results of Operations

Our business and results of operations are affected by general factors affecting online retail markets around the world. Such factors include:

- the growth of the global economy and of our targeted geographic markets;
- per capita disposable income and consumer spending;
- growth of global Internet penetration and online retail;

- government policies and initiatives in our targeted geographic markets that affect online retail and, in particular, the import of products into their respective countries or regions; and

- overall global consumer perception of consumer goods exported from China.

Unfavorable changes in any of these general industry conditions could materially and adversely affect demand for our products and our results of operations. In addition, our operating results are affected by the following company-specific factors:

- our ability to acquire new customers and increase repeat purchases by customers at reasonable cost;

- our ability to control product sourcing costs, fulfillment and other operating expenses;

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- our product selection and pricing;
- our ability to introduce new product offerings and categories;
- our ability to expand into new geographic markets;
- our ability to enhance our brand; and
- our ability to compete effectively.

Net Revenues

Starting in 2016, we begun reporting our operating results in two operating segments:

- *Product sales.* Our product sales segment is comprised of sales of our products through our websites and mobile applications and other supplemental online outlets. Net revenues from our product sales are recorded less business tax, discounts and allowances; and
- *Services*. Our services segment is comprised of provision of logistics and other value-added services such as marketing services, primarily to small businesses in China and our suppliers.

This new presentation reflects (i) how we manage our business to maximize efficiency in allocating resources and (ii) the expansion of our service business as the revenue contribution from such business started to account for a larger portion of our total net revenues in 2016. We present the segment information after elimination of inter-company transactions. In general, net revenues, and cost of revenues are directly attributable, and are allocated, to each segment.

Our consolidated statements of operations for the years ended December 31, 2014, 2015 and 2016 as presented in this annual report are modified to reflect this new presentation for consistency purposes.

In 2014, 2015 and 2016, we generated total net revenues of $382.4 million, $323.8 million and $292.5 million, respectively. The following table sets forth information of our total net revenues by segment and product category in absolute amounts and as percentages of total net revenues for the periods presented.

	Year Ended December 31,					
	2014		2015		2016	
	(U.S. dollars in thousands, except percentage)					
		% of Total Net Revenues		% of Total Net Revenues		% of Total Net Revenues
Product sales						
Apparel	$ 138,570	36.3	$ 118,673	36.7	$ 89,291	30.5
Other general merchandise(1)	243,712	63.7	193,659	59.8	172,792	59.1
Total product sales	382,282	100.0	312,332	96.5	262,083	89.6
Services	125	0.0	11,431	3.5	30,404	10.4
Total net revenues	382,407	100.0	323,763	100.0	292,487	100.0

(1) Includes products such as small accessories and gadgets, home and garden, electronics and communication devices and others.

We deliver products to consumers in over 200 countries and territories. The following table breaks down our total net revenues by geographic regions as determined by shipping addresses or the addresses of our business customers that we provide services to in absolute amounts and as percentages of total net revenues for the periods presented.

	Year Ended December 31,					
	2014		2015		2016	
	(U.S. dollars in thousands, except percentage)					
		% of Total Net Revenues		% of Total Net Revenues		% of Total Net Revenues
Europe	$ 239,176	62.5	$ 184,057	56.8	$ 145,185	49.6
North America	81,675	21.4	88,790	27.4	77,814	26.6
Other countries	61,556	16.1	50,916	15.8	69,488	23.8
Total net revenues	382,407	100.0	323,763	100.0	292,487	100.0

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Product sales

Since our inception, we have primarily focused on selling apparel and electronics and communications devices. We expect to continue to focus on the growth in sales of apparel and expect that sales of apparel will continue to contribute considerably to our total net revenues in the near future. However, we have also expanded offerings of other products in particularly have increased our focus on small accessories and gadgets and home and garden. We expect our revenues to become more diversified in the future as we grow our business and increase our number of products.

We face seasonality for the sale of our products. For example, during the first quarter of the past several years, we experienced greater demand for our wedding dresses and, during the fourth quarter of the past several years, we experienced a general increase in the demand for our products as a result of holiday shopping.

We have made our websites easily accessible by users on their mobile devices. We have also launched our mobile apps to enhance the mobile shopping experience of our users. As the number of customers making purchases through our mobile apps continues to increase, our mobile revenue increased to 38.4% of net revenues from product sales in 2016, compared with 26.8% and 33.5% in 2014 and 2015, respectively.

We expect our net revenues from product sales to grow in the future as we continue to introduce new products and deepen our penetration of various geographic markets around the world. We also expect to expand our customer base and increase product sales to each customer to drive our growth.

Operating Metrics

We regularly review a number of operating metrics, including the following, to evaluate our performance of product sales, identify trends affecting our business, formulate financial projections and make certain strategic decisions: (i) our number of customers, (ii) net revenues from product sales attributed to repeat customers, (iii) net revenues from product sales attributed to new customers and (iv) the change in net revenues from product sales attributed to repeat customers. The following table sets forth the above metrics for our product sales segment for the periods indicated.

	Year Ended December 31,		
	2014	**2015**	**2016**
	(in thousands, unless otherwise stated)		
Our number of customers	6,113	5,902	4,880
Net revenues from product sales attributed to repeat customers	153,811	141,515	99,854
Net revenues from product sales attributed to new customers	228,470	170,817	162,230
Change in net revenues from product sales attributed to repeat customers (1) (percentage)	56.5	(8.0)	(29.4)

(1) Change in net revenues from product sales attributed to repeat customers refers to, in percentage, the difference between (i) net revenues from product sales attributed to repeat customers for a given period and (ii) net revenues from product sales attributed to repeat customers for the prior period, divided by net revenues from product sales attributed to repeat customers from such prior period.

Services

We also record revenues from the provision of logistics and other value-added services to small businesses in China. Such logistics services include product collection, packaging and labeling, shipment and delivery of products from our warehouses to locations designated by such small business customers. Our other value-added services primarily relates to the provision of marketing services.

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Cost of Revenues and Operating Expenses

The following table sets forth our cost of revenues and operating expenses, both in absolute amounts and as percentages of total net revenues for the periods indicated.

	Year Ended December 31,					
	2014		2015		2016	
	(U.S. dollars in thousands, except percentage)					
		% of Total Net Revenues		% of Total Net Revenues		% of Total Net Revenues
Cost of revenues						
Cost of product sales	$ 236,982	62.0	$ 196,753	60.8	$ 160,566	54.9
Cost of services	113	0.0	10,601	3.2	28,371	9.7
Total cost of revenues	237,095	62.0	207,354	64.0	188,937	64.6
Operating expenses:						
Fulfillment	23,926	6.3	22,419	6.9	17,052	5.8
Selling and marketing	105,186	27.5	91,614	28.3	61,090	20.9
General and administrative	46,916	12.3	41,535	12.8	34,492	11.8
Total operating expenses	176,028	46.1	155,568	48.0	112,634	38.5

Cost of Revenues

Our cost of revenues is comprised of cost of product sales and cost of services.

Our cost of product sales consists primarily of cost of consumer products sold by us and shipping charges, and to a much lesser degree, packaging supplies and inventory write-downs. We write down the cost of slow-moving and broken inventory to the estimated market value based on historical trends for such inventory, inventory aging and historical and forecasted consumer demand and such write-down is recorded as part of cost of product sales. Shipping charges to receive products from our suppliers are included as inventory and recognized as cost of product sales upon the sale of such products. Our cost of product sales as percentage of our total net revenues during a specific period is affected by the composition of the type of products sold during that period.

Our cost of services consists primarily of shipping charges and to a lesser extent, packaging supplies in connection with the provision of such services to small businesses customers. Shipping charges primarily include shipping fees we pay to third-party international couriers and are recognized as cost of services when delivery services are completed.

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Operating Expenses

Fulfillment Expenses. Fulfillment expenses include costs incurred in operating and staffing our warehouses and customer service centers, including (i) costs attributable to buying, receiving, inspecting and warehousing inventories, (ii) picking, packaging, and preparing customer orders for shipment and (iii) payment processing and related transaction costs. Our fulfillment expenses are primarily affected by the cost of personnel at our warehouses and our ability to strengthen our logistic management capabilities and increase our economies of scale as our volume of products shipped increases. As we expanded our warehouse network to accommodate increase in purchase orders and provide better coverage of our target markets, our fulfillment expenses increased in absolute amount. We expect that as our business continues to grow and as we achieve economies of scale, our fulfilment cost as a percentage of our total net revenues will decrease in the future.

Selling and Marketing Expenses. Selling and marketing expenses include marketing program expenses and marketing personnel expenses. Marketing program expenses are comprised of targeted online marketing expenses, such as search engine marketing, display advertising and affiliate marketing program expenses. Marketing personnel expenses are comprised of payroll and related expenses for personnel engaged in selling, marketing and business development, including the execution of search engine optimization and social viral marketing activities. The fluctuation of selling and marketing expenses as a percentage of our total net revenues relates to our business expansion into and the testing of new geographic markets, product categories, marketing channels and promotional activities. In the near term, we expect to focus our selling and marketing efforts on growing our customer base, but we expect our selling and marketing expenses as a percentage of our total net revenues to decrease in the long term as we achieve economies of scale and utilize our selling and marketing channels more efficiently.

General and Administrative Expenses. General and administrative expenses include payroll-related expenses and travel-related expenses for personnel engaged in accounting, finance, tax, legal, human resources and other general corporate functions, as well as costs related to the use of facilities and equipment by these personnel, such as depreciation expenses and rent, professional fees and other general corporate costs. General and administrative expenses also include technology development and related expenses, including payroll-related expenses. In addition, general and administrative expenses include credit losses relating to fraudulent credit card activities which resulted in chargebacks from payment processing agencies. We expect our general and administrative expenses as a percentage of our total net revenues to decrease in the future as we achieve economies of scale.

Share-based Compensation Expenses

The table below shows the effect of the share-based compensation expenses on our operating expense line items for the periods indicated.

	Year Ended December 31,								
	2014			2015			2016		
	(U.S. dollars in thousands, except percentage)								
			% of Total Net Revenues			% of Total Net Revenues			% of Total Net Revenues
Fulfillment	$	46	0.0	$	185	0.0	$	211	0.0

Selling and marketing	231	0.1	580	0.2	458	0.2
General and administrative	2,241	0.6	2,431	0.8	1,648	0.6
Total share-based compensation expenses	2,518	0.7	3,196	1.0	2,317	0.8

We expect to continue to grant share options, restricted shares and other share-based awards under our share incentive plan and incur further share-based compensation expenses in future periods. For information regarding share options and restricted shares granted to our officers and directors, see Share Incentive Plan.

Taxation

Cayman Islands

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 the Cayman Islands. In addition, our payment of dividends, if any, is not subject to withholding tax in the Cayman Islands.

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Hong Kong

Our wholly owned subsidiaries in Hong Kong are subject to the uniform profit tax rate of 16.5% in Hong Kong. Under the Hong Kong tax laws, each of Light In The Box Limited and Lanting International is exempted from the Hong Kong income tax on its foreign-derived income and there are no withholding taxes in Hong Kong on remittance of dividends.

PRC

Our subsidiary and VIE in China are companies incorporated under PRC law and, as such, are subject to PRC enterprise income tax on their taxable income in accordance with the relevant PRC income tax laws.

Under the New EIT Law and its implementation rules, both of which became effective on January 1, 2008, a uniform 25% enterprise income tax rate is generally applicable to both foreign- invested enterprises and domestic enterprises, unless they qualify for certain exceptions.

Lanting Huitong, which was qualified as a software enterprise in 2010 and in 2014, is entitled to enjoy a two-year income tax exemption starting from its first year of profitability, such as in 2010, followed by a reduced tax rate of 12.5% for the subsequent three years. Starting from 2015, Lanting Huitong is subject to a uniform 25% enterprise income tax rate. Lanting Gaochuang, which has been qualified as a software enterprise since 2012, is entitled to enjoy a two-year income tax exemption starting from 2013, its first year of profitability, followed by a reduced tax rate of 12.5% for the subsequent three years.

Under the New EIT Law and its implementation rules, dividends from our PRC subsidiary paid out of profits generated after January 1, 2008, are subject to a withholding tax of 20%, although under the detailed implementation rules to the New EIT Law promulgated by the PRC State Council, the withholding tax rate is 10%, unless there is a tax treaty with China that provides for a different withholding arrangement. Distributions of profits generated before January 1, 2008 are exempt from PRC withholding tax. Pursuant to the Double Taxation Avoidance Arrangement, dividends that Light in The Box Limited receives from Lanting Jishi may be subject to withholding tax at a rate of 5%, provided that the conditions and requirements under the Double Taxation Avoidance Arrangement have been satisfied, and subject to the assessment and approval of our relevant local tax authority.

Under the New EIT 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. Further to Circular 82, on July 27, 2011, the SAT issued Bulletin No. 45 to provide more guidance on the implementation of Circular 82, which took effect on September 1, 2011. Bulletin No. 45 provides clarification on the resident status determination, post-determination administration, and competent tax authorities. It also specifies that when provided with a copy of a Chinese tax resident determination certificate from a resident Chinese-controlled offshore-incorporated enterprise, the payer should not withhold 10% income tax when paying certain Chinese-sourced income such as dividends, interest and royalties to the

Chinese-controlled offshore-incorporated enterprise. Although both the circular and the bulletin only apply to offshore enterprises controlled by PRC enterprises and not those by PRC individuals, the determination criteria set forth in the circular and administration clarification made in 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 the administration measures should be implemented, 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 Item 3. Key Information D. Risk Factors Risks Related to Doing Business in China We may be deemed a PRC resident enterprise under the New EIT Law and be subject to PRC taxation on our income.

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Critical Accounting Policies

We prepare our financial statements in conformity with U.S. GAAP, which requires us to make judgments, estimates and assumptions. 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 our expectations as a result of changes in our estimates.

An accounting policy is considered 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, could materially impact the consolidated financial statements. We believe that the following accounting policies involve a higher degree of judgment and complexity in their application and require us to make significant accounting estimates. The following descriptions of critical accounting policies, judgments and estimates should be read in conjunction with our consolidated financial statements and other disclosures included in this annual report.

Revenue Recognition

Product sales

We make product sales through our websites, mobile applications and supplemental online outlets and we recognize revenues from product sales when the following four revenue recognition criteria are met: persuasive evidence of an arrangement exists, products are delivered and received by the customer, the price to the customer is fixed or determinable and collectability is reasonably assured.

Most of our customers are required to make online payments using their credit cards, debit cards or through third party payment platforms, such as PayPal, WorldPay and Global Collect, when they place purchase orders on our websites and mobile applications. We record the payments as advances from customers on the balance sheet when received. We then utilize delivery service providers, primarily express courier companies, to deliver our products to our customers. Shipping and handling charges to the customers are included in revenues, and our corresponding shipping costs are included in cost of revenues. We recognize the amounts advanced from customers as revenues at the time the end customers receive the products, which is typically within a few days of shipment.

Customers in China can also choose to pay upon the receipt of our products, which is called the cash on delivery, or COD, model. In the COD model, our delivery service providers collect the payments from our customers for us. We record an accounts receivable on the balance sheet when our customers receive their products from our delivery service providers.

We allow customers to return certain goods within a period of time subsequent to the delivery of the goods. The return period varies depending on the product category and reasons for the return, which would range from seven days to 30 days. We estimate return allowances based on product categories and historical experience. The estimation of return allowances is adjusted to the extent that actual returns differ, or are expected to differ. Changes in estimated return allowances are recognized through a cumulative catchup adjustment in the period of change and

will impact the amount of total net revenues in that period. We estimated that approximately 2.9%, 5.5% and 4.7% of our total net revenues in December 2014, 2015 and 2016, respectively, would be returned and made provisions accordingly.

We voluntarily provide discount coupons as sales incentives to potential customers from time to time. These coupons can only be utilized in conjunction with a subsequent purchase and are recorded as a reduction of revenues at the time of use. We also provide discount reward, which may only be used in the future, to customers who have made a current purchase. As the right of receiving future discount does not represent a significant and incremental discount to the customer, the discount is treated as a reduction of revenue when the future transaction takes place.

Promotional items or free products, which cannot be redeemed for cash and always shipped together with current qualified product sales. The cost of these promotional items or free products are recorded as cost of product sales when the revenue of the current qualified product sales is recognized.

We established a membership program for certain of our website whereby a registered member earned certain points for visiting *www.ouku.com* . Points could only be redeemed in connection with a future purchase based on a defined ratio of 100 points to RMB1.00. Such points were charged as costs of product sales at the later of when the incentive was offered and when the related revenue was recognized. Since the points earned were not based on past product sales transactions, no accrual was made at the time when earned by the registered members. This program had been terminated since February 2013.

Certain of our employees register with supplemental online outlets under their own name, as these websites require registration using the identity cards of individuals to sell our products on our behalf. We have contractual arrangements with these employees that require them to transfer payments received for the sale of the products to us. We evaluate the product sales transactions performed by certain employees on our behalf to determine whether to recognize the revenues on a gross or net basis. The determination is based upon an assessment as to whether we act as a principal or agent when selling the products. All revenues involving employees performing product sales transactions on the supplemental online outlets on our behalf are currently accounted for on a gross basis since we are the primary obligor and have general and physical inventory risk, latitude in establishing prices, discretion in supplier selection and the credit risks.

We entered into arrangements with certain suppliers, under which the suppliers store their products at our premises. We record these products as inventory when all liabilities and rights of ownership of the products are passed on to us upon the confirmation of orders by our customers. All of the revenues involving these arrangements are accounted for on a gross basis since we are the primary obligor, have physical inventory risk, retain latitude in establishing prices, exercise discretion in supplier selection and are exposed to credit risks.

Services

We derive services revenue mainly from provision of logistic services to small businesses in China. Service revenue is recognized when persuasive evidence of an arrangement exists, service has been performed, the fee is fixed or determinable and collectability is reasonably assured. Revenue for logistic services are recognized when the packages are delivered to the recipients.

Inventories

Inventories, consisting of products available for sale, are accounted for using the first-in first-out method and are valued at the lower of cost or market value. We maintain low levels of inventories by adopting a frequent procurement strategy with short refill cycles from suppliers. Therefore, our obsolete inventory has been insignificant. In estimating the level of inventory write-down, we consider the nature of each category of our inventory, inventory aging, and historical and forecasted consumer demand. This valuation also requires us to make judgments, based on currently-available information, about the likely method of disposition, such as through product sales to individual customers, returns to product vendors, or liquidations, and expected recoverable values of each disposition category. These assumptions about future disposition of inventory are inherently uncertain. Write-downs are recorded in cost of revenues in the consolidated statements of operation.

Share-based Compensation

Our share-based payment transactions with employees are measured based on the grant date fair value of the equity instrument and recognized as compensation expense over the requisite service period based on the straight-line method, with a corresponding impact reflected in additional paid-in capital.

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In determining the fair value of share options, we have used the binomial option pricing model, with assistance from ValueLink Management Consultants Limited. Under this option pricing model, certain assumptions required in order to determine the fair value of our options, including the risk-free interest rate, the exercise multiple, the expected dividends on the underlying ordinary shares, the fair value of the underlying ordinary shares, and the expected volatility of the price of the underlying ordinary shares for the period before the valuation dates with lengths equal to the contractual term of the options. Risk-free interest rate is estimated based on the yield to maturity of China international government bonds with a maturity period close to the contractual term of the options. Exercise multiple represents the value of the underlying share as a multiple of exercise price of the option which, if achieved, results in exercise of the option. Dividend yield is estimated by us based on its expected dividend policy over the contractual term of the options. Volatility of the underlying ordinary shares during the life of the options is estimated based on the historical stock price volatility of comparable listed companies over a period comparable to the contractual term of the options. Prior to the completion of our IPO, the estimated fair value of the ordinary shares underlying the options as of the respective grant dates was determined based on retrospective valuations. When estimating the fair value of the ordinary shares on the grant dates, we considered a number of factors, including the result of the third-party appraisals prepared by independent valuation firms, and our equity transactions. After our IPO, the fair value of the underlying ordinary shares is estimated based on the closing market price of ADS as of the grant date. Changes in these assumptions could significantly affect the fair value of share options and hence the amount of compensation expense we recognize in our consolidated financial statements.

The fair value of nonvested shares as of the grant date is estimated based on the fair value of our ordinary shares.

Changes in the terms or conditions of share options are accounted as a modification under which we calculate whether there is any excess of the fair value of the modified option over the fair value of the original option immediately before its terms are modified, measured based on the share price and other pertinent factors at the modification date. For vested options, we recognize incremental compensation cost in the period of the modification occurred and for unvested options, we recognize, over the remaining requisite service period, the sum of the incremental compensation cost and the remaining unrecognized compensation cost for the original award on the modification date.

Income Taxes

In preparing our consolidated financial statements, we must estimate our income taxes in each of the jurisdictions in which we operate. We estimate our actual tax exposure and assess temporary differences resulting from different treatment of items for tax and accounting purposes. These differences result in deferred tax assets and liabilities, which we include in our consolidated balance sheet. We must then assess the likelihood that we will recover our deferred tax assets from future taxable income. If we believe that recovery is not likely, we must establish a valuation allowance. To the extent we establish a valuation allowance or increase this allowance, we must include an expense within the tax provision in our consolidated statement of operations.

Management must exercise significant judgment to determine our provision for income taxes, our deferred tax assets and liabilities and any valuation allowance recorded against our net deferred tax assets. We base the valuation allowance on our estimates of taxable income in each jurisdiction in which we operate and the period over which our deferred tax assets will be recoverable. If actual results differ from these estimates or we adjust these estimates in future periods, we may need to establish an additional valuation allowance, which could materially impact our financial position and results of operations.

U.S. GAAP requires that an entity recognize the impact of an uncertain income tax position on the income tax return at the largest amount that is more likely than not to be sustained upon audit by the relevant tax authority. If we ultimately determine that payment of these liabilities will be unnecessary, we will reverse the liability and recognize a tax benefit during that period. Conversely, we record additional tax charges in a period in which we determine that a recorded tax liability is less than the expected ultimate assessment. We did not recognize any significant unrecognized tax benefits during the periods presented in this annual report.

Uncertainties exist with respect to the application of the New EIT Law and its implementation rules to our operations, specifically with respect to our tax residency status. The New EIT Law specifies that legal entities organized outside of the PRC will be considered residents for PRC income tax purposes if their de facto management bodies are located within the PRC. The New EIT Law s 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. On April 22, 2009, 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, was issued. 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. Further the Administrative Measures of Enterprise Income Tax of Chinese controlled Offshore Incorporated Resident Enterprises (Trial), or Bulletin No. 45, took effect on September 1, 2011, and provides more guidance on the implementation of Circular 82. See Item 4. Information on the Company B. Business Overview Regulation Regulations on Tax PRC Enterprise Income Tax.

According to Circular 82, a Chinese-controlled offshore-incorporated enterprise will be regarded as a PRC tax resident by virtue of having a de facto management body in China and will be subject to PRC enterprise income tax on its worldwide income only if all of the following conditions set forth in Circular 82 are met: (i) the primary location of the day-to-day operational management is in the PRC; (ii) decisions relating to the enterprise s financial and human resource matters are made or are subject to approval by organizations or personnel in the PRC; (iii) the enterprise s primary assets, accounting books and records, company seals and board and shareholder resolutions are located or maintained in the PRC; and (iv) at least 50% of voting board members or senior executives habitually reside in the PRC. In addition, Bulletin No. 45 provides clarification in resident status determination, post-determination administration and competent tax authorities. It also specifies that when provided with a copy of a Chinese tax resident determination certificate from a resident Chinese-controlled offshore-incorporated enterprise, the payer should not withhold 10% income tax when paying certain Chinese-sourced income such as dividends, interest and royalties to the Chinese-controlled offshore-incorporated enterprise.

Although both the circular and the bulletin only apply to offshore enterprises controlled by PRC enterprises and not those by PRC individuals, the determination criteria set forth in the circular and administration clarification made in 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 the administration measures should be implemented, regardless of whether they are controlled by PRC enterprises or PRC individuals.

Despite the uncertainties resulting from limited PRC tax guidance on the issue, we do not believe that our legal entities organized outside of the PRC are tax residents under the New EIT Law. If one or more of our legal entities organized outside of the PRC were characterized as PRC tax residents, our results of operations could be materially and adversely affected. See Item 4. Information on the Company B. Business Overview Regulation Regulations on Tax PRC Enterprise Income Tax.

Jumpstart Our Business Startups Act of 2012

Section 107(b) of the Jumpstart Our Business Startups Act of 2012 provides that an emerging growth company can take advantage of the extended transition period provided in Section 7(a)(2)(B) of the Securities Act for complying with new or revised accounting standards. In other words, an emerging growth company can delay the adoption of certain accounting standards until those standards would otherwise apply to private companies. We have elected to take advantage of the extended transition period. Although as of the date of this annual report, we have not delayed the adoption of any accounting standard, as a result of this election, our future financial statements may not be comparable to other public companies that comply with the public company effective dates for new or revised accounting standards.

Results of Operations

The following table sets forth a summary of our consolidated results of operations for the periods indicated. This information should be read together with our consolidated financial statements and related notes included elsewhere in this annual report. The results of operations in any period are not necessarily indicative of the results that may be expected for any future period.

	Year Ended December 31,		
	2014	2015	2016
	(U.S. dollars in thousands, except percentage)		

		% of Net Revenues		% of Net Revenues		% of Net Revenues
Net revenues						
Product sales	$ 382,282	100.0	$ 312,332	96.5	$ 262,083	89.6
Services	125	0.0	11,431	3.5	30,404	10.4
Total net revenues	382,407	100.0	323,763	100.0	292,487	100.0
Cost of Revenues						
Product sales	236,982	62.0	196,753	60.8	160,566	54.9
Services	113	0.0	10,601	3.2	28,371	9.7
Total cost of Revenues	237,095	62.0	207,354	64.0	188,937	64.6
Gross profit	145,312	38.0	116,409	36.0	103,550	35.4
Operating expenses:						
Fulfillment	23,926	6.3	22,419	6.9	17,052	5.8
Selling and marketing	105,186	27.5	91,614	28.3	61,090	20.9
General and administrative	46,916	12.3	41,535	12.8	34,492	11.8
Total operating expenses	176,028	46.1	155,568	48.0	112,634	38.5
Loss from operations	(30,716)	(8.0)	(39,159)	(12.1)	(9,084)	(3.1)
Exchange loss on offshore bank accounts	(1,556)	(0.4)	(938)	(0.3)	(120)	(0.0)
Interest income	2,355	0.6	773	0.2	518	0.2
Loss before income taxes	(29,917)	(7.8)	(39,324)	(12.2)	(8,686)	(3.0)
(Loss) gain from equity method investment			(34)	(0.0)	17	0.0
Income taxes expenses	(70)	(0.0)	(49)	(0.0)	(54)	(0.0)
Net loss	(29,987)	(7.8)	(39,407)	(12.2)	(8,723)	(3.0)

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Comparison of the Years Ended December 31, 2014, 2015 and 2016

Net Revenues

Our total net revenues in 2014, 2015 and 2016 were $382.4 million, $323.8 million and $292.5 million, respectively, reflecting a decrease of 15.3% from 2014 to 2015 and a decrease of 9.7% from 2015 to 2016.

Product sales

The decrease in our net revenues from products sales from $312.3 million in 2015 to $262.1 million in 2016 was primarily due to a decrease in our sales orders resulting from a decrease in our repeat customers from product sales, partially offset by an increase in our unit price per sales order. Our total number of sales orders in 2015 and 2016 was approximately 8.9 million and 6.6 million, respectively, reflecting a decrease of 25.8% from 2015 to 2016. Our number of customers in 2015 and 2016 was approximately 5.9 million and 4.9 million, respectively, reflecting a decrease of 16.9% from 2015 to 2016. Net revenues from product sales attributable to our repeat customers as a percentage of our net revenues from product sales decreased from 45.3% in 2015 to 38.1% 2016. Our unit price per sales order during the same periods, however, increased from approximately $36.4 in 2015 to $39.6 in 2016, reflecting an increase of 8.8% from 2015 to 2016 due to changes in our product mix, enhanced customer satisfaction of our products and improved quality of our supply chain.

The decrease in our net revenues from products sales from $382.3 million in 2014 to $312.3 million in 2015 was due to decreases in (i) our sales orders resulting from decreases in our new and repeat customers from product sales and (ii) our unit price per sales order. Our total number of sales orders in 2014 and 2015 was approximately 9.7 million and 8.9 million, respectively, reflecting a decrease of 8.2% from 2014 to 2015. Our number of customers in 2014 and 2015 was approximately 6.1 million and 5.9 million, respectively, reflecting a slight decrease of 3.3% from 2014 to 2015. Net revenues from product sales attributable to our repeat customers as a percentage of our net revenues from product sales, however, increased from 40.2% in 2014 to 45.3% 2015. Our unit price per sales order during the same periods decreased from approximately $39.4 in 2014 to $36.4 in 2015, reflecting a decrease of 7.6% from 2014 to 2015 due to changes in our product mix.

We have optimized our product listings to offer a more focused variety and choices to our customers, which has allowed us to capture additional customer demand. We have reduced the number of product listings in our existing product categories with increased new product listings each month in 2015 and 2016. As of December 31, 2014, 2015 and 2016, we had more than 764,000, 687,800 and 322,000 product listings, respectively.

We have also increased our customer base by increasing our penetration of various geographic markets. We have initially focused on the North American market prior to 2010 but have since expanded our marketing efforts to increase the sale of our products to customers in Europe and other parts of the world. In each of 2014, 2015 and 2016, Europe represented the largest region in which our products were sold.

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Services

The increase in our net revenues from services from $125 thousand in 2014 to $30.4 million in 2016 was due to the expansion of our logistics services business.

Cost of Revenues

Our cost of revenues in 2014, 2015 and 2016 were $237.1 million, $207.4 million and $188.9 million, respectively, representing a decrease of 12.5% from 2014 to 2015 and a decrease of 8.9% from 2015 to 2016, primarily attributable to decreases in cost of product sales.

Cost of product sales

The decrease in our cost of product sales from $196.8 million in 2015 to $160.6 million in 2016 was primarily due to the decreases in both sales of our products and shipping charges. Our product costs and other associated charges in 2015 and 2016 were $126.5 million and $100.6 million, respectively, representing a decrease of 20.5% from 2015 to 2016. Our shipping charges related to the sale of our products in 2015 and 2016 were $70.3 million and $60.0 million, respectively, representing a decrease of 14.7% from 2015 to 2016.

The decrease in our cost of product sales from $237.0 million in 2014 to $196.8 million in 2015 was primarily due to the decreases in both sales of our products and shipping charges. Our product costs and other associated charges in 2014 and 2015 were $142.6 million and $126.5 million, respectively, representing a decrease of 11.3% from 2014 to 2015. Our shipping charges related to the sale of our products in 2014 and 2015 were $94.4 million and $70.3 million, respectively, representing a decrease of 25.5% from 2014 to 2015.

Cost of services

The increase in our cost of services from $113 thousand in 2014 to $28.4 million in 2016 was due to the increase in costs associated with the increase in our net revenues from services.

Gross Profit

As a result of the foregoing, our gross profits in 2014, 2015 and 2016 were $145.3 million, $116.4 million and $103.6 million, respectively, reflecting a decrease of 19.9% from 2014 to 2015 and a decrease of 11.0% from 2015 to 2016. Our gross margins in 2014, 2015 and 2016 were 38.0%, 36.0% and 35.4%, respectively.

Products sales

The gross profits of our product sales segment in 2014, 2015 and 2016 were $145.3 million, $115.6 million and $101.5 million, respectively, reflecting a decrease of 20.4% from 2014 to 2015 and a decrease of 12.2% from 2015 to 2016. The gross margins of our product sales segment in 2014, 2015 and 2016 remained relatively stable at 38.0%, 37.0% and 38.7%, respectively.

Services

The gross profits of our services segment in 2014, 2015 and 2016 were $12 thousand, $0.8 million and $2.0 million, respectively, reflecting an increase of 656.7% from 2014 to 2015 and an increase of 150.0% from 2015 to 2016. The gross margins of our services segment in 2014, 2015 and 2016 were 9.6%, 7.3% and 6.7%, respectively.

Fulfillment Expenses

Our fulfillment expenses in 2014, 2015 and 2016 were $23.9 million, $22.4 million and $17.1 million, respectively. Fulfillment expenses as a percentage of our total net revenues in 2014, 2015 and 2016 were 6.3%, 6.9% and 5.8%, respectively.

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The decrease in our fulfillment expenses as a percentage of our total net revenues from 2015 to 2016 was due to economics of scales and improved operational efficiency in both our back office and fulfillment centers with the launch of enhanced in-house developed IT systems.

The increase in our fulfillment expenses as a percentage of our total net revenues from 2014 to 2015 was due to the increase in fulfillment personnel compensation and payment processing costs associated with our expansion of overseas fulfillment facilities in Warsaw, Poland, Hong Kong and Reno, Nevada in the United States.

Selling and Marketing Expenses

Our selling and marketing expenses in 2014, 2015 and 2016 were $105.2 million, $91.6 million and $61.1 million, respectively.

Selling and marketing expenses as a percentage of our total net revenues in 2014, 2015 and 2016 were 27.5%, 28.3% and 20.9%, respectively. The decrease in our selling and marketing expenses as a percentage of our total net revenues from 2015 to 2016 was primarily due to economics of scales and our improvements in customer acquisition strategies and techniques which led to higher marketing efficiency. The increase in our selling and marketing expenses as a percentage of our total net revenues from 2014 to 2015 was primarily due to our strengthened marketing efforts to promote our online marketing platforms and to diversify traffic acquisition channels.

General and Administrative Expenses

Our general and administrative expenses in 2014, 2015 and 2016 were $46.9 million, $41.5 million and $34.5 million, respectively, reflecting a decrease of 11.5% from 2014 to 2015 and a decrease of 16.9% from 2015 to 2016. The decrease in our general and administrative expenses from 2014 to 2016 was primarily due to our efforts to streamline organizational structure and to optimize staff allocation. Share-based compensation expenses included in general and administrative expenses in 2014, 2015 and 2016 were $2.2 million, $2.4 million and $1.6 million, respectively.

General and administrative expenses as a percentage of our total net revenues in 2014, 2015 and 2016 were 12.3%, 12.8% and 11.8%, respectively. The decrease in general and administrative expenses as a percentage of total net revenues from 2015 to 2016 was primarily due to our improved economies of scale. The increase in general and administrative expenses as a percentage of total net revenues from 2014 to 2015 was primarily due to our increased investments on technologies and deleverage of economies of scale.

Loss from Operations

As a result of the foregoing, our losses from operations in 2014, 2015 and 2016 were $30.7 million, $39.2 million and $9.1 million, respectively.

Exchange Loss on Offshore Bank Accounts

We recorded exchange loss on offshore bank accounts of $1.6 million, $0.9 million and $0.1 million in 2014, 2015 and 2016, respectively. Such exchange loss was due to the appreciation from 2014 and 2016 of our reporting currency, U.S. dollar, against other major world currencies that our customers used in purchasing our products.

Interest Income

Our interest income was $2.4 million, $0.8 million and $0.5 million in 2014, 2015 and 2016, respectively. Interest income increased in 2014 due to an increase in our average bank deposits. Interest income decreased in 2015 and 2016, primarily due to lower level of deposits as compared to that of previous years.

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Income Taxes Expenses

Our income taxes expenses in 2014, 2015 and 2016 were $70 thousand, $49 thousand and $54 thousand, respectively, primarily attributable to profits made by one of our PRC subsidiaries in the past three years.

Net Loss

As a result of the foregoing, our net losses in 2014, 2015 and 2016 were $30.0 million, $39.4 million and $8.7 million, respectively.

B. Liquidity and Capital Resources

Cash Flow and Working Capital

To date, we have financed our operations primarily through the proceeds from the issuance of our preferred shares and convertible notes and the net proceeds of our initial public offering and subsequent private placements, as well as cash flow generated from operations. As of December 31, 2016, we had approximately $91.1 million in cash and cash equivalents, and restricted cash. In March 2012, we issued convertible notes with an aggregate principal amount of $8.0 million, which were automatically converted into 2,224,610 ordinary shares upon the completion of our initial public offering. In June 2013, we completed our initial public offering, in which we offered and sold 19,090,000 ordinary shares in the form of ADSs, raising $75.0 million in proceeds before expenses to us. In March 2016, we completed the issuance of 42,500,000 ordinary shares to Zall E-Commerce in a private placement transaction, which amounted to $76.5 million in proceeds before expenses to us.

We believe the cash we received from our initial public offerings, private placement in March 2016 and the anticipated cash flow from operations will provide us with sufficient capital to meet the expenses and other expenditures required for our business operations for the 12 months from December 31, 2016. In the event that our operating expenses or other expenditures exceed our working capital, we may seek to issue debt or equity securities or obtain credit facilities. Any issuance of equity securities could cause dilution for our shareholders. Any incurrence of indebtedness could increase our debt service obligations and subject us to restrictive operating and financial covenants. Additionally, financing may not be available to us in amounts or on terms acceptable to us, or at all.

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

	Year Ended December 31,		
	2014	2015	2016
	(U.S. dollars in thousands)		

Net cash used in operating activities	$ (6,889)	$ (37,901)	$ (15,334)
Net cash provided by (used in) investing activities	69,181	3,138	(287)
Net cash (used in) provided by financing activities	(10,420)	(9,224)	74,635
Net increase (decrease) in cash and cash equivalents	51,872	(43,987)	59,014
Effect of exchange rate changes on cash and cash equivalents	(259)	(470)	(398)
Cash and cash equivalents at beginning of the period	23,745	75,358	30,901
Cash and cash equivalents at end of the period	75,358	30,901	89,517

Operating Activities

We experienced negative cash flow from operating activities from 2014 to 2016, primarily attributable to operating loss incurred during the same periods which was a result of changes in our product mix and increases in our operating expenses, and to a lesser extent, increases to our inventory as we expanded our product offerings to provide customers more choices and a better selection.

Net cash used in operating activities was $15.3 million in 2016, primarily attributable to our net loss of $8.7 million, adjusted by the reconciliation of non-cash items of $7.1 million, which mainly included share-based compensation of $2.3 million, depreciation and amortization of $1.4 million, inventory provision of $3.3 million and exchange loss on offshore bank accounts of $0.1 million. Net cash used in operating activities was also attributable to a decrease of $6.8 million in accounts payable and a decrease of $9.0 million in prepaid expenses and other current assets, accounts receivable and inventories which were in connection with cash prepayment for procurement, offset by an increase of $2.1 million in accrued expenses and other current liabilities and advances from customers which were a result of legal, arbitral or administrative proceedings arising in the ordinary course of our business that we may from time to time participate into, and increases in audit fees and other expenses.

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Net cash used in operating activities was $37.9 million in 2015, primarily attributable to our net loss of $39.4 million, adjusted by the reconciliation of non-cash items of $8.2 million, which mainly included share-based compensation of $3.2 million, depreciation and amortization of $2.1 million, inventory provision of $1.9 million and exchange loss on offshore bank accounts of $0.9 million. Net cash used in operating activities was offset by an increase of $4.1 million in accounts payable and an increase of $0.1 million in prepaid expenses and other current assets, which were a result of operating loss in 2015.

Net cash used in operating activities was $6.9 million in 2014, primarily attributable to our net loss of $30.0 million, adjusted by the reconciliation of non-cash items of $7.1 million, which mainly included share-based compensation of $2.5 million, depreciation and amortization of $1.9 million, exchange loss on offshore bank accounts of $1.6 million and inventory provision of $1.2 million. Net cash used in operating activities was partially offset by an increase of $9.5 million in accrued expenses and other current liabilities, an increase of $6.6 million in accounts payable and an increase of $3.6 million in prepaid expenses and other current assets, which were a result of increased business activities that led to increased overhead and orders placed with our suppliers.

Investing Activities

Net cash used in investing activities was $0.3 million in 2016, primarily due to our purchase of property and equipment for our office and information technology infrastructure.

Net cash provided by investing activities was $3.1 million in 2015, primarily due to maturity of term deposits of $43.1 million, which was offset by the purchase of term deposit of $37.7 million and long term investment of $2.1 million in Shantou Demon Network Technology Co. Ltd.

Net cash provided by investing activities was $69.2 million in 2014, primarily due to the maturity of term deposits of $157.5 million, which was offset by the purchase of term deposit of $84.9 million, purchase of property and equipment for our office and information technology infrastructure for $2.6 million and the decrease in restricted cash of $0.9 million.

Financing Activities

Net cash provided by financing activities was $74.6 million in 2016 which was primarily due to net proceeds from private placement by Zall E-Commerce of $75.4 million, offset by the repurchase of our ADSs of $0.8 million.

Net cash used in financing activities was $9.2 million in 2015 which was primarily due to the repurchase of our ADSs of $9.3 million, offset by the proceeds from exercise of shares options of $0.1 million.

Net cash used in financing activities was $10.4 million in 2014 which was primarily due to the repurchase of our ADSs of $10.7 million, offset by the proceeds from exercise of shares options of $0.3 million.

Capital Expenditures

Our capital expenditures amounted to $2.6 million, $0.8 million and $0.3 million in 2014, 2015 and 2016, respectively. Our capital expenditures have historically comprised of leasehold improvements, purchase of equipment for our warehouses and our information technology infrastructure. Our capital expenditures in 2017 is expected to be approximately 0.5 million, which will be primarily used to expand our office and warehouse spaces. Our capital expenditures may increase in the future as we continue to invest in our fulfillment and technology infrastructure.

Holding Company Structure

We are a holding company with no material operations of our own. We conduct our operations primarily through Light In The Box Limited, our Hong Kong subsidiary, and Lanting Jishi, our wholly owned subsidiary in China. Under Hong Kong law, there are no withholding taxes on remittance of dividends. Under PRC law, each of Lanting Jishi, Lanting Huitong, Lanting Gaochuang and Shanghai Ouku is required to set aside at least 10% of its after-tax profits each year, if any, to fund certain statutory reserves until the accumulated amount of such reserves reaches 50% of its respective registered capital. Although the statutory reserves can be used, among other ways, to increase the registered capital and eliminate future losses in excess of retained earnings of the respective companies, the reserve funds are not distributable as cash dividends except in the event of liquidation. Lanting Jishi is permitted to pay dividends to us only out of its retained earnings, if any, as determined in accordance with PRC accounting standards and regulations.

Pursuant to the contractual arrangements among Lanting Jishi and our VIEs, Lanting Jishi can charge our VIEs service fee equal to substantially all of their net income. After paying the withholding taxes applicable to Lanting Jishi s revenue and earnings, making appropriations for its statutory reserve requirement and retaining any profits from accumulated profits, the remaining net profits of Lanting Jishi would be available for distribution to its sole shareholder, Light In The Box Limited, and from Light In The Box Limited to us.

We have not, and do not have any present plan, for our PRC subsidiary, Lanting Jishi, to distribute any dividends. We do not believe our current structure will limit our holding company s ability to timely meet our cash obligations in the near future, as we currently generate and expect to continue to generate the majority of our revenues and receive the majority of our cash from customers outside of China through Light In The Box Limited, our Hong Kong subsidiary. However, if, in the future, we require our PRC subsidiary to distribute dividends to us, restrictions on the distribution of dividends may have an adverse effect on our ability to meet our cash obligations in a timely manner. Please see Item 3. Key Information D. Risk Factors Risks Related to Doing Business in China We may rely on dividends and other cash distributions on equity paid by our subsidiaries to fund and financing requirements we may have, and any limitation on the ability of our subsidiaries payments to us could have a material adverse effect on our ability to conduct our businesses.

Inflation

Inflation in China has not in the past materially impacted our results of operations. However, China has recently experienced a significant increase in inflation levels, which may materially impact our results of operations in the future. According to the National Bureau of Statistics of China, the change of consumer price index in China was 2.0% in 2014, 1.4% in 2015 and 2.0% in 2016.

Recent Accounting Pronouncements

A list of recent accounting pronouncements that are relevant to us is included in note 2 to our consolidated financial statements, which are included in this annual report.

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

Research and Development

We have focused on and will continue to invest in our information technology infrastructure and applications. We have built a proprietary modularized and scalable technology infrastructure, which enables us to quickly expand system capacity and add new features and functionalities in response to our business needs and evolving customer demand without affecting our existing operations or incurring significant costs.

Intellectual Property

We rely on a combination of trademark, trade secret, patent and other intellectual property laws as well as confidentiality agreements with our employees, manufacturers and others to protect our intellectual property. We have registered domain names for all of our websites, including *www.lightinthebox.com, www.ouku.com* and *www.miniinthebox.com*, and trademarks and service marks in China, Hong Kong and the European Union, including for *Lightinthebox* and *MiniInTheBox*. We also have 19 registered computer software copyrights in China and one registered computer software copyright in the United States. In addition, we have filed additional trademark applications in China, Hong Kong, Japan, Korea, Brazil, Russia, Austria, the European Union and the United States, as well as patent applications in China and the United States.

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In addition to the protection of our intellectual property, we are also focused on ensuring that our product offerings do not infringe the intellectual property of others. We have adopted internal policies and guidelines during product design and procurement process to make sure our suppliers and products we offer do not infringe on third-party intellectual property rights. All our supplier agreements contain provisions to safeguard against potential intellectual property infringement by our suppliers and impose severe penalties in the event of any infringement. We will also refuse to work with or terminate our relationship with suppliers in the event of intellectual property right violations. In addition, we have also engaged third-party advisors to assist us in ensuring compliance with third-party intellectual property rights.

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 current fiscal year that are reasonably likely to have a material effect on our total net revenues, income, profitability, liquidity or capital reserves, 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 have not entered into any financial guarantees or other commitments to guarantee the payment obligations of any third parties. In addition, we have not entered into any derivative contracts that are indexed to our shares and classified as shareholders equity or that are not reflected in our consolidated financial statements. Furthermore, we do not have any retained or contingent interest in assets transferred to an unconsolidated entity that serves as credit, liquidity or market risk support to such entity. Moreover, we do not have any variable interest in any unconsolidated entity that provides financing, liquidity, market risk or credit support to us or engages in leasing, hedging or research and development services with us.

F. Tabular Disclosure of Contractual Obligations

We have operating lease agreements for warehouses and offices. Rent expenses under operating leases for the years ended December 31, 2014, 2015 and 2016 were $3.9 million, $4.5 million and $4.2 million, respectively. Future minimum lease payments under non-cancellable operating lease agreements as of December 31, 2016 are as follows:

		(in thousands)
2017	$	3,759
2018		2,448
2019		261
	$	6,468

G. Safe Harbor

See 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. The business address of each of our directors and executive officers is LightInTheBox Holding Co., Ltd., Tower 2, Area D, Diantong Square, No. 7 Jiuxianqiao North Road, Chaoyang District, Beijing 100015, People s Republic of China.

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Name(1)	Age	Position/Title
Quji (Alan) Guo	41	Chairman of the board and chief executive officer
Zhentao Wang	51	Director
Xiongping Yu	41	Director
Zhi Yan	44	Director
Gang Yu	57	Director
Sean Shao	60	Independent director
Kai-Fu Lee	55	Independent director
Xiaoping (Bob) Xu	60	Independent director
Liang Zhang	40	Executive Vice President
Bin (Robin) Lu	47	Chief financial officer
Bin Shi	38	Chief technology officer

Note:

(1) Mr. Xin (Kevin) Wen, our co-founder and former executive vice president, has moved from a management role to an advisory consultant role with our company in 2017 in order to pursue his other personal interests and focuses.

Biographical Information

Quji (Alan) Guo is our co-founder, chairman and chief executive officer who joined our company in 2008. Prior to joining our company, Mr. Guo served as the chief strategist and the special assistant to the president of Google China from 2005 to 2008, where he was instrumental for building Google s China operation and led many of its strategic product and business initiatives, including the launch of Google Music, the first advertiser-sponsored free music download service in China, as well as certain strategic investments. Prior to joining Google China, he was a product manager with Google in the United States. In 2004, he worked for the corporate business development team at Amazon participating in the acquisition of Joyo.com, the predecessor of Amazon s China operation. From 2001 to 2003, he was a software design engineer at the headquarters of Microsoft Corporation, participating in the development of MSN, IE and Windows. Mr. Guo received his bachelor s degree from the University of Science and Technology of China in 1999, his master s degree in electrical engineering from the University of Illinois at Urbana-Champaign in 2001, and his MBA degree from Stanford University in 2005. Mr. Guo is a holder of a number of patents in software and Internet technologies in the United States.

Zhentao Wang has been our director since July 2015. Mr. Wang is the founder and chairman of the board of directors of AoKang. He founded Yongjia County Aolin Shoe Factory, the predecessor of AoKang, in 1988. Mr. Wang received his EMBA degree from Cheung Kong Graduate School of Business in 2006 and also an EMBA degree from the HEC School of Management in France in 2007. Mr. Wang has received numerous accolades and awards in China, including the National Labor Day Award in 2002, China s Industry Leader of Private Industrial Enterprises in 2003, and the Outstanding Person of China s Economic Development in 2006.

Xiongping Yu has been our director since June 2016. Mr. Yu is a director of Aokang and was previously the chief financial officer of Aokang Group Co., Ltd. Mr. Yu received a bachelor s degree from Dongbei University of Finance & Economics in 2005.

Zhi Yan has been our director since March 2016. Mr. Yan is the founder, chief executive officer and co-chairman of the board of directors of Zall Group (HKSE Code: 2098). Mr. Yan has approximately 12 years of experience in the commercial property and wholesale shopping mall industries, as well as approximately 20 years of experience in business management in various industries. Mr. Yan has been appointed as a non-executive director and the chairman of CIG Yangtze Ports PLC (HKSE Code: 8233) since 2011. Mr. Yan received a master s degree in business administration for senior executives from Wuhan University in February 2008 and an executive master of business administration degree at Cheung Kong Graduate School of Management in 2013.

Gang Yu has been our director since March 2016. Dr. Yu is an executive director and co-chairman of the board of directors of Zall Group (HKSE Code: 2098). Dr. Yu has extensive experience in e-commerce and operation and logistics management and has previously served in various positions at multi-national corporations such as Dell Inc. and Amazon.com. Dr. Yu obtained his bachelor degree in science from Wuhan University in 1982 and his master degree in science from Cornell University in 1985. Dr. Yu received his Ph.D. from the Wharton School of Business, University of Pennsylvania in 1990.

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Sean Shao has served as our independent director since June 5, 2013. Mr. Shao currently serves as (i) independent director and chairman of the audit committee of: 21Vianet Group, Inc., a leading carrier-neutral internet data center services provider listed on NASDAQ since August 2015; Jumei International Holding Ltd., an e-commerce company listed on NYSE since May 2014 and UTStarcom Holdings Corp., a provider of broadband equipment and solutions listed on NASDAQ since October 2012, (ii) independent director and chairman of the audit and compensation committees of China Biologic Products, Inc., a biopharmaceutical company listed on NASDAQ since July 2008. He served as the chief financial officer and a Board member of Trina Solar Limited from 2006 to 2008 and from 2015 to 2017, respectively. In addition, Mr. Shao served from 2004 to 2006 as the chief financial officer of ChinaEdu Corporation, an educational service provider, and of Watchdata Technologies Ltd., a Chinese security software company. Prior to that, Mr. Shao worked at Deloitte Touche Tohmatsu CPA Ltd. for approximately a decade. Mr. Shao received his master s degree in health care administration from the University of California at Los Angeles in 1988 and his bachelor s degree in art from East China Normal University in 1982. Mr. Shao is a member of the American Institute of Certified Public Accountants.

Kai-Fu Lee has served as our independent director since June 5, 2013. Dr. Lee has been the chairman of board of directors and chief executive officer of Innovation Works, a business creation platform and investment company focused on Internet technology and cloud computing since 2009. Prior to that, Dr. Lee had served as a vice president at Google and the president of Google Greater China from 2005 to 2009. Other than Innovation Works, Dr. Lee also serves on the board of certain private companies. Dr. Lee received a bachelor s degree in computer science from Columbia University in 1983 and a Ph.D. in computer science from Carnegie Mellon University in 1988.

Xiaoping (Bob) Xu has served as our independent director since June 2014. Since 2011, Mr. Xu has been the founder and managing partner of Zhenfund, a seed stage fund focusing on investments in technology, media and telecommunications sectors. Prior to that, he was one of the founding partners of New Oriental Education & Technology Group. Mr. Xu received a bachelor s degree from the Central Conservatory of Music in 1983, and a master s degree from University of Saskatchewan in 1992.

Liang Zhang is a co-founder of our company and has served as our executive vice president (formerly co-president) responsible for sourcing and supply chain since 2007. Mr. Zhang was also responsible for our operations from 2007 to 2009. From 2001 to 2006, Mr. Zhang founded and served as the chief executive officer of Zhongrun Ltd., a supplier for large Chinese online retail companies such as Dangdang.com and Amazon China, including its predecessor Joyo.com. He was a marketing manager at Netease.com Inc. from 1999 and 2001 and a program manager at Samsung Electronics from 1998 to 1999. Mr. Zhang received his bachelor s degree in business management from Nankai University in 1998.

Bin (Robin) Lu has been our chief financial officer since May 2014. Mr. Lu had been the chief financial officer and an executive director of A8 Digital Music Holdings Ltd since 2011 to 2014. Mr. Lu had also served as a director of Duomi Music Corporation from 2011 to 2014. From 2008 to 2010, Mr. Lu worked for Anaren, Inc as a division controller. Prior to Anaren, Robin was an executive director of Janney & Lee Investment LLC. He had also held

various finance management positions at China Network Communication Co., Ltd. (which has been acquired by China Unicom), Dell Inc. and China International Trust and Investment Corporation (currently known as CITIC Group). Mr. Lu received his bachelor s degree in automotive engineering from Tsinghua University in 1992 and his MBA degree in operation and finance from Ohio State University in 2000.

Bin Shi has been our chief technology officer since December 2015. Prior to that, Mr. Shi has served as our senior vice president of technology since March 2009. Before joining our Company, he worked for myspace.cn as the chief architect from March 2007 to March 2009 and Yahoo China as Messenger technical director of from April 2004 to March 2007. Mr. Shi had also held various technology management position at Shareware Freelancer and STAR Computer. Mr. Shi received his bachelor s degrees in both chemistry and computer science from Tsinghua University in 2000.

B. Compensation of Directors and Executive Officers

In 2016, we and our subsidiaries paid an aggregate cash compensation and benefits in kind of approximately $0.6 million to our directors and executive officers as a group. We set aside approximately $0.1 million for pensions, retirement or other benefits for our officers and directors in 2016. For information regarding options and restricted shares granted to officers and directors, see Share Incentive Plan.

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Employment Agreements

We have entered into employment agreements with each of our executive officers. We may terminate their employment for cause. In the event of termination for cause, we have no further obligations or liabilities to such executive officer other than to pay any accrued but unpaid compensation through the date of termination and we are not required to provide any prior notice of such termination. For purposes of these agreements, the term cause means: (a) the executive officer commits willful misconduct or gross negligence in performance of his duties hereunder, or Malfeasance, and fails to correct such Malfeasance within a reasonable period specified by us after we have sent the executive officer a written notice demanding correction within such a period; (b) the executive officer has committed Malfeasance and has caused serious losses and damages to us; (c) the executive officer seriously violates our internal rules and fails to correct such violation within a reasonable period specified by us after we have sent the executive officer a written notice demanding correction within such a period; (d) the executive officer has seriously violated the internal rules of and has caused serious losses and damages to us; (e) the executive officer is convicted by a court or has pleaded guilty of theft, fraud or other criminal offense; or (f) the executive officer seriously breaches his/her duty of loyalty to us or our affiliate under the laws of the Cayman Islands, the PRC or other relevant jurisdictions. We may terminate their employment at any time, without cause, upon 30-day prior written notice to the executive officer. Executive officers may terminate their employment with us at any time, without cause, upon three months written notice to us. If any severance pay is mandated by law, executive officers will be entitled to such severance pay in the amount mandated by law when his or her employment is terminated. However, an executive officer will not be entitled to any severance pay if his/her employment is terminated by him/her for any reason. In addition, we have been advised by our PRC counsel that notwithstanding any provision to the contrary in our employment agreements, we may still be required to make severance payments upon termination without cause to comply with the PRC Labor Law, the labor contract law and other relevant PRC regulations, which entitle employees to severance payments in case of early termination of de facto employment relationships by PRC entities without statutory cause regardless of whether there exists a written employment agreement with such entities.

Share Incentive Plan

We adopted our Amended and Reinstated 2008 Share Incentive Plan, or the Plan, on October 27, 2008. The Plan is 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 and other eligible persons. An aggregate of 4,444,444 ordinary shares were reserved for issuance under the Plan. On June 9, 2014, the Plan was amended to increase the maximum aggregate number of ordinary shares reserved for issuance under the Plan to 11,344,444. As of March 24, 2017, we had granted, after forfeitures, 6,512,154 restricted shares and options to purchase 2,121,550 ordinary shares, with 2,710,740 ordinary shares available for future grants. As of March 24, 2017, we had 5,987,649 unvested restricted shares and 1,564,588 unvested share options outstanding under the Plan. As of March 24, 2017, options to purchase 959,450 ordinary shares of our company were outstanding.

The following table summarizes the share options granted to our employees under the Plan that were outstanding as of March 24, 2017:

Name	Number of Ordinary Shares Underlying Outstanding Options	Exercise Price ($/Share)	Grant Date	Expiration Date

Our employees	70,000	0.50	December 31, 2008	The earlier of (1) the tenth anniversary of the date of grant, or (2) the fifth anniversary of the completion date of our initial public offering.
	79,000	0.01	March 31, 2009	
	36,000	0.01	June 30, 2009	
	15,000	0.50	June 30, 2009	
	18,000	0.96	June 30, 2009	
	30,100	0.96	September 30, 2009	
	3,900	0.96	December 31, 2009	
	136,000	0.96	March 31, 2010	
	2,500	0.96	June 30, 2010	
	49,000	0.96	October 31, 2010	
	63,000	4.25	July 31, 2011	
	158,186	4.75	May 22, 2013	
	1,018,278	2.50	June 20, 2014	
	16,000	3.00	September 26, 2014	
	6,000	3.00	December 12, 2014	
	541,800	2.25	June 2, 2015	
	4,600	2.64	October 1, 2015	
	4,000	1.40	September 20, 2016	

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We have historically determined the exercise price of shares granted under the Plan based on a number of factors, such as the type of awards, the length of time in which such employees were with our company, the function of such employees and the price of our preferred share issuances. Certain employees who joined our company near its inception were issued options with lower exercise prices than other employees. In addition, employees who we consider to be our key personnel may also be issued options with a lower exercise price.

In addition, as of March 24, 2017, a total of 9,042,681 restricted shares were granted to certain of our executive officers and other employees under the Plan. For the avoidance of doubt, restricted shares under the Plan are the same as nonvested shares disclosed in Note 11 to the Consolidated Financial Statements for the Years Ended December 31, 2014, 2015 and 2016 as filed as part of this annual report. For the avoidance of doubt, restricted shares under the Plan are the same as nonvested shares disclosed in Note 11 to the Consolidated Financial Statements for the Years Ended December 31, 2014, 2015 and 2016 as filed as part of this annual report.

The following paragraphs summarize the principal terms of the Plan.

Types of Awards and Exercise Prices . The Plan permits the grant of several kinds of awards, including among others, options, restricted shares, restricted share units, share appreciation rights and dividend equivalent rights.

Plan Administration . The Plan administrator is the chairman of our board or, in the case of administration with respect to directors and officers, a committee consisting of at least two non-employee directors designated by the board, and, with respect to consultants and other employees, a committee consisting of one or more directors of the company designated by the board. The plan administrator designates the eligible optionees and determines the award type, award period, grant date, performance requirements and such other provisions and terms not inconsistent with the plan in the award agreement.

Award Agreement . Options and other awards granted under the Plan are and will be evidenced by an award agreement that sets forth the terms, provisions, limitations and performance requirements for each grant.

Eligibility . At the discretion of the board of directors, we may grant awards to employees, officers, directors or consultants of our company.

Term of Awards . The term of each award shall be the term stated in the award agreement, provided that the term of an incentive share option shall be no more than ten years from the date of grant, subject to certain exceptions.

Acceleration of Awards upon Corporate Transaction . The plan administrator may upon or in anticipation of a corporate

transaction, accelerate awards or modify the terms of the awards.

Vesting Schedule . The plan administrator may determine the vesting schedule and may provide additional vesting conditions in the award agreement to each optionee.

Amendment and Termination . Our board of directors may at any time by resolutions amend, suspend or terminate the Plan, subject to certain exceptions. Unless earlier terminated by the board or directors, the Plan will terminate on October 26, 2018.

C. Board Practices

We have eight directors, three of whom are independent directors, on our board of directors. Any director on our board may be removed by way of an ordinary resolution of shareholders. Any vacancies on our board of directors or additions to the existing board of directors can be filled by the affirmative vote of all of the remaining directors. Each of our directors holds office until such director resigns or is removed by way of an ordinary resolution of shareholders. We have no service contracts with any of our directors that provide benefits to them upon termination.

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All of our executive officers are appointed by and serve at the discretion of our board of directors. Our executive officers are elected by and may be removed by a majority vote of our board of directors.

Board Committees

Our board of directors have established an audit committee, a compensation committee and a corporate governance and nominating committee. We have adopted a charter for each of these committees. Each committee s members and functions are as follows.

Audit Committee

Our audit committee consists of Mr. Sean Shao, Dr. Kai-Fu Lee and Mr. Xiaoping (Bob) Xu. Mr. Sean Shao is the chairman of our audit committee and satisfies the criteria of an audit committee financial expert as set forth under the applicable rules of the SEC. Each of Mr. Shao, Dr. Lee and Mr. Xu satisfies the requirements for an independent director within the meaning of Section 303A of the New York Stock Exchange Listed Company Manual and meets the criteria for independence set forth in Rule 10A-3 of the United States Securities Exchange Act of 1934, as amended, or the Exchange Act.

The audit committee oversees our accounting and financial reporting processes and the audits of the financial statements of our company. The audit committee is responsible for, among other things:

- selecting our independent registered public accounting firm and pre-approving all auditing and non-auditing services permitted to be performed by our independent registered public accounting firm;

- reviewing any audit problems or difficulties and management s response with our independent registered public accounting firm;

- reviewing and approving all proposed related-party transactions, as defined in Item 404 of Regulation S-K under the Securities Act;

- discussing the annual audited financial statements with management and our independent registered public accounting firm;

- reviewing major issues as to the adequacy of our internal controls and any special audit steps adopted in light of significant control deficiencies;

- 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 and periodically with management and our internal auditor and independent registered public accounting firm; and reporting regularly to the full board of directors.

Compensation Committee

Our compensation committee consists of Dr. Kai-Fu Lee, Mr. Sean Shao and Dr. Gang Yu. Dr. Kai-Fu Lee is the chairperson of our compensation committee. Dr. Lee and Mr. Shao satisfy the requirements for an independent director within the meaning of Section 303A of the New York Stock Exchange Listed Company Manual.

The compensation committee is responsible for, among other things:

- approving and overseeing the compensation package for our chief executive officer and chief financial officer;

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- reviewing and making recommendations to the board with respect to the compensation of our directors;

- reviewing and approving corporate goals and objectives relevant to the compensation of our chief executive officer and chief financial officer, evaluating the performance of our chief executive officer and chief financial officer in light of those goals and objectives, and setting the compensation level of our chief executive officer and chief financial officer based on such evaluation; and

- reviewing periodically and making recommendations to the board regarding any long-term incentive compensation or equity plans, programs or similar arrangements, annual bonuses, employee pension and welfare benefit plans.

Corporate Governance and Nominating Committee

Our corporate governance and nominating committee consists of Dr. Kai-Fu Lee, Mr. Sean Shao and Mr. Zhi Yan. Dr. Kai-Fu Lee is the chairman of our corporate governance and nominating committee. Dr. Lee and Mr. Shao satisfy the requirements for an independent director within the meaning of Section 303A of the New York Stock Exchange Listed Company Manual.

The corporate governance and nominating committee is responsible for, among other things:

- identifying and recommending to the board nominees for election or re-election to the board, or for appointment to fill any vacancy;

- conducting annual reviews of the Board s independence, qualifications and experiences in light of the availability of potential Board members; and

- monitoring compliance with our code of business conduct and ethics, including reviewing the adequacy and effectiveness of our internal rules and procedures.

Duties of Directors

Under Cayman Islands law, our directors have a fiduciary duty to act honestly, in good faith and with a view to our best interests. Our directors also have a duty to exercise the skill they actually possess and such care and diligence that a reasonably prudent person would exercise in comparable circumstances. In fulfilling their duty of care to us, our directors must ensure compliance with our memorandum and articles of association, as amended and restated from time to time. We have 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 annual general meetings and reporting its work to shareholders at such meetings;
- declaring dividends and distributions;
- appointing officers and determining the term of office of officers;
- exercising the borrowing powers of our company and mortgaging the property of our company; and approving the transfer of shares of our company, including registering such shares in our share register.

Corporate Governance

Our board of directors has adopted a code of business conduct and ethics, which is applicable to all of our directors, officers and employees. Our code of business conduct and ethics is publicly available on our website.

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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 amended and restated memorandum and articles of association.

Remuneration and Borrowing

The directors may determine remuneration to be paid to the directors. The compensation committee will assist the directors in reviewing and approving the compensation structure for the directors. The directors may exercise all the powers of our company to borrow money and to mortgage or charge its undertaking, property and uncalled capital, and to issue debentures or other securities whether outright or as security for any debt obligations of our company or of any third party.

Qualification

There is no requirement for our directors to own any shares in our company in order for them to qualify as a director.

Terms of Directors and Executive Officers

Our officers are elected by and serve at the discretion of our board of directors. Our directors are not subject to a term of office and hold office until such time as they are removed from office by special resolution or the unanimous written resolution of all shareholders. A director will be removed from office automatically if, among other things, the director (1) dies or becomes bankrupt or makes any arrangement or composition with his creditors generally; or (2) is found a lunatic or becomes of unsound mind. We do not have service contracts with any of our directors that would provide our directors with benefits upon their termination.

D. Employees

Employees

As of December 31, 2014, 2015 and 2016, we had 1,852, 896 and 703 full-time employees, respectively. All of our employees are based in China. We have employees from nine countries and districts, namely the United States, Italy, the South Kazakhstan, Denmark, Guatemala, The Republic of Byelorussia, Brazil, China and Hong Kong. The following table sets forth the number of our employees by function as of December 31, 2016:

	Number of Employees
Fulfillment	219
Selling and Marketing	288
Technology, Research and Development	127
General and Administrative	69
Total	703

We believe that we offer our employees competitive compensation packages and, as a result, we have generally been able to attract and retain qualified personnel and maintain a stable management team.

We generally enter into standard employment contracts with our employees, which contain non-compete provisions. Furthermore, we have entered into confidentiality agreements with many of our key employees that aim to protect our trademarks, designs, trade secrets and other intellectual property rights.

As required by PRC regulations, we participate in various employee social security plans that are organized by municipal and provincial governments, including pension, unemployment insurance, childbirth insurance, work-related injury insurance, medical insurance and housing fund. We are required under PRC law to make contributions to employee benefit plans at specified percentages of the salaries, bonuses and certain allowances of our employees, up to a maximum amount specified by the local government. The total amounts of contributions we made to employee benefit plans in 2014, 2015 and 2016 were $5.5 million, $5.2 million and $3.7 million, respectively.

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We believe that we have a good working relationship with our employees and we have not experienced any significant labor disputes.

D. Share Ownership

For information regarding the share ownership of our directors and officers, see Item 7. Major Shareholders and Related Party Transactions A. Major Shareholders. For information as to stock options granted to our directors, executive officers and other employees, see Item 6. Directors, Senior Management and Employees B. Compensation Share Incentive Plan.

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ITEM 7. MAJOR SHAREHOLDERS AND RELATED PARTY TRANSACTIONS

A. Major Shareholders

The following table sets forth information with respect to beneficial ownership of our ordinary shares as of March 24, 2017 by:

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

Beneficial ownership is determined in accordance with the rules and regulations of the SEC. In computing the number of shares beneficially owned by a person and the percentage ownership of that person, we have included shares that the person has the right to acquire within 60 days of this annual report, including through the exercise of any option, warrant or other right, the vesting of restricted shares or the conversion of any other security. These shares, however, are not included in the computation of the percentage ownership of any other person.

The calculations in the table below is based on 137,729,169 ordinary shares outstanding as of March 24, 2017, being the total ordinary shares issued and outstanding based on our register of members maintained by our Cayman Islands registrar, excluding (1) ordinary shares represented by the ADSs repurchased by the Company; (2) ordinary shares issued to the depositary that are issuable upon the exercise of share options outstanding and vesting of restricted shares issued to employees, or reserved for future award grants under our Amended and Reinstated 2008 Share Incentive Plan, or the Plan; and (3) ordinary shares underlying restricted shares issued to the grantees under the Plan that are in the process of being cancelled.

Name	Number	Percent
Directors and Executive Officers:		
Quji (Alan) Guo(1)	7,147,805	5.2%
Zhentao Wang(2)	24,553,810	17.8%
Xiongping Yu		
Zhi Yan(3)	52,954,540	36.5%
Gang Yu		
Sean Shao	*	*
Kai-Fu Lee	*	*
Xiaoping (Bob) Xu(4)	3,921,498	2.8%
Liang Zhang(5)	2,571,065	1.9%
Bin (Robin) Lu	*	*
Bin Shi	*	*
All directors and executive officers as a group	91,680,768	63.1%

Principal Shareholders:		
Zall Entities(6)	52,954,540	36.5%
AOGANG International (Hong Kong) Corporation Limited(7)	24,553,810	17.8%
Ceyuan Entities(8)	13,291,591	9.7%
GSR Ventures III, L.P. (9)	9,932,391	7.2%
Wincore Holdings Limited (10)	7,147,805	5.2%

Notes:

* Less than 1% of our total outstanding shares.

(1) Represents 6,681,251 ordinary shares and 233,277 ADSs representing 466,554 ordinary shares held by Wincore Holdings Limited. Wincore Holdings Limited, a British Virgin Islands company, is wholly owned by Mr. Quji (Alan) Guo, our chairman of the board and chief executive officer. The registered address of Wincore Holdings Limited is Palm Grove House, P.O. Box 438, Road Town, Tortola, British Virgin Islands.

(2) Represents 20,260,082 ordinary shares and 2,146,864 ADSs representing 4,293,728 ordinary shares held by AOGANG International. For a description of the beneficial ownership of our ordinary shares by AOGANG International, see Note 7 below. Mr. Wang disclaims beneficial ownership of our ordinary shares held by AOGANG International, except to the extent of his pecuniary interest in these shares.

(3) Represents 42,500,000 ordinary shares held by Zall E-Commerce, 1,499,770 ADSs representing 2,999,540 ordinary shares held by Zall Development (HK) Holding Company Limited, or Zall Development HK, and 7,455,000 ordinary shares purchasable through the exercise of warrant held by Zall E-Commerce. For a description of the beneficial ownership of our ordinary shares by Zall E-Commerce and Zall Development HK, see Note 6 below. Mr. Yan disclaims beneficial ownership of our ordinary shares held by Zall E-Commerce and Zall Development HK, except to the extent of their pecuniary interest in these shares.

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(4) Represents 1,960,749 ADSs representing 3,921,498 ordinary shares held by Focus China Holdings Limited. Focus China Holdings Limited, a British Virgin Islands company, is wholly owned by Mr. Xiaoping (Bob) Xu, a founding angel. The registered address of Focus China Holdings Limited is Trinity Chambers, P.O. Box 4301, Road Town, Tortola, British Virgin Islands.

(5) Represents 2,542,541 ordinary shares and 14,262 ADSs representing 28,524 ordinary shares held by Clinet Investments Limited. Clinet Investments Limited, a British Virgin Islands company, is wholly owned by Mr. Liang Zhang, our executive vice president. The registered address of Clinet Investments Limited is Palm Grove House, P.O. Box 438, Road Town, Tortola, British Virgin Islands.

(6) Represents 42,500,000 ordinary shares held by Zall E-Commerce, 1,499,770 ADSs representing 2,999,540 ordinary shares held by Zall Development HK and 7,455,000 ordinary shares purchasable through the exercise of warrant held by Zall E-Commerce. Zall E-Commerce, a company incorporated in the British Virgin Islands, is directly and wholly owned by Zall Development (BVI) Holding Company Limited, or Zall Development BVI, a company incorporated in the British Virgin Islands, which is a wholly owned subsidiary of Zall Group. Zall Development HK, a limited liability company incorporated under the laws of Hong Kong, is also directly and wholly owned by Zall Group. Mr. Zhi Yan is the founder, co-chairman of the board of directors, chief executive officer and an executive director of Zall Group and holds his beneficial interest in Zall Group through Zall Development Investment Company Limited, or Zall Development Investment, a company incorporated in the British Virgin Islands. Zall E-Commerce, Zall Development BVI, Zall Development HK, Zall Group and Zall Development Investment are collectively referred to in this annual report as Zall Entities. The address of the principal office of Zall Entities is Suite 2101, 21st Floor, Two Exchange Square, Central, Hong Kong.

(7) Represents 20,260,082 ordinary shares and 2,146,864 ADSs representing 4,293,728 ordinary shares held by AOGANG International. AOGANG International, a limited liability company incorporated under the laws of Hong Kong, is directly and wholly owned by AoKang, a company incorporated under the laws of the Peoples Republic of China. Mr. Zhentao Wang is the chairman of the board and controlling person of AoKang and the sole director of AOGANG International. Of the total outstanding shares of AoKang: (i) AoKang Investment Holdings Co., Ltd. in which Mr. Zhentao Wang and Mr. Chen Wang (son of Mr. Zhentao Wang) directly holds 90% and 10%, respectively, of its total outstanding shares, directly holds 17.80%, (ii) Mr. Zhentao Wang directly holds 14.93%, (iii) Mr. Chen Wang directly holds 9.98% and (iv) Mr. Jinquan Wang (brother of Mr. Zhentao Wang and the president and a director of AoKang) directly holds 4.98%. The registered address of AOGANG International is RM.19C, Lockhart CTR., 301-307 Lockhart RD, Wan Chai, Hong Kong. The address of the principal office of AoKang is Aokang Industrial Park, Dongou Industrial District, Oubei Town, Yongjia County, Zhejiang Province, People s Republic of China.

(8) Represents 11,683,530 ordinary shares and 557,471 ADSs representing 1,114,942 ordinary shares held by Ceyuan Ventures II, L.P., and 450,161 ordinary shares and 21,479 ADSs representing 42,958 ordinary shares held by Ceyuan Ventures Advisors Fund II, LLC, respectively. Ceyuan Ventures II, L.P. and Ceyuan Ventures Advisors Fund II, LLC are collectively referred to in this annual report as the Ceyuan Entities. Ceyuan Ventures II, L.P. and Ceyuan Ventures Advisors Fund II, LLC are under the common control of Ceyuan Ventures Management II, LLC, which is the general partner of Ceyuan Ventures II, L.P. and sole director of Ceyuan Ventures Advisors II, LLC. Mr. Bo Feng, Ceyuan Partners, Yanxi Holding Co., Ltd., Mr. Weiguo Zhao, NewMargin Fund Management Company Limited and Mr. John S. Wadsworth Jr. collectively hold 100% shares of Ceyuan Ventures Management II, LLC. Mr. Christopher Wadsworth has the voting and dispositive power over the shares held by Ceyuan Partners. Mr. Ye Yuan has the voting and dispositive power over the shares held by Yanxi Holding Co., Ltd. Mr. Tao Feng has the voting and dispositive power over the shares held by NewMargin Fund Management Company Limited. The registered address of Ceyuan

Entities is c/o Maples Corporate Services Limited, P.O. Box 309, Ugland House, Grand Cayman, KY1-1104, Cayman Islands, British West Indies.

(9) Represents 9,721,891 ordinary shares and 105,250 ADSs representing 210,500 ordinary shares held by GSR Ventures III, L.P. The general partner of GSR Ventures III, L.P. is GSR Partners III, L.P., whose general partner is GSR Partners III, Ltd., a company incorporated in the Cayman Islands, which is owned by Messrs. Jin-Choon (Richard) Lim, Sonny Wu, Ding Jian (James), Alexander Pan and Ms. Ryann Yap. The registered address of GSR Ventures III, L.P. is Floor 4, Willow House, Cricket Square, P.O. Box 268, Grand Cayman KY1-1104, Cayman Islands.

(10) Wincore Holdings Limited, a British Virgin Islands company, is wholly owned by Mr. Quji (Alan) Guo, our chairman of the board and chief executive officer. The registered address of Wincore Holdings Limited is Palm Grove House, P.O. Box 438, Road Town, Tortola, British Virgin Islands.

We have one class of ordinary shares, and each holder of our ordinary shares is entitled to one vote per share. However, in matters related to change of control, pursuant to our amended and restated memorandum and articles of association, Wincore Holdings Limited, Clinet Investments Limited and Vitz Holdings Limited will be entitled to three votes per share for each ordinary share registered in their names in the register of members of the Company, and each other holder is entitled to one vote per share. Such change of control events include: (a) a merger, amalgamation, consolidation or similar transaction involving our company, (b) the filing of a petition for a scheme of arrangement involving our company, or the giving of consent to such a filing or the co-operation by our company in the making of such filing, and (c) a sale, transfer or other disposition of all or substantially all of the assets of our company. As of March 24, 2017, each of Wincore Holdings Limited, Clinet Investment Limited and Vitz Holdings Limited holds 5.2%, 2.6% and 1.9% of the shares of our company, respectively, entitling them to 13.1%, 6.5% and 4.7% voting rights, respectively, and an aggregate of 24.3% of voting rights in such matters related to a change of control, assuming all the ADSs held by such entities were converted into ordinary shares of the Company.

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As of March 24, 2017, 137,729,169 of our ordinary shares were issued and outstanding, being the total ordinary shares issued and outstanding based on our register of members maintained by our Cayman Islands registrar, excluding (1) ordinary shares represented by the ADSs repurchased by the Company; (2) ordinary shares issued to the depositary that are issuable upon the exercise of share options outstanding and vesting of restricted shares issued to employees, or reserved for future award grants under our Amended and Reinstated 2008 Share Incentive Plan, or the Plan; and (3) ordinary shares underlying restricted shares issued to the grantees under the Plan that are in the process of being cancelled. Based on a review of our register of members, we believe that as of March 24, 2017, 38,866,445 ordinary shares, representing approximately 28.2% of our total outstanding shares, were held by two record shareholders in the United States, which includes 38,866,444 ordinary shares held of record by The Bank of New York Mellon, the depositary of our ADS program. The number of beneficial owners of our ADSs in the United States is likely to be much larger than the number of record holders of our ordinary shares in the United States. We are not aware of any arrangement that may at a subsequent date, result in a change of control of our company.

B. Related Party Transactions

Indemnification Agreements

The Company entered into indemnification agreements with our directors and senior executive officers. These agreements require the Company to indemnify such individuals, to the fullest extent permitted by law, for certain liabilities to which they may become subject as a result of their affiliation with the Company.

Purchase from related parties

In 2016, we purchased goods in an aggregate amount of approximately $5 thousand from Aokang, one of our major shareholders.

Employment Agreements

See Item. 6 Directors, Senior Management and Employees B. Compensation Employment Agreements.

Share Options

See Item. 6 Directors, Senior Management and Employees B. Compensation Share Incentive Plan.

E. Interests of Experts and Counsel

Not applicable.

ITEM 8. FINANCIAL INFORMATION

A. Consolidated Statements and Other Financial Information

See Item 18. Financial Statements.

Legal and Administrative Proceedings

We are not currently a party to any legal proceeding or investigation which, in the opinion of our management, is likely to have a material adverse effect on our business, financial condition or results of operations.

Dividend Policy

Since our inception, we have not declared or paid any dividends on our ordinary shares. We have no present plan to pay any dividends on our ordinary shares in the foreseeable future. We intend to retain most, if not all, of our available funds and any future earnings to operate and expand our business.

Any future determination to pay dividends will be made at the discretion of our board of directors and may be based on a number of factors, including our future operations and earnings, capital requirements and surplus, general financial condition, contractual restrictions and other factors that the board of directors may deem relevant. If we pay any dividends, we will pay the ADS holders to the same extent as holders of our ordinary shares, subject to the terms of the deposit agreement, including the fees and expenses payable thereunder. Cash dividends on our ordinary shares, if any, will be paid in U.S. dollars.

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We are a holding company incorporated in the Cayman Islands. In order for us to distribute any dividends to our shareholders and ADS holders, we may rely on dividends and cash distributed by our Hong Kong subsidiary and may, in the future, rely on dividends and cash distributed by our PRC subsidiary through our Hong Kong subsidiary for the cash requirement of the holding company. Certain payments from our PRC subsidiary to us are subject to PRC taxes, such as withholding income tax. In addition, regulations in the PRC currently permit payment of dividends of a PRC company only out of accumulated distributable after-tax profits as determined in accordance with its articles of association and the accounting standards and regulations in China. Each of our PRC subsidiary, VIEs and Shanghai Ouku, the subsidiary of Lanting Huitong, is required to set aside at least 10% of its after-tax profit based on PRC accounting standards every year to certain statutory reserves until the accumulated amount of such reserves reaches 50% of its respective registered capital. Such statutory reserves are not distributable as loans, advances or cash dividends. Our PRC subsidiary, VIEs and Shanghai Ouku are also required to set aside a certain amount of its after-tax profits each year, if any, to fund a private fund for employees. The specific size of the employee fund is at the discretion of the relevant entity. These reserve funds can only be used for specific purposes and are not transferable to the company s parent in the form of loans, advances or dividends. See Item 3. Key Information D. Risk Factors Risks Related to Doing Business in China We may rely on dividends and other cash distributions on equity paid by our subsidiaries to fund any cash and financing requirements we may have and any limitation on the ability of our subsidiaries to make payments to us could have a material adverse effect on our ability to conduct our businesses.

B. Significant Changes

We have not experienced any significant changes since the date of our audited consolidated financial statements included in this annual report.

ITEM 9. THE OFFER AND LISTING

A. Offer and Listing Details.

Our ADSs, each representing two of our ordinary shares, have been listed on the New York Stock Exchange since June 6, 2013 under the symbol LITB. The table below shows, for the periods indicated, the high and low market prices on the New York Stock Exchange for our ADSs until March 29, 2017.

	Sale Price	
	High	**Low**
Annual highs and lows		
2015	6.53	2.36
2016	3.59	1.95
Quarterly highs and lows		
First quarter 2015	6.53	3.87
Second quarter 2015	6.46	4.29
Third quarter 2015	4.64	2.36
Fourth quarter 2015	4.29	2.63
First quarter 2016	3.07	1.95
Second quarter 2016	3.54	2.31
Third quarter 2016	3.59	2.70

Fourth quarter 2016	3.10	2.40
First quarter 2017(through March 29, 2017)	3.20	2.70
Monthly highs and lows		
September 2016	3.28	2.70
October 2016	3.00	2.53
November 2016	2.85	2.55
December 2016	3.10	2.40
January 2017	3.20	2.85
February 2017	3.15	2.79
March 2017 (through March 29, 2017)	3.02	2.70

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B. Plan of Distribution

Not applicable.

C. Markets

Our ADSs, each representing two of our ordinary shares, have been listed on the New York Stock Exchange since June 6, 2013 under the symbol LITB.

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 and Articles of Association

We incorporate by reference into this annual report the description of our fourth amended and restated memorandum and articles of association contained in our F-1 registration statement (File No. 333-187965), as amended, filed with the SEC on May 23, 2013. Our shareholders adopted our fourth amended and restated memorandum and articles of association by unanimous resolutions on the same date, and effective upon completion of our initial public offering of ordinary shares represented by our ADSs.

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 or elsewhere in this annual report.

D. Exchange Controls

See Item 4. Information on the Company B. Business Overview Regulation Regulations on Foreign Exchange.

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E. Taxation

The following is a general summary of the material Cayman Islands, People s Republic of China and U.S. federal income tax consequences relevant to an investment in the 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. 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 U.S. 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. To the extent that the discussion relates to matters of Cayman Islands tax law, and subject to the qualifications, assumptions and limitations related thereto, the discussion of the material Cayman Islands tax consequences of the ownership of our ordinary shares and ADSs represents the opinion of Maples and Calder (Hong Kong) LLP, our Cayman Islands counsel. To the extent that the discussion relates to matters of People s Republic of China tax law, and subject to the qualifications, assumptions and limitations related thereto, the discussion of the material People s Republic of China tax consequences of the ownership of our ordinary shares and ADSs represents the opinion of TransAsia Lawyers, our PRC counsel. To the extent that the discussion relates to matters of United States federal income tax law, and subject to the qualifications, assumptions and limitations related thereto, the discussion of the material United States federal income tax consequences to United States Holders of the ownership of our ordinary shares and ADSs represents the opinion of Simpson Thacher & Bartlett LLP, our United States counsel. You should consult your own tax advisors with respect to the consequences of acquisition, ownership and disposition of the ADSs and ordinary shares.

Cayman Islands Taxation

The Cayman Islands currently levies no taxes on individuals or corporations based upon profits, income, gains or appreciation and there is no taxation in the nature of inheritance tax or estate duty or withholding tax applicable to us or to any holder of the ADSs and 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, or produced before a court 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 applicable to payments made to or by us. There are no exchange control regulations or currency restrictions in the Cayman Islands.

People s Republic of China Taxation

The New EIT Law, which was issued in 2007 and amended in 2017, and its Implementation Rules, which was issued in 2007, provide that China-sourced income of foreign enterprises, such as dividends paid by a PRC subsidiary to its foreign investor, will normally be subject to PRC withholding tax at a rate of 10%, unless any such foreign investor s jurisdiction of incorporation has a tax treaty with China that provides for a different withholding arrangement. We are a Cayman Islands holding company and we plan to conduct substantially all of our business in China through Lanting Jishi, which is 100% owned by Light In the Box Limited, our wholly owned subsidiary located in Hong Kong. According to the Mainland and Hong Kong Special Administrative Region Arrangements on the Avoidance of Double

Taxation and the Prevention of Fiscal Evasion with Respect to Taxes on Income, or the Double Taxation Avoidance Arrangement, dividends that Light In The Box Limited receives from Lanting Jishi may be subject to withholding tax at a rate of 5%, provided that: (a) Light In The Box Limited is determined by the relevant PRC tax authorities to be a non-resident enterprise under the New EIT Law; (b) Light In The Box Limited is the beneficial owner of the PRC sourced income; (c) Light In The Box Limited holds at least 25% of the equity interest of Lanting Jishi and (d) all other conditions and requirements under the Double Taxation Avoidance Arrangement shall be satisfied.

Under the New EIT Law, enterprises established under the laws of jurisdictions outside China with their de facto management bodies located within China may be considered to be PRC tax resident enterprises for tax purposes. If we are considered a PRC tax resident enterprise, then our global income will be subject to PRC enterprise income tax at the rate of 25%.

The Implementation Rules of the New EIT Law provide that, (i) if the enterprise that distributes dividends is domiciled in the PRC, or (ii) if gains are realized from transferring equity interests of enterprises domiciled in the PRC, then such dividends or capital gains are treated as China-sourced income. It is not clear how domicile may be interpreted under the New EIT Law, and it may be interpreted as the jurisdiction where the enterprise is a tax resident. Therefore, if we are considered as a PRC tax resident enterprise for tax purposes, any dividends we pay to our overseas shareholders or ADS holders which are non-resident enterprises as well as gains realized by such shareholders or ADS holders from the transfer of our shares or ADSs may be regarded as China-sourced income and as a result become subject to PRC withholding tax at a rate of up to 10%.

Furthermore, if we are considered a PRC resident enterprise and the competent PRC tax authorities consider dividends we pay with respect to our shares or ADSs and the gains realized from the transfer of our shares or ADSs to be income derived from sources within the PRC, such dividends we pay to our overseas shareholders or ADS holders who are non-resident individuals and such gains realized by such shareholders from the transfer of our shares or ADSs may be subject to PRC individual income tax at a rate of 20%, unless any such non-resident individuals jurisdiction has a tax treaty with China that provides for a preferential tax rate or a tax exemption. It is also unclear whether, if we are considered a PRC resident enterprise, holders of our shares or ADSs would be able to claim the benefit of income tax treaties or agreements entered into between China and other countries or areas.

Material United States Federal Income Tax Considerations

The following summary describes the material United States federal income tax consequences to United States Holders (as defined below) of the ownership of our ordinary shares and ADSs as of the date hereof. Except where noted, this summary deals only with ordinary shares and ADSs held as capital assets. As used herein, the term United States Holder means a holder of an ordinary share or ADS that is for United States federal income tax purposes:

- an individual citizen or resident of the United States;
- a corporation (or other entity treated as a corporation for United States federal income tax purposes) created or organized in or under the laws of the United States, any state thereof or the District of Columbia;
- an estate the income of which is subject to United States federal income taxation regardless of its source; or
- a trust if it (1) is subject to the primary supervision of a court within the United States and one or more United States persons have the authority to control all substantial decisions of the trust, or (2) has a valid election in effect under applicable United States Treasury regulations to be treated as a United States person.

This summary does not represent a detailed description of the United States federal income tax consequences applicable to you if you are subject to special treatment under the United States federal income tax laws, including if you are:

- a dealer in securities or currencies;
- a financial institution;

- a regulated investment company;
- a real estate investment trust;
- an insurance company;
- a U.S. expatriate;
- a tax-exempt organization;
- a person holding our ordinary shares or ADSs as part of a hedging, integrated or conversion transaction, a constructive sale or a straddle;

- a trader in securities that has elected the mark-to-market method of accounting for your securities;
- a person liable for alternative minimum tax;
- a person who owns or is deemed to own 10% or more of our voting stock;
- a person who acquired ordinary shares or ADSs pursuant to the exercise of any employee share option or otherwise as compensation;
- a partnership or other pass-through entity for United States federal income tax purposes; or
- a person whose functional currency is not the United States dollar.

The discussion below is based upon the provisions of the Internal Revenue Code of 1986, as amended (the Code), and regulations, rulings and judicial decisions thereunder as of the date hereof, and such authorities may be replaced, revoked or modified so as to result in United States federal income tax consequences different from those discussed below. In addition, this summary is based, in part, upon representations made by the depositary to us and assumes that the deposit agreement, and all other related agreements, will be performed in accordance with their terms.

If a partnership (or other entity treated as a partnership for United States federal income tax purposes) holds our ordinary shares or ADSs, the tax treatment of a partner will generally depend upon the status of the partner and the activities of the partnership. If you are a partner of a partnership holding our ordinary shares or ADSs, you should consult your tax advisors.

This summary does not contain a detailed description of all the United States federal income tax consequences to you in light of your particular circumstances and does not address the Medicare tax on net investment income, or the effects of any state, local or non-United States tax laws. If you are considering the purchase, ownership or disposition of our ordinary shares or ADSs, you should consult your own tax advisors concerning the United States federal income tax consequences to you in light of your particular situation as well as any consequences arising under the laws of any other taxing jurisdiction.

ADSs

If you hold ADSs you generally will be treated, for United States federal income tax purposes, as the owner of the underlying ordinary shares that are represented by such ADSs. Accordingly, deposits or withdrawals of ordinary shares for ADSs will not be subject to United States federal income tax.

Taxation of Dividends

Subject to the discussion under Passive Foreign Investment Company below, the gross amount of distributions on the ADSs or ordinary shares (including any amounts withheld to reflect PRC withholding taxes) will be taxable as dividends to the extent paid out of our current or accumulated earnings and profits, as determined under United States federal income tax principles. Such income (including withheld taxes) will be includable in your gross income as ordinary income on the day actually or constructively received by you, in the case of the ordinary shares, or by the depositary, in the case of ADSs. Such dividends will not be eligible for the dividends received deduction allowed to corporations under the Code.

With respect to non-corporate United States investors, certain dividends received from a qualified foreign corporation may be subject to reduced rates of taxation. A foreign corporation is treated as a qualified foreign corporation with respect to dividends received from that corporation on ordinary shares (or ADSs backed by such shares) that are readily tradable on an established securities market in the United States. United States Treasury Department guidance indicates that the ADSs, which are listed on the New York Stock Exchange, are readily tradable on an established securities market in the United States. Thus, we believe that dividends we pay on ordinary shares represented by the ADSs will meet the conditions required for the reduced tax rates. Since we do not expect that our ordinary shares will be listed on an established securities market, we do not believe that dividends that we pay on our ordinary shares that are not represented by ADSs currently meet the conditions required for these reduced tax rates. There can be no assurance that the ADSs will be considered readily tradable on an established securities market in later years. A qualified foreign corporation also includes a foreign corporation that is eligible for the benefits of certain income tax treaties with the United States. In the event that we are deemed to be a PRC resident enterprise under the PRC tax law, we may be eligible for the benefits of the income tax treaty between the United States and the PRC (the Treaty), and if we are eligible for such benefits, dividends we pay on our ordinary shares, regardless of whether such shares are represented by ADSs, would be eligible for the reduced rates of taxation whether or not such shares are readily tradable on an established securities market in the United States. See People s Republic of China Taxation. Non-corporate United States Holders that do not meet a minimum holding period requirement during which they are not protected from the risk of loss or that elect to treat the dividend income as investment income pursuant to Section 163(d)(4) of the Code will not be eligible for the reduced rates of taxation regardless of our status as a qualified foreign corporation. In addition, the rate reduction will not apply to dividends if the recipient of a dividend is obligated to make related payments with respect to positions in substantially similar or related property. This disallowance applies even if the minimum holding period has been met. Non-corporate United States Holders will not be eligible for reduced rates of taxation on any dividends received from us, if we are a PFIC in the taxable year in which such dividends are paid or in the preceding taxable year. You should consult your own tax advisors regarding the application of these rules given your particular circumstances.

In the event that we are deemed to be a PRC resident enterprise under the PRC tax law, you may be subject to PRC withholding taxes on dividends paid to you with respect to the ADSs or ordinary shares. See People s Republic of China Taxation. In that case, subject to certain conditions and limitations, PRC withholding taxes on dividends may be treated as foreign taxes eligible for credit against your United States federal income tax liability. For purposes of calculating the foreign tax credit, dividends paid on the ADSs or ordinary shares will be treated as foreign-source income and will generally constitute passive category income. However, in certain circumstances, if you have held the ADSs or ordinary shares for less than a specified minimum period during which you are not protected from risk of loss, or are obligated to make payments related to the dividends, you will not be allowed a foreign tax credit for any PRC withholding taxes imposed on dividends paid on the ADSs or ordinary shares. The rules governing the foreign tax credit are complex. You are urged to consult your tax advisors regarding the availability of the foreign tax credit under your particular circumstances.

To the extent that the amount of any distribution exceeds our current and accumulated earnings and profits for a taxable year, as determined under United States federal income tax principles, the distribution will first be treated as a tax-free return of capital, causing a reduction in the adjusted basis of the ADSs or ordinary shares (thereby increasing the amount of gain, or decreasing the amount of loss, to be recognized by you on a subsequent disposition of the ADSs or ordinary shares), and the balance in excess of adjusted basis will be taxed as capital gain recognized on a sale or exchange. However, we do not expect to determine our earnings and profits in accordance with United States federal income tax principles. Therefore, you should expect that a distribution will generally be treated as a dividend (as discussed above).

Passive Foreign Investment Company

Based on the past and projected composition of our income and valuation of our assets, including goodwill, we do not believe that we were a PFIC for 2016. However, as the determination of our PFIC status is based on an annual determination that cannot be made until the close of a taxable year, and involves extensive factual investigation, including ascertaining the fair market value of all of our assets on a quarterly basis and the character of each item of income we earn, our United States counsel expresses no opinion with respect to our PFIC status.

In general, we will be a PFIC for any taxable year in which:

- at least 75% of our gross income is passive income, or

- at least 50% of the value (determined on a quarterly basis) of our assets is attributable to assets that produce or are held for the production of passive income.

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For this purpose, passive income generally includes dividends, interest, royalties and rents (other than royalties and rents derived in the active conduct of a trade or business and not derived from a related person). If we own at least 25% (by value) of the stock of another corporation, we will be treated, for purposes of the PFIC tests, as owning our proportionate share of the other corporation s assets and receiving our proportionate share of the other corporation s income. However, it is not entirely clear how the contractual arrangements between us and our VIEs will be treated for purposes of the PFIC rules. If it is determined that we do not own the stock of our VIEs for United States federal income tax purposes, we may be treated as a PFIC.

The determination of whether we are a PFIC is made annually. Accordingly, it is possible that we may become a PFIC in the current or any future taxable year due to changes in our asset or income composition. Because we have valued our goodwill based on the market value of our equity, and given the volatility of the market price of the ADSs, a decrease in the price of the ADSs may also result in our becoming a PFIC. If we are a PFIC for any taxable year during which you hold the ADSs or ordinary shares, you will be subject to special tax rules discussed below.

If we are a PFIC for any taxable year during which you hold the ADSs or ordinary shares, you will be subject to special tax rules with respect to any excess distribution received and any gain realized from a sale or other disposition, including a pledge, of ADSs or ordinary shares. Distributions received in a taxable year will be treated as excess distributions to the extent that they are greater than 125% of the average annual distributions received during the shorter of the three preceding taxable years or your holding period for the ADSs or ordinary shares. Under these special tax rules:

- the excess distribution or gain will be allocated ratably over your holding period for the ADSs or ordinary shares,

- the amount allocated to the current taxable year, and any taxable year in your holding period prior to the first taxable year in which we were a PFIC, will be treated as ordinary income, and

- the amount allocated to each other year will be subject to tax at the highest tax rate in effect for each such year and the interest charge generally applicable to underpayments of tax will be imposed on the resulting tax attributable to each such year.

The tax liability for amounts allocated to taxable years prior to the year of disposition or excess distribution cannot be offset by any net operating losses for such years, and gains (but not losses) realized on the sale or other disposition of the ADSs or ordinary shares cannot be treated as capital gain, even if you hold the ADSs or ordinary shares as capital assets.

Although the determination of whether we are a PFIC is made annually, if we are a PFIC for any taxable year in which you hold our ADSs or ordinary shares, you will generally be subject to the special tax rules described above for that year and for each subsequent year in which you hold the ADSs or ordinary shares (even if we do not qualify as a PFIC in such subsequent years). However, if we cease to be a PFIC, you can avoid the continuing impact of the PFIC rules by making a special election to recognize gain as if your ADSs or ordinary shares had been sold on the last day of the last taxable year during which we were a PFIC. You are urged to consult your own tax advisor about this election.

In addition, non-corporate United States Holders will not be eligible for reduced rates of taxation on any dividends received from us, if we are a PFIC in the taxable year in which such dividends are paid or in the preceding taxable year. Furthermore, unless otherwise provided by the United States Treasury Department, each United States Holder of a PFIC is generally required to file an annual report containing such information as the United States Treasury Department may require.

If we are a PFIC for any taxable year during which you hold the ADSs or ordinary shares and any of our non-United States subsidiaries is also a PFIC or we make direct or indirect equity investments in other entities that are PFICs, a United States Holder would be treated as owning a proportionate amount (by value) of the shares of the lower-tier PFIC for purposes of the application of these rules. You are urged to consult your tax advisors about the application of the PFIC rules to any of our subsidiaries.

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In certain circumstances, in lieu of being subject to the excess distribution rules discussed above, you may make an election to include gain on the stock of a PFIC as ordinary income under a mark-to-market method, provided that such stock is regularly traded on a qualified exchange. Under current law, the mark-to-market election may be available to United States Holders of ADSs because the ADSs are listed on the New York Stock Exchange, which constitutes a qualified exchange, although there can be no assurance that the ADSs will be regularly traded for purposes of the mark-to-market election. It should also be noted that it is intended that only the ADSs and not the ordinary shares will be listed on the New York Stock Exchange. Consequently, if you are a United States Holder of ordinary shares that are not represented by ADSs, you generally will not be eligible to make a mark-to-market election if we are or were to become a PFIC.

If you make an effective mark-to-market election, you will include in each year that we are a PFIC as ordinary income the excess of the fair market value of your ADSs at the end of your taxable year over your adjusted tax basis in the ADSs. You will be entitled to deduct as an ordinary loss in each such year the excess of your adjusted tax basis in the ADSs over their fair market value at the end of the year, but only to the extent of the net amount previously included in income as a result of the mark-to-market election. If you make an effective mark-to-market election, in each year that we are a PFIC any gain you recognize upon the sale or other disposition of your ADSs will be treated as ordinary income and any loss will be treated as ordinary loss, but only to the extent of the net amount previously included in income as a result of the mark-to-market election.

Your adjusted tax basis in the ADSs will be increased by the amount of any income inclusion and decreased by the amount of any deductions under the mark-to-market rules. If you make a mark-to-market election it will be effective for the taxable year for which the election is made and all subsequent taxable years unless the ADSs are no longer regularly traded on a qualified exchange or the Internal Revenue Service consents to the revocation of the election. You are urged to consult your tax advisors about the availability of the mark-to-market election, and whether making the election would be advisable in your particular circumstances.

Alternatively, you can sometimes avoid the PFIC rules described above by electing to treat a PFIC as a qualified electing fund under Section 1295 of the Code. However, this option likely will not be available to you because we do not intend to comply with the requirements necessary to permit you to make this election.

You are urged to consult your tax advisors concerning the United States federal income tax consequences of holding ADSs or ordinary shares if we are considered a PFIC in any taxable year.

Taxation of Capital Gains

For United States federal income tax purposes, you will recognize taxable gain or loss on any sale or exchange of ADSs or ordinary shares in an amount equal to the difference between the amount realized for the ADSs or ordinary shares and your tax basis in the ADSs or ordinary shares. Subject to the discussion under Passive Foreign Investment Company above, such gain or loss will generally be capital gain or loss. Capital gains of non-corporate United States Holders derived with respect to capital assets held for more than one year are eligible for reduced rates of taxation. The deductibility of capital losses is subject to limitations. Any gain or loss recognized by you will generally be treated as United States source gain or loss for foreign tax credit limitation purposes. However, if we are treated as a PRC resident enterprise for PRC tax purposes and PRC tax was imposed on any gain, and if you are eligible for the benefit of the Treaty, you may elect to treat such gain as PRC source gain. If you are not eligible for the benefits of the Treaty or you fail to make the election to treat any gain as PRC source, then you may not be able to use the foreign tax credit arising from any PRC tax imposed on the disposition of the ADSs or ordinary shares unless such credit can be applied (subject to applicable limitations) against tax due on other income derived from foreign sources. You are urged to consult your tax advisors regarding the tax consequences if any PRC tax is imposed on gain on a disposition of the ADSs or ordinary shares, including the availability of

the foreign tax credit and the election to treat any gain as PRC source, under your particular circumstances.

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Information Reporting and Backup Withholding

In general, information reporting will apply to dividends in respect of the ADSs or ordinary shares and the proceeds from the sale, exchange or redemption of the ADSs or ordinary shares that are paid to you within the United States (and in certain cases, outside the United States), unless you are an exempt recipient. A backup withholding tax may apply to such payments if you fail to provide a taxpayer identification number or certification of other exempt status or fail to report in full dividend and interest income.

Backup withholding is not an additional tax and any amounts withheld under the backup withholding rules will be allowed as a refund or a credit against your United States federal income tax liability provided the required information is furnished to the Internal Revenue Service in a timely manner.

Additional Reporting Requirements

Certain United States Holders are required to report information relating to an interest in the ADSs or ordinary shares, subject to certain exceptions (including an exception for ADSs or ordinary shares held in accounts maintained by certain financial institutions), by attaching a complete Internal Revenue Service Form 8938, Statement of Specified Foreign Financial Assets, with their tax return for each year in which they hold ADSs or ordinary shares . United States Holders should consult their tax advisors regarding the effect, if any, of these rules on their ownership and disposition of the ADSs and ordinary shares.

F. Dividends and Paying Agents

Not applicable.

G. Statement by Experts

Not applicable.

H. Documents on Display

We have previously filed with the SEC our registration statement on Form F-1 (File No. 333-187965), as amended, including the prospectus contained therein, to register the issuance and sale of our ordinary shares represented by ADSs in relation to our initial public offering and our

registration statement on Form F-3 (File No. 333-212007), including the prospectus contained therein, to register the proposed sale of our ordinary shares represented by ADSs from time to time by certain of our shareholders. As allowed by the SEC, in Item 19 of this annual report, we incorporate by reference certain information we previously filed with the SEC. This means that we can disclose important information to you by referring you to another document filed separately with the SEC. The information incorporated by reference is considered to be part of this annual report.

You may read and copy this annual report, including the exhibits incorporated by reference in this annual report, at the SEC s Public Reference Room at 100 F Street, N.E., Washington, D.C. 20549 and at the SEC s regional offices in New York, New York and Chicago, Illinois. You can also request copies of this annual report, including the exhibits incorporated by reference in this annual report, upon payment of a duplicating fee, by writing information on the operation of the SEC s Public Reference Room.

The SEC also maintains a website at *www.sec.gov* that contains reports and other information regarding registrants that file electronically with the SEC. Our annual report and some of the other information submitted by us to the SEC may be accessed through this website.

As a foreign private issuer, we are exempt from the rules under the Exchange Act prescribing the furnishing and content of quarterly reports and proxy statements, and officers, directors and principal shareholders are exempt from the reporting and short-swing profit recovery provisions contained in Section 16 of the Exchange Act.

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In accordance with NYSE Rule 203.01, we will post this annual report on our website *ir.lightinthebox.com* . In addition, we will provide hardcopies of our annual report to shareholders, including ADS holders, free of charge upon request.

I. Subsidiary Information

Not applicable.

ITEM 11. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

Market Risks

Interest Rate Risk

Our exposure to interest rate risk primarily relates to the interest income generated by our bank deposits, which are unrestricted as to withdrawal and use, and highly liquid investments that have maturities of three months of less. We have not used any derivative financial instruments to manage our interest risk exposure. Interest-earning instruments carry a degree of interest rate risk. We have not been exposed to material risks due to changes in interest rates. An increase in interest rates, however, may raise the cost of any debt we incur in the future. In addition, our future interest income may be lower than expected due to changes in market interest rates.

Foreign Exchange Risk

Most of our revenues are denominated in U.S. dollars, while some of our expenses are denominated in Renminbi. In addition, our PRC subsidiary and consolidated affiliated entities hold U.S. dollars in PRC bank accounts to pay for certain Renminbi-denominated expenses such as payroll and rent. As such, they are subject to foreign exchange translation differences on their U.S. dollar balances. The foreign exchange impacts relate to accounts payable denominated in Renminbi were approximately negative $49 thousand, negative $65 thousand and positive $595 thousand for the years ended December 31, 2014, 2015 and 2016, respectively, and the foreign exchange impacts relate to the U.S. dollars held by PRC entities with Renminbi as functional currency were approximately positive $1 thousand, negative $6 thousand and $99 thousand for each of the years ended December 31, 2014, 2015 and 2016, respectively. All foreign exchange impact was recorded in general and administrative expenses in our consolidated statement of operations (expect for those exchange impact caused by translation of financial statements, which is recorded in other comprehensive losses in our consolidated statement of operations).

We have no hedges against currency risk. If Renminbi appreciates relative to the U.S. dollar, our cost to acquire products priced in Renminbi and our expenses denominated in Renminbi will become more expensive in U.S. dollars. Consequently, any increase in the value of the Renminbi against the U.S. dollar may reduce our margins, reduce our competiveness against retailers with costs denominated in currencies other

than Renminbi or render us unable to meet our costs.

The value of the Renminbi against the U.S. dollar and other currencies may fluctuate and is affected by, among other things, changes in political and economic conditions and the foreign exchange policy adopted by the PRC government. On July 21, 2005, the PRC government changed its policy of pegging the value of the Renminbi to the U.S. dollar. Under the current policy, the Renminbi is permitted to fluctuate within a narrow and managed band against a basket of certain foreign currencies. Following the removal of the U.S. dollar peg, the Renminbi appreciated more than 20% against the U.S. dollar over the following three years. During the period between July 2008 and June 2010, the Renminbi has traded stably within a narrow range against the U.S. dollar. Since June 2010, the Renminbi has appreciated further against the U.S. dollar, though there have been periods, especially during 2014, when the U.S. dollar has appreciated against the Renminbi as well. Since August 2015, the U.S. dollar has also started to gradually appreciated against the Renminbi. It is difficult to predict how market forces or PRC or U.S. government policy may impact the exchange rate between the Renminbi and the U.S. dollar in the future .

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In addition, many of our customers pay for our products in currencies other than U.S. dollars but we report our financial results in U.S. dollars and, as a result, our financial results may be impacted by fluctuations in foreign currency exchange rates. We sell to customers in over 200 countries and territories. If the U.S. dollar appreciates against these foreign currencies, our translation of foreign currency denominated transactions will results in lower total net revenues, operating expenses and net income. Since January 2014, the U.S. Dollar Index, a measure of the value of the U.S. dollars against a basket of six major world currencies including the euro, has appreciated over 20%. In particular, Europe represented the largest region to which our products were sold in 2016 with our net revenues generated from Europe being 49.6% of our total net revenues in 2016. Since January 2014, the U.S. dollar has, on the whole, been appreciating against the Euro and in March 2015, the Euro fell to a 13-year low against the U.S. dollar with 1 Euro equating 1.04 U.S. dollars. We have no hedges against currency risk. Fluctuations in foreign currency exchange rates could significantly impact our financial results, which may result in an impact on our share prices.

ITEM 12. DESCRIPTION OF SECURITIES OTHER THAN EQUITY SECURITIES

A. Debt Securities

Not applicable.

B. Warrants and Rights

In connection with the issuance of 42,500,000 ordinary shares to Zall E-Commerce in March 2016, we have agreed to issue a warrant to Zall E-Commerce pursuant to which it may subscribe for up to 7,455,000 ordinary shares, equivalent to 3,727,500 ADSs, of our company, at an exercise price of $2.75 per ordinary share, equivalent to $5.50 per ADS, pursuant to the terms and conditions of such warrant. The warrant is exercisable starting from September 30, 2016 and will terminate on March 30, 2018.

C. Other Securities

Not applicable.

D. American Depositary Shares

Fees Paid by Our ADS Holders

As an ADS holder, you will be required to pay the following service fees to the depositary, The Bank of New York Mellon:

Persons depositing or withdrawing shares or ADS holders must pay:	**For:**
$5.00 (or less) per 100 ADSs (or portion of 100 ADSs)	• Issuance of ADSs, including issuances resulting from a distribution of shares or rights or other property • Cancellation of ADSs for the purpose of withdrawal, including if the deposit agreement terminates
$.05 (or less) per ADS	• Any cash distribution to ADS holders
A fee equivalent to the fee that would be payable if securities distributed to you had been shares and the shares had been deposited for issuance of ADSs	• Distribution of securities distributed to holders of deposited securities which are distributed by the depositary to ADS holders
$.05 (or less) per ADS per calendar year	• Depositary services Registration or transfer fees
Registration or transfer fees	• Transfer and registration of shares on our share register to or from the name of the depositary or its agent when you deposit or withdraw shares
Expenses of the depositary	• Cable, telex and facsimile transmissions (when expressly provided in the deposit agreement) • converting foreign currency to U.S. dollars
Taxes and other governmental charges the depositary or the custodian have to pay on any ADS or share underlying an ADS, for example, stock transfer taxes, stamp duty or withholding taxes	• As necessary
Any charges incurred by the depositary or its agents for servicing the deposited securities	• As necessary

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As an ADS holder you will also be responsible to pay certain fees and expenses incurred by the depositary and certain taxes and governmental charges such as:

- Fees for the transfer and registration of ordinary shares charged by the registrar and transfer agent for the ordinary shares in the Cayman Islands (i.e., upon deposit and withdrawal of ordinary shares).

- Expenses incurred for converting foreign currency into U.S. dollars.

- Expenses for cable, telex and fax transmissions and for delivery of securities.

- Taxes and duties upon the transfer of securities (i.e., when ordinary shares are deposited or withdrawn from deposit).

- Fees and expenses incurred in connection with the delivery or servicing of ordinary shares on deposit.

Depositary fees payable upon the issuance and cancellation of ADSs are typically paid to the depositary bank by the brokers (on behalf of their clients) receiving the newly issued ADSs from the depositary bank and by the brokers (on behalf of their clients) delivering the ADSs to the depositary bank for cancellation. The brokers in turn charge these fees to their clients. Depositary fees payable in connection with distributions of cash or securities to ADS holders and the depositary services fee are charged by the depositary bank to the holders of record of ADSs as of the applicable ADS record date.

The Depositary fees payable for cash distributions are generally deducted from the cash being distributed. In the case of distributions other than cash (i.e., stock dividend, rights), the depositary bank charges the applicable fee to the ADS record date holders concurrent with the distribution. In the case of ADSs registered in the name of the investor (whether certificated or uncertificated in direct registration), the depositary bank sends invoices to the applicable record date ADS holders. In the case of ADSs held in brokerage and custodian accounts (via DTC), the depositary bank generally collects its fees through the systems provided by DTC (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 turn charge their clients accounts the amount of the fees paid to the depositary banks.

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

Note that the fees and charges you may be required to pay may vary over time and may be changed by us and by the depositary. You will receive prior notice of such changes.

Fees and Payments from the Depositary to Us

Our depositary has agreed to reimburse us for certain expenses we incur that are related to the administration and maintenance of the ADS program. There are limits on the amount of expenses for which the depositary will reimburse us, but the amount of reimbursement available to us is not related to the amounts of fees the depositary collects from investors. The depositary has reimbursed us for any expenses related to the administration and maintenance of the facility in an amount of $1.2 million in total, after deduction of applicable U.S. taxes.

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PART II

ITEM 13. DEFAULTS, DIVIDEND ARREARAGES AND DELINQUENCIES

None.

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

See Item 10. Additional Information for a description of the rights of securities holders, which remain unchanged.

Our ADSs, each representing two of our ordinary shares, have been listed on the New York Stock Exchange since June 6, 2013 under the symbol LITB. We completed our initial public offering of 9,545,000 ADSs, representing 19,090,000 ordinary shares, at $9.50 per ADS on June 6, 2013 after our ADRs were registered under the Securities Act. The effective date of our registration statement on Form F-1 (File number: 333-187965) was June 6, 2013. Credit Suisse Securities (USA) LLC and Stifel, Nicolaus & Company, Incorporated are acting as joint bookrunners for our initial public offering and as representatives of the underwriters.

For the period from the effective date of our registration statement on Form F-1 to December 31, 2016, all of the net proceeds from our initial public offering had been used to finance our business operations as well as our share repurchase program.

We also filed a registration statement on Form F-3 (File No. 333-212007) in relation to the proposed sale of our ordinary shares represented by ADSs from time to time by certain of our shareholders and we did not and will not receive any of the proceeds from the sale of ADSs by the selling shareholders.

ITEM 15. CONTROLS AND PROCEDURES

Evaluation of Disclosure Controls and Procedures

We maintain disclosure controls and procedures designed to provide reasonable assurance that information required to be disclosed in reports filed under the Exchange Act is recorded, processed, summarized and reported within the specified time periods and accumulated and

communicated to our management, including our chief executive officer and chief financial officer, as appropriate, to allow timely decisions regarding required disclosure.

Our management, under the supervision and with the participation of our principal executive officer and our principal financial officer, evaluated the effectiveness of our disclosure controls and procedures, as defined in Rules 13a-15(e) or 15d-15 (e) promulgated under the Exchange Act, at December 31, 2016. Based on that evaluation, our principal executive officer and principal financial officer have concluded that, as of December 31, 2016, our disclosure controls and procedures were effective in ensuring that material information required to be disclosed in this annual report is recorded, processed, summarized and reported to them for assessment, and required disclosure is made within the time period specified in the rules and forms of the SEC.

Management s Annual Report on Internal Control over Financial Reporting

Our management is responsible for establishing and maintaining adequate internal control over financial reporting as defined in Rules 13a-15(f) and 15d-15(f) under the Securities Exchange Act of 1934, as amended. Our internal control over financial reporting is a process designed to provide reasonable assurance regarding the reliability of our financial reporting and the preparation of financial statements for external purposes in accordance with U.S. GAAP 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 the assets of our company; (2) provide reasonable assurance that transactions are recorded as necessary to permit preparation of consolidated financial statements in accordance with U.S. GAAP, and that receipts and expenditures of our company are being made only in accordance with authorizations of our management and directors; and (3) provide reasonable assurance regarding prevention or timely detection of the unauthorized acquisition, use or disposition of our 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 of our internal control over financial reporting to future periods are subject to the risks that controls may become inadequate because of changes in conditions, or that the degree of compliance with the policies or procedures may deteriorate.

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Our management conducted an evaluation of the effectiveness of our company s internal control over financial reporting as of December 31, 2016 based on the framework in Internal Control Integrated Framework (2013) issued by the Committee of Sponsoring Organizations of the Treadway Commission. Based on this evaluation, our management concluded that our internal control over financial reporting was effective as of December 31, 2016.

Changes in Internal Control over Financial Reporting

In preparing our consolidated financial statements as of and for the year ended December 31, 2016 included in our annual report on Form 20-F for 2016, we identified certain control deficiencies in our internal control over financial reporting. There were no significant changes in our internal control over financial reporting during the period covered by this annual report on Form 20-F that have materially affected, or are reasonably likely to materially affect, our internal control over financial reporting. We may identify additional control deficiencies in the future. Should we discover such deficiencies, we intend to remediate them as soon as possible.

ITEM 16A. AUDIT COMMITTEE FINANCIAL EXPERT

Our Board of Directors has determined that Mr. Sean Shao qualifies as audit committee financial expert as defined in Item 16A of Form 20-F. All three members of our audit committee satisfy the independence requirements of the NYSE rules and Rule 10A-3(b)(1) under the Exchange Act.

ITEM 16B. CODE OF ETHICS

Our board of directors has adopted a code of ethics that applies to our directors, officers, employees and agents, including certain provisions that specifically apply to our executive officers, including our principal executive and financial officers, president and vice presidents and any other persons who perform similar functions for us. We have filed our code of business conduct and ethics as an exhibit to our registration statement on Form F-1 (File Number 333-187965), as amended, initially filed with the SEC on April 17, 2013. The code is also available on our official website under the investor relations section at *http://ir.lightinthebox.com* .

We hereby undertake to provide to any person without charge, a copy of our code of business conduct and ethics within ten working days after we receive such person s written request.

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 Certified Public Accountants LLP, our principal external auditors, for the periods indicated. We did not pay any other

fees to our auditors during the periods indicated below.

	Year Ended December 31,	
	2015	2016
	(in thousands of $)	
Audit Fees (1)	$ 670	$ 690
Audit-related Fees (2)		152
Total	$ 670	$ 842

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(1) Audit fees represent the aggregate fees billed for each of the fiscal years listed for professional services rendered by our principal auditors for the audit of our annual financial statements or services that are normally provided by the auditors in connection with statutory and regulatory filings or engagements.

(2) Audit-related fees represent the aggregate fees billed in each of the fiscal years listed for assurance and related services by our principal auditors for services rendered that are reasonably related to the performance of the audit or review of our consolidated financial statements and are not reported under Audit fees . The fees disclosed under the category of Audit-related fees in 2016 are principally related to services rendered in connection with our registration statement on Form F-3.

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The policy of our audit committee is to pre-approve all audit and non-audit services provided by Deloitte Touche Tohmatsu Certified Public Accountants LLP, including audit services, audit-related services, tax services and other services as described above, other than those for de minimus services which are approved by the Audit Committee prior to the completion of the audit.

ITEM 16D. EXEMPTIONS FROM THE LISTING STANDARDS FOR AUDIT COMMITTEES

Not applicable.

ITEM 16E. PURCHASES OF EQUITY SECURITIES BY THE ISSUER AND AFFILIATED PURCHASERS.

2013 Share Repurchase Program

We announced a share repurchase program approved by our board of directors on December 16, 2013, under which we may repurchase up to $20.0 million worth of our issued and outstanding ADSs. The repurchases have been and will be, made from time to time on the open market at prevailing market prices or in privately negotiated transactions subject to the restrictions relating to volume, price and timing. This share repurchase program was implemented over the course of 12 months from December 16, 2013 to December 15, 2014, in a manner consistent with market conditions, the interest of the shareholders, the trading price of the ADSs and in compliance with relevant rules under the Exchange Act. On December 16, 2014, our board of directors has authorized to extend this share repurchase program for an additional 12-month period from December 16, 2014 to December 15, 2015 with all terms and conditions of the share repurchase program remain unchanged. As of August 31, 2015, we had completed the $20.0 million share repurchase program.

2016 Share Repurchase Program

On June 8, 2016, we announced the implementation of another share repurchase program of up to $10.0 million worth of our outstanding ADSs each representing two of ordinary shares on the open market at prevailing market prices or in privately negotiated transactions from June 15, 2016 through June 14, 2017.

The following table sets forth information about our purchases of outstanding ADSs from June 15, 2016 to March 24, 2017:

Period	Total Number of ADSs Purchased	Average Price Paid per ADS(1)	Total Number of ADSs Purchased as Part of Publicly Announced Plans	Approximate Dollar Value of ADSs that May Yet Be Purchased

			or Programs(2)		Under the Program(2)
June 15, 2016 through June 30, 2016	47,713	3.19	47,713	$	9.8 million
July 2016	1,035	3.25	1,035	$	9.8 million
August 2016	21,312	3.20	21,312	$	9.8 million
September 2016	41,300	2.94	41,300	$	9.7 million
October 2016	37,702	2.74	37,702	$	9.6 million
November 2016	31,739	2.70	31,739	$	9.5 million
December 2016	90,813	2.94	90,813	$	9.2 million
January 2017	25,000	3.02	25,000	$	9.1 million
February 2017	18,796	3.00	18,796	$	9.0 million
March 2017 (through March 24, 2017)	26,922	2.87	26,922	$	9.0 million
Total	342,332	2.95	342,332	$	9.0 million

(1) Each of our ADSs represents two ordinary shares. The average price per ADS is calculated using the execution price for each repurchase excluding commissions paid to brokers.

(2) Under our share purchase program announced in 2016, repurchases of our ADSs have been and will be, made from time to time on the open market at prevailing market prices or in privately negotiated transactions subject to the restrictions relating to volume, price and timing. This share repurchase program will be implemented over the course of 12 months from June 15, 2016 to June 14, 2017, in a manner consistent with market conditions, the interest of the shareholders, the trading price of the ADSs and in compliance with relevant rules under the Exchange Act.

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ITEM 16F. CHANGE IN REGISTRANT S CERTIFYING ACCOUNTANT.

Not applicable.

ITEM 16G. CORPORATE GOVERNANCE.

We are a foreign private issuer (as such term is defined in Rule 3b-4 under the Exchange Act), and our ADSs, each representing two ordinary share, are listed on the New York Stock Exchange. Under Section 303A of the New York Stock Exchange Listed Company Manual, New York Stock Exchange listed companies that are foreign private issuers are permitted to follow home country practice in lieu of the corporate governance provisions specified by the New York Stock Exchange with limited exceptions. The following summarizes some significant ways in which our corporate governance practices differ from those followed by domestic companies under the listing standards of the New York Stock Exchange.

Under the New York Stock Exchange Listed Company Manual, or the NYSE Manual, U.S. domestic listed companies are required to have a compensation committee and a nominating/corporate governance committee, each composed entirely of independent directors, which are not required under the Companies Law (2016 Revision) of the Cayman Islands, our home country. Currently, our compensation committed is composed of three members, only two of whom are independent directors. Our corporate governance and nominating committee is composed of three members, only two of whom are independent directors. The NYSE Manual also requires U.S. domestic listed companies to regularly hold executive sessions for non-management directors, or an executive session that only includes independent directors at least once a year. We are not subject to this requirement under the Cayman Islands law and have decided to follow our home country practice on this matter. In addition, the NYSE Manual requires shareholder approval for certain matters, such as requiring that shareholders must be given the opportunity to vote on all equity compensation plans and material revisions to those plans, which is not required under the Cayman Islands law. We intend to follow the home country practice in determining whether shareholder approval is required.

ITEM 16H. MINE SAFETY DISCLOSURE.

Not applicable.

PART III

ITEM 17. FINANCIAL STATEMENTS.

We have elected to provide financial statements pursuant to Item 18.

ITEM 18. FINANCIAL STATEMENTS.

The following financial statements are filed as part of this annual report, together with the report of the independent auditors:

- Report of Independent Registered Public Accounting Firm
- Consolidated Balance Sheets as of December 31, 2015 and 2016
- Consolidated Statements of Operations for the years ended December 31, 2014, 2015 and 2016
- Consolidated Statements of Comprehensive Loss for the years ended December 31, 2014, 2015 and 2016
- Consolidated Statements of Changes in Equity (Deficit) for the years ended December 31, 2014, 2015 and 2016
- Consolidated Statements of Cash Flows for the years ended December 31, 2014, 2015 and 2016
- Notes to the Consolidated Financial Statements

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ITEM 19. EXHIBITS.

Exhibit Number	Description of Document
1.1*	Fourth Amended and Restated Memorandum and Articles of Association of the Registrant as currently in effect
2.1*	Registrant s Form of Ordinary Share Certificate
2.2	Form of Deposit Agreement between the Registrant and The Bank of New York Mellon, as depositary and Owners and Holders of the American Depositary Shares issued therein
2.3	Form of American depositary receipt evidencing American depositary shares (included in Exhibit 2.2)
2.4*	Second Amended and Restated Shareholders Agreement, dated as of September 28, 2010, among the Registrant, Ceyuan Ventures II, L.P., Ceyuan Ventures Advisors Fund II, LLC, GSR Ventures III, L.P., Banean Holdings Ltd, Trustbridge Partners III, L.P. and certain other persons named therein
2.5*	Amended and Restated Right of First Refusal and Co-Sale Agreement, dated as of September 28, 2010, among the Registrant, Ceyuan Ventures II, L.P., Ceyuan Ventures Advisors Fund II, LLC, GSR Ventures III, L.P., Banean Holdings Ltd, Trustbridge Partners III L.P. and certain other persons named therein
2.6**	Investor Rights Agreement dated as of March 30, 2016 between the Registrant and Zall Cross-Border E-Commerce Investment Company Limited, Mr. Alan Quji Guo and Wincore Holdings Limited
4.1*	Form of Indemnification Agreement between the Registrant and its directors and executive officers
4.2*	Form of Employment Agreement between the Registrant and its executive officers
4.3*	Exclusive Technical and Consulting Service Agreement between Lanting Jishi and Lanting Huitong
4.4*	Business Operation Agreement among Lanting Jishi, Lanting Huitong and Lanting Huitong s shareholders
4.5*	Equity Disposal Agreement among Lanting Jishi, Lanting Huitong and Lanting Huitong s shareholders
4.6*	Share Pledge Agreement among Lanting Jishi, Lanting Huitong and Lanting Huitong s shareholders
4.7*	Powers of Attorney issued by each of Lanting Huitong s shareholders
4.8*	Spousal Consent Letters issued by spouses of certain shareholders of Lanting Huitong
4.9*	Exclusive Technical and Consulting Service Agreement between Lanting Jishi and Lanting Gaochuang
4.10*	Business Operation Agreement among Lanting Jishi, Lanting Gaochuang and Lanting Gaochuang s shareholders
4.11*	Equity Disposal Agreement among Lanting Jishi, Lanting Gaochuang and Lanting Gaochuang s shareholders
4.12*	Share Pledge Agreement among Lanting Jishi, Lanting Gaochuang and Lanting Gaochuang s shareholders
4.13*	Loan Agreement between Mr. Quji (Alan) GUO and Lanting Jishi
4.14*	Powers of Attorney issued by each of Lanting Gaochuang s shareholders
4.15*	Amended and Reinstated 2008 Share Incentive Plan of the Registrant

4.16	Amendment No. 1 to the LightInTheBox Holding Co., Ltd. Amended and Reinstated 2008 Share Incentive Plan
4.17	Subscription Agreement dated as of March 17, 2016 between Zall Cross-Border E-Commerce Investment Company Limited and LighInTheBox Holding Co., Ltd.
4.18**	Warrant to Purchase Ordinary Share of LightInTheBox Holding Co., Ltd. dated as of March 30, 2016 among the Registrant and Zall Cross-Border E-Commerce Investment Company Limited
4.19	Declaration of Trust executed by Mr. Tang Le dated July 4, 2016 as to Light Square Limited
8.1	List of Subsidiaries of the Registrant
11.1*	Code of Business Conduct and Ethics of the Registrant
12.1	Principal Executive Officer Certification Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002

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Exhibit Number	Description of Document
12.2	Principal Financial Officer Certification Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002
13.1***	Principal Executive Officer Certification Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002
13.2***	Principal Financial Officer Certification Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002
15.1	Consent of Deloitte Touche Tohmatsu Certified Public Accountants LLP
15.2	Consent of TransAsia Lawyers
15.3	Consent of Maples and Calder (Hong Kong) LLP
101.INS	XBRL Instance Document
101.SCH	XBRL Taxonomy Extension Schema Document
101.CAL	XBRL Taxonomy Extension Calculation Linkbase Document
101.DEF	XBRL Taxonomy Extension Definition Linkbase Document
101.LAB	XBRL Taxonomy Extension Label Linkbase Document
101.PRE	XBRL Taxonomy Extension Presentation Linkbase Document

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* Previously filed with the Registration Statement on Form F-1 (File No. 333-187965), initially filed on April 17, 2013 and incorporated herein by reference.

Previously filed with the Registration Statement on Form F-6 (File No. 333-188794), dated May 23, 2013 and incorporated herein by reference.

Previously filed with the Registration Statement on Form S-8 (File No. 333-201100), dated December 19, 2014 and incorporated herein by reference.

Incorporated by reference to an exhibit to the Form 6-K (File No. 001-35942) filed with the Securities and Exchange Commission on March 17, 2016.

** Previously filed with our annual report on Form 20-F for the fiscal year ended December 31, 2015 (File No. 001-35942) filed on April 29, 2016 and incorporated herein by reference.

*** Furnished with this annual report on Form 20-F.

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SIGNATURES

The registrant hereby certifies that it meets all of the requirements for filing its annual report on Form 20-F and that it has duly caused and authorized the undersigned to sign this annual report on its behalf.

LightInTheBox Holding Co., Ltd.

By: /s/ Quji (Alan) Guo

Name: Quji (Alan) Guo

Title: Chief Executive Officer and Chairman

Date: March 30, 2017

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LIGHTINTHEBOX HOLDING CO., LTD.

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LIGHTINTHEBOX HOLDING CO., LTD.

REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM

TO THE BOARD OF DIRECTORS AND SHAREHOLDERS OF LIGHTINTHEBOX HOLDING CO., LTD.

We have audited the accompanying consolidated balance sheets of LightInTheBox Holding Co., Ltd. (the Company), its subsidiaries, its variable interest entities (the VIEs) and its VIE s subsidiary (collectively the Group) as of December 31, 2015 and 2016, and the related consolidated statements of operations, comprehensive loss, changes in shareholders equity (deficit), and cash flows for each of the three years in the period ended December 31, 2016. These financial statements are the responsibility of the Group s management. Our responsibility is to express an opinion on these 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. The Group is not required to have, nor were we engaged to perform, an audit of its internal control over financial reporting. Our audits included consideration of internal control over financial reporting as a basis for designing audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Group s internal control over financial reporting. Accordingly, we express no such opinion. An audit also includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements, assessing the accounting principles used and significant estimates made by management, 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 December 31, 2015 and 2016, and the results of its operations and its cash flows for each of the three years in the period ended December 31, 2016, in conformity with accounting principles generally accepted in the United States of America.

/s/ Deloitte Touche Tohmatsu Certified Public Accountants LLP

Beijing, the People s Republic of China

March 30, 2017

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LIGHTINTHEBOX HOLDING CO., LTD.

CONSOLIDATED BALANCE SHEETS

(U.S. dollars in thousands, except share data and per share data, or otherwise noted)

	December 31, 2015	December 31, 2016
ASSETS		
Current assets		
Cash and cash equivalents	$ 30,901	$ 89,517
Restricted cash	1,606	1,559
Accounts receivable	920	2,401
Inventories	11,261	10,587
Prepaid expenses and other current assets	5,053	9,674
Total current assets	49,741	113,738
Property and equipment, net	2,209	1,071
Intangible assets, net	232	215
Goodwill	690	690
Long-term rental deposit	658	638
Long-term investment	1,963	1,849
TOTAL ASSETS	$ 55,493	$ 118,201
LIABILITIES AND SHAREHOLDERS EQUITY		
Current Liabilities		
Accounts payable (including accounts payable of the consolidated VIEs without recourse to LightInTheBox Holding Co., Ltd. of $22 and $20 as of December 31, 2015 and December 31, 2016, respectively)	$ 29,351	$ 22,523
Advance from customers (including advance from customers of the consolidated VIEs without recourse to LightInTheBox Holding Co., Ltd. of nil and nil as of December 31, 2015 and December 31, 2016, respectively)	8,282	8,758
Accrued expenses and other current liabilities (including accrued expenses and other current liabilities of the consolidated VIEs without recourse to LightInTheBox Holding Co., Ltd. of $1,760 and $1,537 as of December 31, 2015 and December 31, 2016, respectively)	19,983	21,084
Total current liabilities	57,616	52,365
TOTAL LIABILITIES	$ 57,616	$ 52,365
SHAREHOLDERS EQUITY (DEFICIT)		
Ordinary shares ($0.000067 par value; 750,000,000 shares authorized; 101,847,447 and 145,754,507 shares issued as of December 31, 2015 and December 31, 2016 respectively; 94,456,773 and 137,820,605 shares outstanding as of December 31, 2015 and December 31, 2016 respectively)	$ 7	$ 10
Additional paid-in capital	159,190	236,949
Treasury shares, at cost (7,390,674 and 7,933,902 shares as of December 31, 2015, and December 31, 2016 respectively)	(19,996)	(20,806)
Accumulated deficit	(141,015)	(149,738)
Accumulated other comprehensive loss	(309)	(579)
TOTAL SHAREHOLDERS EQUITY (DEFICIT)	(2,123)	65,836
TOTAL LIABILITIES AND SHAREHOLDERS EQUITY	$ 55,493	$ 118,201

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

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LIGHTINTHEBOX HOLDING CO., LTD.

CONSOLIDATED STATEMENTS OF OPERATIONS

(U.S. dollars in thousands, except share data and per share data, or otherwise noted)

	Years ended December 31		
	2014	**2015**	**2016**
Net revenues			
Product sales	$ 382,282	$ 312,332	$ 262,083
Services	125	11,431	30,404
Total net revenues	382,407	323,763	292,487
Cost of revenues			
Product sales	236,982	196,753	160,566
Services	113	10,601	28,371
Total cost of revenues	237,095	207,354	188,937
Gross profit	145,312	116,409	103,550
Operating expenses:			
Fulfillment	23,926	22,419	17,052
Selling and marketing	105,186	91,614	61,090
General and administrative	46,916	41,535	34,492
Total operating expenses	176,028	155,568	112,634
Loss from operations	(30,716)	(39,159)	(9,084)
Exchange loss on offshore bank accounts	(1,556)	(938)	(120)
Interest income	2,355	773	518
Total other income (loss)	799	(165)	398
Loss before income taxes	(29,917)	(39,324)	(8,686)
Income taxes expenses	(70)	(49)	(54)
(Loss) gain from long-term investment		(34)	17
Net loss	(29,987)	(39,407)	(8,723)
Net loss attributable to ordinary shareholders	$ (29,987)	$ (39,407)	$ (8,723)
Net loss per ordinary share-basic	$ (0.30)	$ (0.41)	$ (0.07)
Net loss per ordinary share-diluted	$ (0.30)	$ (0.41)	$ (0.07)

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

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LIGHTINTHEBOX HOLDING CO., LTD.

CONSOLIDATED STATEMENTS OF COMPREHENSIVE LOSS

(U.S. dollars in thousands, or otherwise noted)

	Years ended December 31		
	2014	2015	2016
Net loss	$ (29,987)	$ (39,407)	$ (8,723)
Other comprehensive loss, net of tax:			
Foreign currency translation adjustment, net of tax of nil	(12)	(178)	(270)
Total comprehensive loss	$ (29,999)	$ (39,585)	$ (8,993)

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

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LIGHTINTHEBOX HOLDING CO., LTD.

CONSOLIDATED STATEMENTS OF CHANGES IN SHAREHOLDERS EQUITY (DEFICIT)

(U.S. dollars in thousands, except share data and per share data, or otherwise noted)

	Ordinary Shares		Additional Paid-in Capital	Treasury shares at cost	Accumulated Other Comprehensive Loss	Accumulated Deficit	Total shareholders Equity (Deficit)
	Shares	Amount					
Balance at January1, 2014	99,194,991	$ 7	$ 153,124	$	$ (119)	$ (71,621)	$ 81,391
Issuance of ordinary shares upon vesting of nonvested shares	611,010						
Exercise of share options	548,800		230				230
Share-based compensation			2,518				2,518
Repurchase of ordinary shares	(3,737,452)			(10,957)			(10,957)
Net loss						(29,987)	(29,987)
Foreign currency translation adjustment					(12)		(12)
Balance at December 31, 2014	96,617,349	7	155,872	(10,957)	(131)	(101,608)	43,183
Issuance of ordinary shares upon vesting of nonvested shares	1,316,696						
Exercise of share options	175,950		122				122
Share-based compensation			3,196				3,196
Repurchase of ordinary shares	(3,653,222)			(9,039)			(9,039)
Net loss						(39,407)	(39,407)
Foreign currency translation adjustment					(178)		(178)
Balance at December 31, 2015	94,456,773	7	159,190	(19,996)	(309)	(141,015)	(2,123)
Issuance of ordinary shares upon private placement, net of issuance costs	42,500,000	3	75,420				75,423
Issuance of ordinary shares upon vesting of nonvested shares	1,367,560						
Exercise of share options	39,500		22				22
Share-based compensation			2,317				2,317

three and six months ended June 30, 2017 and 2016, the Company had no material impairments related to these assets.

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Financial Instruments Measured at Other Than Fair Value

The following tables disclose the estimated fair value of the Company's financial assets and financial liabilities that are not required to be carried at fair value (dollars in millions):

	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)	Total	Carrying Value
Balance at June 30, 2017					
Assets					
States and political subdivisions of states	$ —	$ 1	$ —	$ 1	$ 1
Residential mortgage-backed securities - Agency	—	179	—	179	179
Held-to-maturity investment securities	$ —	$ 180	$ —	$ 180	$ 180
Cash and cash equivalents	$ 12,950	$ —	$ —	$ 12,950	$ 12,950
Restricted cash	$ 93	$ —	$ —	$ 93	$ 93
Net loan receivables	$ —	$ —	$ 78,819	$ 78,819	$ 75,613
Accrued interest receivables	$ —	$ 746	$ —	$ 746	$ 746
Liabilities					
Deposits	$ —	$ 53,024	$ —	$ 53,024	$ 52,864
Long-term borrowings - owed to securitization investors	$ —	$ 16,127	$ 743	$ 16,870	$ 16,738
Other long-term borrowings	$ —	$ 10,222	$ —	$ 10,222	$ 9,700
Accrued interest payables	$ —	$ 191	$ —	$ 191	$ 191
Balance at December 31, 2016					
Assets					
States and political subdivisions of states	$ —	$ 2	$ —	$ 2	$ 2
Residential mortgage-backed securities - Agency	—	150	—	150	150
Held-to-maturity investment securities	$ —	$ 152	$ —	$ 152	$ 152
Cash and cash equivalents	$ 11,914	$ —	$ —	$ 11,914	$ 11,914
Restricted cash	$ 95	$ —	$ —	$ 95	$ 95
Net loan receivables	$ —	$ —	$ 78,252	$ 78,252	$ 75,087
Accrued interest receivables	$ —	$ 724	$ —	$ 724	$ 724
Liabilities					
Deposits	$ —	$ 52,183	$ —	$ 52,183	$ 51,992
Long-term borrowings - owed to securitization investors	$ —	$ 15,617	$ 900	$ 16,517	$ 16,411
Other long-term borrowings	$ —	$ 9,470	$ —	$ 9,470	$ 9,032
Accrued interest payables	$ —	$ 168	$ —	$ 168	$ 168

The fair values of these financial assets and liabilities, which are not carried at fair value on the condensed consolidated statements of financial condition, were determined by applying the fair value provisions discussed herein. The use of different assumptions or estimation techniques may have a material effect on these estimated fair value amounts. The following describes the valuation techniques of these financial instruments measured at other than fair value.

Cash and Cash Equivalents

The carrying value of cash and cash equivalents approximates fair value due to the low level of risk these assets present to the Company as well as the relatively liquid nature of these assets, particularly given their short maturities.

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Restricted Cash
The carrying value of restricted cash approximates fair value due to the low level of risk these assets present to the Company as well as the relatively liquid nature of these assets, particularly given their short maturities.
Held-to-Maturity Investment Securities
Held-to-maturity investment securities consist of residential mortgage-backed securities issued by agencies and municipal bonds. The fair value of residential mortgage-backed securities included in the held-to-maturity portfolio is estimated similarly to residential mortgage-backed securities carried at fair value on a recurring basis discussed herein. Municipal bonds are valued based on quoted market prices for the same or similar securities.
Net Loan Receivables
The Company's loan receivables are comprised of credit card and installment loans, including the PCI student loans. Fair value estimates are derived utilizing discounted cash flow analyses, the calculations of which are performed on groupings of loan receivables that are similar in terms of loan type and characteristics. Inputs to the cash flow analysis of each grouping consider recent prepayment trends and seasonality factors, if appropriate, as well as interest accrual estimates based on recent yields. The expected future cash flows, derived through the cash flow analysis, of each grouping are discounted at rates at which similar loans within each grouping could be originated under current market conditions. Significant inputs to the fair value measurement of the loan portfolio are unobservable and, as such, are classified as Level 3.
Accrued Interest Receivables
The carrying value of accrued interest receivables, which is included in other assets on the condensed consolidated statements of financial condition, approximates fair value as it is due in less than one year.
Deposits
The carrying values of money market deposits, savings deposits and demand deposits approximate fair value due to the potentially liquid nature of these deposits. For time deposits for which readily available market rates do not exist, fair values are estimated by discounting expected future cash flows using market rates currently offered for deposits with similar remaining maturities.
Long-Term Borrowings - Owed to Securitization Investors
Fair values of long-term borrowings owed to credit card securitization investors are determined utilizing quoted market prices of the same transactions and, as such, are classified as Level 2. Fair values of long-term borrowings owed to student loan securitization investors are calculated by discounting cash flows using estimated assumptions including, among other things, maturity and market discount rates. A portion of the difference between the carrying value and the fair value of the long-term borrowings owed to student loan securitization investors relates to purchase accounting adjustments recorded in connection with the December 2010 purchase of SLC. Significant inputs to these fair value measurements are unobservable and, as such, are classified as Level 3.
Other Long-Term Borrowings
Fair values of other long-term borrowings, consisting of subordinated and senior debt, are determined utilizing current observable market prices for those transactions and, as such, are classified as Level 2. A portion of the difference between the carrying value and the fair value of other long-term borrowings relates to the cash premiums paid in connection with the 2012 fiscal year debt exchanges.
Accrued Interest Payables
The carrying value of accrued interest payables, which is included in accrued expenses and other liabilities on the condensed consolidated statements of financial condition, approximates fair value as it is payable in less than one year.

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14. Derivatives and Hedging Activities

The Company uses derivatives to manage its exposure to various financial risks. The Company does not enter into derivatives for trading or speculative purposes. Certain derivatives used to manage the Company's exposure to interest rate movements and other identified risks are not designated as hedges and do not qualify for hedge accounting. Derivatives may give rise to counterparty credit risk, which generally is addressed through collateral arrangements as described under the sub-heading "— Collateral Requirements and Credit-Risk Related Contingency Features." The Company enters into derivative transactions with established dealers that meet minimum credit criteria established by the Company. All counterparties must be pre-approved prior to engaging in any transaction with the Company. Counterparties are monitored on a regular basis by the Company to ensure compliance with the Company's risk policies and limits. In determining the counterparty credit risk valuation adjustment for the fair values of derivatives, the Company considers collateral and legally enforceable master netting agreements that mitigate credit exposure to related counterparties.

All derivatives are recorded in other assets at their gross positive fair values and in accrued expenses and other liabilities at their gross negative fair values. See Note 13: Fair Value Measurements and Disclosures for a description of the valuation methodologies of derivatives. Cash collateral posted and held balances are recorded in other assets and deposits, respectively, in the condensed consolidated statements of financial condition. Collateral amounts recorded in the condensed consolidated statements of financial condition are based on the net collateral posted or held position for each applicable legal entity's master netting arrangement with each counterparty. Effective in the first quarter of 2017, certain cash collateral amounts associated with derivative positions that are cleared through an exchange are now legally characterized as settlement of the derivative positions. This change results in such collateral amounts being reflected as offsets to the associated derivatives balances recorded in other assets or in accrued expenses and other liabilities, instead of as collateral in other assets or deposits. There is no change to the presentation in the condensed consolidated statements of financial condition of collateral related to positions that are not cleared through an exchange.

Derivatives Designated as Hedges

Derivatives designated and qualifying as a hedge of the exposure to variability in expected future cash flows arising from changes in interest rates, or other types of forecasted transactions, are considered cash flow hedges. Derivatives designated and qualifying as a hedge of the exposure to changes in the fair value of an asset, liability, or firm commitment attributable to a particular risk, such as interest rate risk, are considered fair value hedges.

Cash Flow Hedges

The Company uses interest rate swaps to manage its exposure to changes in interest rates related to future cash flows resulting from interest payments on credit card securitized debt and deposits. The Company's outstanding cash flow hedges are for an initial maximum period of seven years for securitized debt and deposits. The derivatives are designated as hedges of the risk of changes in cash flows on the Company's LIBOR or Federal Funds rate-based interest payments, and qualify for hedge accounting in accordance with ASC Topic 815, Derivatives and Hedging ("ASC 815").

The effective portion of the change in the fair value of derivatives designated as cash flow hedges is recorded in OCI and is subsequently reclassified into earnings in the period that the hedged forecasted cash flows affect earnings. The ineffective portion of the change in fair value of the derivative, if any, is recognized directly in earnings. Amounts reported in AOCI related to derivatives at June 30, 2017 will be reclassified to interest expense as interest payments are made on certain of the Company's floating-rate securitized debt or deposits. During the next 12 months, the Company estimates it will reclassify $9 million of pretax losses to interest expense related to its derivatives designated as cash flow hedges.

Fair Value Hedges

The Company is exposed to changes in fair value of certain of its fixed-rate debt obligations due to changes in interest rates. The Company uses interest rate swaps to manage its exposure to changes in fair value of certain fixed-rate senior notes, securitized debt, bank notes and interest-bearing brokered deposits attributable to changes in LIBOR, a benchmark interest rate as defined by ASC 815. These interest rate swaps qualify as fair value hedges in accordance with ASC 815. Changes in both (i) the fair values of the derivatives and (ii) the hedged fixed-rate senior notes,

securitized debt, bank notes and interest-bearing brokered deposits relating to the risk being hedged are recorded in interest expense. The changes generally provide substantial offset to one another, with any difference, or ineffectiveness recorded in interest expense. Any basis differences between the fair value and the carrying amount of the hedged item at the inception of the hedging relationship are amortized to interest expense.

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Derivatives Not Designated as Hedges

Foreign Exchange Forward Contracts

The Company has foreign exchange forward contracts that are economic hedges and are not designated as accounting hedges. The Company enters into foreign exchange forward contracts to manage foreign currency risk. Changes in the fair value of these contracts are recorded in other income.

Derivatives Cleared Through an Exchange

Effective January 3, 2017, the Chicago Mercantile Exchange ("CME") changed the legal characterization of cash variation margin payments on derivatives cleared through its exchange as "settlements" rather than as "collateral". The Company currently utilizes only CME for all cleared transactions. The International Swaps and Derivatives Association ("ISDA") outlined their conclusions regarding the impact of the change, stating that variation margin payments that are legally considered settlement payments should be accounted for with corresponding derivative positions as one unit of account and should no longer be accounted for separately as collateral. The Securities and Exchange Commission staff did not object to the ISDA's conclusions. The results of the change are reflected in the table below for the current period. With settlement payments on derivative positions cleared through the CME reflected as offsets to the associated derivative asset and liability balances, the fair values of derivative instruments and collateral balances shown are generally reduced. At June 30, 2017, the change resulted in a decrease of $64 million in both derivative assets/liabilities and collateral posted on the condensed consolidated statements of financial condition.

Derivatives Activity

The following table summarizes the fair value (including accrued interest) and outstanding notional amounts of derivative instruments and related collateral balances (dollars in millions):

	June 30, 2017				December 31, 2016		
	Notional Amount	Number of Outstanding Derivative Contracts	Derivative Assets	Derivative Liabilities	Notional Amount	Derivative Assets	Derivative Liabilities
Derivatives designated as hedges							
Interest rate swaps—cash flow hedge[1]	$3,800	7	$ 3	$ 9	$3,700	$ —	$ 22
Interest rate swaps—fair value hedge[1]	$5,645	31	2	4	$6,208	7	72
Derivatives not designated as hedges							
Foreign exchange forward contracts[2]	$12	6	—	—	$13	—	—
Interest rate swap	$—	—	—	—	$149	—	—
Total gross derivative assets/liabilities[3]			5	13		7	94
Less: Collateral held/posted[4]			(1)	(13)		(2)	(94)
Total net derivative assets/liabilities			$ 4	$ —		$ 5	$ —

(1) Effective in the first quarter of 2017, certain cash collateral amounts (variation margin) associated with derivative positions that are cleared through an exchange are reflected as offsets to the associated derivative asset and derivative liability balances, generally reducing the fair values to approximately zero. The affected contracts remain term instruments and are reflected in notional amounts and number of outstanding derivative contracts.

(2) The foreign exchange forward contracts have notional amounts of EUR 7 million, GBP 2 million and SGD 1 million as of June 30, 2017 and notional amounts of EUR 6 million, GBP 5 million and SGD 1 million as of December 31, 2016.

(3) In addition to the derivatives disclosed in the table, the Company enters into forward contracts to purchase when-issued mortgage-backed securities as part of its community reinvestment initiatives. At June 30, 2017, the Company had one outstanding contract with a notional amount of $2 million and immaterial fair value. At December 31, 2016, the Company had one outstanding contract with a notional amount of $36 million and immaterial fair value.

(4)

Collateral amounts, which consist of both cash and investment securities, are limited to the related derivative asset/liability balance and do not include excess collateral received/pledged. Effective in the first quarter of 2017, collateral held/posted excludes amounts that are recorded as offsets to the associated derivative asset or derivative liability balances.

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The following tables summarize the impact of the derivative instruments on income and OCI and indicates where within the condensed consolidated financial statements such impact is reported (dollars in millions):

	Location	Amount of Gain (Loss) Recognized in OCI			
		For the Three Months Ended June 30,		For the Six Months Ended June 30,	
		2017	2016	2017	2016
Derivatives designated as hedges					
Interest rate swaps - cash flow/net investment hedges					
Total gain (loss) recognized in OCI after amounts reclassified into earnings, pre-tax	OCI	$8	$(10)	$19	$(53)
Total gain (loss) recognized in OCI		$8	$(10)	$19	$(53)

	Location	Amount of (Loss) Gain Recognized in Income			
		For the Three Months Ended June 30,		For the Six Months Ended June 30,	
		2017	2016	2017	2016
Derivatives designated as hedges					
Interest rate swaps - cash flow hedges					
Amount reclassified from OCI into income	Interest Expense	$(3)	$(9)	$(8)	$(18)
Total amount reclassified from OCI into income on cash flow hedges		(3)	(9)	(8)	(18)
Interest rate swaps - fair value hedges					
Gain (loss) on interest rate swaps		13	13	(3)	44
(Loss) Gain on hedged items		(12)	(13)	4	(44)
Net ineffectiveness gain	Interest Expense	1	—	1	—
Increase to interest expense related to net settlements on interest rate swaps	Interest Expense	2	8	8	17
Total gain on fair value hedges		3	8	9	17
Total gain (loss) on derivatives designated as hedges recognized in income		$—	$(1)	$1	$(1)
Derivatives not designated as hedges					
Total (loss) gain on derivatives not designated as hedges recognized in income	Other Income	$(1)	$1	$(1)	$—

Collateral Requirements and Credit-Risk Related Contingency Features

The Company has master netting arrangements and minimum collateral posting thresholds with its counterparties for its fair value and cash flow hedge interest rate swaps and foreign exchange forward contracts. The Company has not

sought a legal opinion in relation to the enforceability of its master netting arrangements and, as such, does not report any of these positions on a net basis. Collateral is required by either the Company or its subsidiaries or the counterparty depending on the net fair value position of these derivatives held with that counterparty. The Company may also be required to post collateral with a counterparty for its fair value and cash flow hedge interest rate swaps depending on the credit rating it or Discover Bank receives from specified major credit rating agencies. Collateral receivable or payable amounts are generally not offset against the fair value of these derivatives, but are recorded separately in other assets or deposits. However, effective in the first quarter of 2017, certain cash collateral amounts related to positions cleared through an exchange are reflected as offsets to the associated derivatives balances recorded in other assets and accrued expenses and other liabilities.

At June 30, 2017, Discover Bank’s credit rating met specified thresholds set by its counterparties. However, if its credit rating is reduced by one rating notch, Discover Bank would be required to post additional collateral. The amount of

additional collateral as of June 30, 2017 would have been $38 million. DFS (Parent Company) had no outstanding derivatives as of June 30, 2017, therefore, no collateral was required.

The Company also has agreements with certain of its derivative counterparties that contain a provision where if the Company defaults on any of its indebtedness, including default where repayment of the indebtedness has not been accelerated by the lender, then the Company could also be declared in default on its derivative obligations.

15. Segment Disclosures

The Company's business activities are managed in two segments: Direct Banking and Payment Services.

- Direct Banking: The Direct Banking segment includes Discover-branded credit cards issued to individuals on the Discover Network and other consumer products and services, including private student loans, personal loans, home equity loans, and other consumer lending and deposit products. The majority of Direct Banking revenues relate to interest income earned on the segment's loan products. Additionally, the Company's credit card products generate substantially all revenues related to discount and interchange, protection products and loan fee income.
- Payment Services: The Payment Services segment includes PULSE, an automated teller machine, debit and electronic funds transfer network; Diners Club, a global payments network; and the Company's Network Partners business, which provides payment transaction processing and settlement services on the Discover Network. The majority of Payment Services revenues relate to transaction processing revenue from PULSE and royalty and licensee revenue from Diners Club.

The business segment reporting provided to and used by the Company's chief operating decision maker is prepared using the following principles and allocation conventions:

- The Company aggregates operating segments when determining reportable segments.
- Corporate overhead is not allocated between segments; all corporate overhead is included in the Direct Banking segment.
- Through its operation of the Discover Network, the Direct Banking segment incurs fixed marketing, servicing and infrastructure costs that are not specifically allocated among the segments, with the exception of an allocation of direct and incremental costs driven by the Company's Payment Services segment.
- The assets of the Company are not allocated among the operating segments in the information reviewed by the Company's chief operating decision maker.
- The revenues of each segment are derived from external sources. The segments do not earn revenue from intercompany sources.
- Income taxes are not specifically allocated between the operating segments in the information reviewed by the Company's chief operating decision maker.

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The following table presents segment data (dollars in millions):

	Direct Banking	Payment Services	Total
For the Three Months Ended June 30, 2017			
Interest income			
Credit card loans	$ 1,916	$ —	$ 1,916
Private student loans	127	—	127
PCI student loans	41	—	41
Personal loans	207	—	207
Other	47	—	47
Total interest income	2,338	—	2,338
Interest expense	400	—	400
Net interest income	1,938	—	1,938
Provision for loan losses	639	1	640
Other income	408	73	481
Other expense	876	36	912
Income before income tax expense	$ 831	$ 36	$ 867
For the Three Months Ended June 30, 2016			
Interest income			
Credit card loans	$ 1,734	$ —	$ 1,734
Private student loans	110	—	110
PCI student loans	47	—	47
Personal loans	171	—	171
Other	28	—	28
Total interest income	2,090	—	2,090
Interest expense	339	—	339
Net interest income	1,751	—	1,751
Provision for loan losses	411	1	412
Other income	396	69	465
Other expense	868	38	906
Income before income tax expense	$ 868	$ 30	$ 898

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The following table presents segment data (dollars in millions):

	Direct Banking	Payment Services	Total
For the Six Months Ended June 30, 2017			
Interest income			
Credit card loans	$ 3,792	$ —	$ 3,792
Private student loans	251	—	251
PCI student loans	82	—	82
Personal loans	405	—	405
Other	86	—	86
Total interest income	4,616	—	4,616
Interest expense	786	—	786
Net interest income	3,830	—	3,830
Provision for loan losses	1,233	(7)	1,226
Other income	783	145	928
Other expense	1,725	72	1,797
Income before income tax expense	$ 1,655	$ 80	$ 1,735
For the Six Months Ended June 30, 2016			
Interest income			
Credit card loans	$ 3,467	$ —	$ 3,467
Private student loans	217	—	217
PCI student loans	96	—	96
Personal loans	338	—	338
Other	56	—	56
Total interest income	4,174	—	4,174
Interest expense	673	—	673
Net interest income	3,501	—	3,501
Provision for loan losses	834	2	836
Other income	802	137	939
Other expense	1,719	73	1,792
Income before income tax expense	$ 1,750	$ 62	$ 1,812

16. Subsequent Events

The Company has evaluated events and transactions that have occurred subsequent to June 30, 2017 and determined that there were no subsequent events that would require recognition or disclosure in the condensed consolidated financial statements.

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

The following discussion and analysis of our financial condition and results of operations should be read in conjunction with our condensed consolidated financial statements and related notes included elsewhere in this quarterly report. This quarterly report contains forward-looking statements within the meaning of the Private Securities Litigation Reform Act of 1995. Such statements, which speak to our expected business and financial performance, among other matters, contain words such as “believe,” “expect,” “anticipate,” “intend,” “plan,” “aim,” “will,” “m “should,” “could,” “would,” “likely,” and similar expressions. Such statements are based upon the current beliefs and expectations of our management and are subject to significant risks and uncertainties. Actual results may differ materially from those set forth in the forward-looking statements. These forward-looking statements speak only as of the date of this quarterly report, and there is no undertaking to update or revise them as more information becomes available.

The following factors, among others, could cause actual results to differ materially from those set forth in the forward-looking statements: changes in economic variables, such as the availability of consumer credit, the housing market, energy costs, the number and size of personal bankruptcy filings, the rate of unemployment, the levels of consumer confidence and consumer debt and investor sentiment; the impact of current, pending and future legislation, regulation, supervisory guidance and regulatory and legal actions, including, but not limited to, those related to financial regulatory reform, consumer financial services practices, anti-corruption and funding, capital and liquidity; the actions and initiatives of current and potential competitors; our ability to manage our expenses; our ability to successfully achieve card acceptance across our networks and maintain relationships with network participants; our ability to sustain and grow our private student loan, personal loan and home equity loan products; losses as a result of mortgage loan repurchase and indemnification obligations to secondary market purchasers; difficulty obtaining regulatory approval for, financing, transitioning, integrating or managing the expenses of acquisitions of or investments in new businesses, products or technologies; our ability to manage our credit risk, market risk, liquidity risk, operational risk, legal and compliance risk and strategic risk; the availability and cost of funding and capital; access to deposit, securitization, equity, debt and credit markets; the impact of rating agency actions; the level and volatility of equity prices, commodity prices and interest rates, currency values, investments, other market fluctuations and other market indices; losses in our investment portfolio; limits on our ability to pay dividends and repurchase our common stock; limits on our ability to receive payments from our subsidiaries; fraudulent activities or material security breaches of key systems; our ability to remain organizationally effective; our ability to increase or sustain Discover card usage or attract new customers; our ability to maintain relationships with merchants; the effect of political, economic and market conditions, geopolitical events and unforeseen or catastrophic events; our ability to introduce new products and services; our ability to manage our relationships with third-party vendors; our ability to maintain current technology and integrate new and acquired systems; our ability to collect amounts for disputed transactions from merchants and merchant acquirers; our ability to attract and retain employees; our ability to protect our reputation and our intellectual property; and new lawsuits, investigations or similar matters or unanticipated developments related to current matters. We routinely evaluate and may pursue acquisitions of or investments in businesses, products, technologies, loan portfolios or deposits, which may involve payment in cash or our debt or equity securities.

Additional factors that could cause our results to differ materially from those described below can be found in this section in this quarterly report and in “Risk Factors,” “Business—Competition,” “Business—Supervision and Regulation” and “Management’s Discussion and Analysis of Financial Condition and Results of Operations” in our annual report on Form 10-K for the year ended December 31, 2016, which is filed with the SEC and available at the SEC’s internet site (http://www.sec.gov).

Introduction and Overview

Discover Financial Services ("DFS") is a direct banking and payment services company. We provide direct banking products and services and payment services through our subsidiaries. We offer our customers credit card loans, private student loans, personal loans, home equity loans and deposit products. We also operate the Discover Network, the PULSE network (“PULSE”) and Diners Club International (“Diners Club”). The Discover Network processes transactions for Discover-branded credit cards and provides payment transaction processing and settlement services. PULSE

operates an electronic funds transfer network, providing financial institutions issuing debit cards on the PULSE network with access to ATMs domestically and internationally, as well as point-of-sale terminals at retail locations throughout the U.S. for debit card transactions. Diners Club is a global payments network of licensees, which are generally financial institutions, that issue Diners Club branded charge cards and/or provide card acceptance services. Our primary revenues consist of interest income earned on loan receivables and fees earned from customers, financial institutions, merchants and issuers. The primary expenses required to operate our business include funding costs (interest

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expense), loan loss provisions, customer rewards and expenses incurred to grow, manage and service our loan receivables and networks. Our business activities are funded primarily through consumer deposits, securitization of loan receivables and the issuance of unsecured debt.

Quarter Highlights

- Net income for the three months ended June 30, 2017 was $546 million compared to $616 million for the same period in 2016.
- Total loans grew $6.1 billion, or 8%, from June 30, 2016 to $78.0 billion.
- Credit card loans grew $4.6 billion, or 8%, to $61.8 billion, and Discover card sales volume increased 5% from June 30, 2016.
- Net charge-off rate excluding PCI loans increased 52 basis points from the prior year to 2.79% and the credit card delinquency rate for loans over 30 days past due increased 37 basis points from the prior year to 2.00%.
- Direct-to-consumer deposits grew $3.6 billion, or 11%, from the prior year to $37.7 billion.
- Payment Services transaction dollar volume for the segment was $50.1 billion, up 12% from the prior year.
- We received a non-objection to our 2017 Comprehensive Capital Analysis and Review ("CCAR") submission from the Federal Reserve.

Outlook

We plan on continuing to provide strong capital returns to shareholders and proceed to execute against our 2017 capital plan. This plan includes our recently increased quarterly dividend and share repurchase program. We will continue to invest in marketing and rewards to drive growth in our receivables, which we expect will result in higher interest income levels. Investments in marketing and infrastructure are expected to continue in the second half of 2017. We remain focused on utilizing our rewards programs to support growth, which is expected to result in a higher rewards rate year over year.

Along with expected loan growth, we expect net interest margin to increase slightly during the year, driven by our balance sheet positioning for anticipated interest rate increases. Our total charge-off rate is also expected to be higher in comparison to the prior year. We expect to add to the loan loss reserve to provide for the seasoning of recent loan growth and increasing consumer leverage.

In our payments segment, we continue to pursue new ways to drive volume growth while we expect competition to remain intense. We continue to leverage our network to support our card-issuing business.

Regulatory Environment and Developments

In recent years, federal banking regulators have implemented and continue to propose and finalize new regulations and supervisory guidance, including under the Dodd-Frank Wall Street Reform and Consumer Protection Act (the "Dodd-Frank Act"). Regulators have also increased their examination and enforcement action activities. The Dodd-Frank Act creates a framework for regulation of large systemically significant financial firms, including Discover, through a variety of measures, including increased capital and liquidity requirements and limits on leverage and enhanced supervisory authority. The Dodd-Frank Act contains comprehensive provisions governing the practices and oversight of financial institutions as well as other participants in the financial markets. We expect regulators to continue taking formal enforcement actions against financial institutions in addition to addressing concerns through non-public supervisory actions or findings. While the new Congress and Administration have expressed support for Dodd-Frank modifications that could reduce regulatory burdens through a variety of channels including executive action, rulemaking and legislation, prospects for the enactment of significant changes are uncertain.

The impact of the evolving regulatory environment on our business and operations depends upon a number of factors, including supervisory priorities and actions, our actions, those of our competitors and other marketplace participants, and the behavior of consumers. Regulatory developments, enforcement actions, findings and ratings could affect supervisory priorities, actions, and rule-making, as well as negatively impact our business strategies, require us to limit or change our business practices, limit our product offerings, invest more management time and resources in compliance efforts, limit the fees we can charge for services, limit our ability to pursue certain business opportunities and obtain related required regulatory approvals, or change how we compensate certain of our employees. For example, in 2016, federal banking

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regulators issued a proposed rulemaking on incentive compensation. Unlike the principles-based 2010 Interagency Guidance on Sound Incentive Compensation Policies, the proposed rule is prescriptive in nature and would require an extensive restructuring of incentive compensation practices for certain employees, including our executives. Any changes to our business or compensation structure arising out of this rule could impact our ability to attract, hire or retain certain personnel. The timing and substance of the final rule are unknown. For more information on recent matters affecting Discover, see Note 12: Litigation and Regulatory Matters to our condensed consolidated financial statements. Regulatory developments, enforcement actions, findings and ratings could also have an impact on our strategies, the value of our assets, or otherwise adversely affect our businesses.

As a result of the growing cybersecurity threat and the mounting number of incidents involving unauthorized access to consumer information, banking regulators and policymakers at the federal and state levels are increasingly focused on measures to enhance data security and incident response capabilities. The Federal Financial Institutions Examination Council recently revised examiner guidance for evaluating the adequacy of a financial institution's information security program and associated risk management practices. In addition, in October 2016, federal banking regulators issued an advanced notice of proposed rulemaking that provides for enhanced cyber risk management standards to increase the operational resilience of large financial services firms and reduce the systemic impact of a cybersecurity event. The timing and final form of any final rule is uncertain at this time. Legislation at various levels of government has also been proposed to address security breach notification. While it is too early to know their impact, these developments could ultimately result in the imposition of requirements on Discover and other card issuers or networks that could increase costs or adversely affect the competitiveness of our credit card or debit card products.

Compliance expenditures have increased significantly for Discover and other financial services firms, and we expect them to continue to increase as regulators remain focused on controls and operational processes. We may face additional compliance and regulatory risk to the extent that we enter into new business arrangements with third-party service providers, alternative payment providers or other industry participants. The additional expense, time and resources needed to comply with ongoing regulatory requirements may adversely impact our business and results of operations.

Consumer Financial Services

The Consumer Financial Protection Bureau (the "CFPB") regulates consumer financial products and services, as well as certain financial services providers, including Discover. The CFPB has rulemaking and interpretive authority under the Dodd-Frank Act and other federal consumer financial services laws, as well as broad supervisory, examination and enforcement authority over designated financial services providers. The CFPB’s regulatory authority includes the exercise of rulemaking, supervision and enforcement powers with respect to “unfair, deceptive or abusive acts or practices” and consumer access to fair, transparent and competitive financial products and services. The CFPB's policy priorities for 2017, as in recent years, include a focus on several financial products of the type we offer (e.g. credit cards and student loans).

The CFPB recently issued a final rule that will significantly limit the use of pre-dispute arbitration agreements and class action waivers. For more information, see Note 12: Litigation and Regulatory Matters to our condensed consolidated financial statements.

In addition, the CFPB publishes regular Complaint Reports and Supervisory Highlights about specific products, services and practices. The CFPB also maintains an online consumer complaint portal that shows the nature of each consumer's complaint and the financial services provider's responses, such as whether the requested relief was provided. The complaint portal allows consumers' narratives of their complaints to be included, although the Bureau does not verify the accuracy of the narratives. On July 29, 2016 the CFPB proposed to replace the dispute function on the portal, whereby the customer can dispute a company’s response to the complaint, with a survey that will allow the customer to provide feedback on the financial services provider's handling of the complaint. The CFPB seeks to implement this survey in 2017. In addition to conducting regular examinations of regulated financial services providers the CFPB regularly collects account-level information about certain financial products (e.g. credit cards) from Discover and other large financial services providers. The CFPB's analysis of complaint and account-level data, together with its supervisory examinations, can inform future decisions about its regulatory and examination priorities and influence consumers' decisions about doing business with financial services providers.

Credit Cards

Pursuant to the CARD Act, the CFPB is conducting its bi-annual review of the consumer credit card market. The review may result in additional guidance for credit card issuers, regulatory changes or legislative recommendations to

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Congress. The cost and availability of credit, credit disclosures and consumer experience with debt collectors continue to be an area of focus of the CFPB. The CFPB may propose debt collection regulations that apply to our lending business in 2017. The CFPB is developing a comprehensive debt collection rule that is expected to address practices of both third party debt collectors, which are currently regulated under the Fair Debt Collection Practices Act, and creditors like Discover.

Private Student Loans

There continues to be legislative and regulatory focus on the private student loan market, including by the CFPB, the Federal Deposit Insurance Corporation (the "FDIC") and some state legislatures and state attorneys general. This regulatory focus has resulted in an increase in supervisory examinations of Discover related to private student loans. On July 22, 2015, the CFPB and Discover entered into a consent order pertaining to certain student loan servicing practices of Discover Bank, The Student Loan Corporation and Discover Products, Inc. See Note 12: Litigation and Regulatory Matters to our condensed consolidated financial statements for more information.

Recent areas of regulatory attention include servicing, payments and collection practices, originations at for-profit schools, and other matters. Student loan servicing laws were recently enacted in California and the District of Columbia, and several other similar bills are pending that would impose new licensing, servicing, reporting and regulatory oversight requirements on non-bank student loan servicers. The enactment of new legislation or the adoption of new regulations or guidance may increase the complexity and expense of servicing student loans. Legislators and regulators may take additional actions that impact the student loan market in the future, which could cause us to change our private student loan products or servicing practices in ways that we may not currently anticipate.

Mortgage Lending

The mortgage industry continues to be an area of supervisory focus and the CFPB has stated that it will concentrate its examinations on a variety of mortgage-related topics including steering consumers to less favorable products, discrimination, abusive or unfair lending practices, predatory lending, origination disclosures, minimum mortgage underwriting standards, mortgage loan origination compensation and servicing practices. The CFPB has recently published several final rules impacting the mortgage industry. For example, on August 4, 2016, the CFPB issued final rules that expand the obligations of servicers and resolve some ambiguities. These changes will generally take effect in 2017. The CFPB has also recently proposed changes to the rules for integrated mortgage origination disclosures. The timing and substance of a final rule is uncertain at this point.

Payment Networks

The Dodd-Frank Act contains several provisions impacting the debit card market, including network participation requirements and interchange fee limitations. The changing debit card environment, including competitor actions related to merchant and acquirer pricing and transaction routing strategies, has adversely affected, and is expected to continue to adversely affect, our PULSE network's business practices, network transaction volume, revenue and prospects for future growth. We continue to closely monitor competitor pricing strategies in order to assess their impact on our business and on competition in the marketplace. The U.S. Department of Justice is examining some of these competitor pricing strategies. In addition, PULSE filed a lawsuit against Visa in late 2014 with respect to these competitive concerns, which will significantly impact expenses for the payment services segment. In addition, the Dodd-Frank Act's network participation requirements impact PULSE's ability to enter into exclusivity arrangements, which affects PULSE's current business practices and may materially adversely affect its network transaction volume and revenue.

European interchange fee regulation entered into force in June 2015. The regulation, among other things, caps interchange fees of "four-party" networks such as Visa and MasterCard. However, the regulation provides that “three-party” networks should be treated as “four-party” networks when they license third-party providers to issue cards and/or acquire merchants or when they issue cards with a co-brand partner or through an agent. This means the caps apply to elements of the financial arrangements agreed to between Diners Club and each of our stand-alone acquirers in Western Europe. The caps took effect in December 2015. The regulation excludes commercial card transactions from the scope of the caps. The regulation also contains a number of business rules, which we have, to the extent applicable, implemented in our Diners Club business.

There are additional initiatives in Europe that may have an impact on our Diners Club business, including revisions to the Payment Services Directive ("PSD2") and the new General Data Protection Regulation ("GDPR"). The PSD2 was published in the Official Journal of the EU in December 2015. Each European Union member state will transpose the PSD2

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into its national law, and in January 2018 the PSD2 will enter into force. Among other terms, the PSD2 includes provisions that once transposed into local law will regulate surcharging and network access requirements, which may result in differential surcharging of Diners Club cards and may impact Diners Club licensing arrangements in Europe. The European Parliament's Civil Liberties, Justice and Home Affairs Committee approved the final draft of the GDPR in December 2015. The final GDPR was published in the Official Journal of the European Union on May 4, 2016. Organizations have two years to prepare before the legislation comes into force on May 25, 2018. We are preparing for implementation of the GDPR.

The Chinese State Council previously announced that foreign payments companies would be able to participate in the Chinese domestic market and be eligible to apply for a license to operate a Bank Card Clearing Institution ("BCCI") in China. In June 2016 the People's Bank of China ("PBOC"), in conjunction with the China Banking Regulatory Commission, promulgated the Administrative Measures on BCCIs. On June 30, 2017, the PBOC published the implementation guidelines. We are analyzing any potential impact on our business and preparing for implementation.

Capital, Liquidity and Funding

Capital

Discover Financial Services and Discover Bank are subject to regulatory capital requirements that became effective January 1, 2015 under final rules issued by the Board of Governors of the Federal Reserve System (the "Federal Reserve")and the FDIC to implement the provisions under the Basel Committee's December 2010 framework (referred to as "Basel III"). The final capital rules ("Basel III rules") require minimum risk-based capital and leverage ratios and define what constitutes capital for purposes of calculating those ratios. In addition, the Basel III rules establish a capital conservation buffer above the regulatory minimum capital requirements, which must consist entirely of Common Equity Tier 1 ("CET1") capital and result in higher required minimum ratios by up to 2.5%. The new capital conservation buffer requirement became effective on January 1, 2016; however, the buffer threshold amounts are subject to a gradual phase-in period. In 2016, the highest capital conservation buffer threshold was 0.625%, which has risen to 1.25% for the 2017 calendar year. The full 2.5% buffer requirement will not be fully phased-in until January 2019. A banking organization is subject to limitations on paying dividends, engaging in share repurchases and paying discretionary bonuses if its capital level falls below any of the minimum capital requirements, taking into account the applicable capital conservation buffer thresholds. Based on our current capital composition and levels and business plans, we are and expect to continue to be in compliance with the requirements for the foreseeable future. For additional information, see "— Liquidity and Capital Resources — Capital."

The Basel Committee has previously proposed revisions to its standardized approach to measuring credit risk for purposes of calculating regulatory capital requirements. The proposed revisions include a provision that would, for the first time, require banking organizations to include a percentage of "unconditionally cancellable commitments" in risk-weighted asset calculations. This change could require credit card issuers, such as Discover, to substantially increase the amount of capital they hold against unused credit card lines. If the Basel Committee were to adopt the revisions as proposed, they would become applicable to Discover only if implemented within the United States by the domestic federal bank regulatory agencies, and made applicable to all "Standardized Approach" banks. Those agencies have publicly acknowledged the Basel Committee's proposals, indicating that the revisions "would apply primarily to large, internationally active banking organizations."

Liquidity

We are subject to the Federal Reserve's final rule implementing certain enhanced prudential standards under the Dodd-Frank Act for large U.S. bank holding companies, including enhanced liquidity and risk management requirements, which became effective January 1, 2015. The final rule prescribes a broad range of qualitative liquidity risk management practices.

Additionally, we are subject to the U.S. liquidity coverage ratio rule issued by federal banking regulators in 2014, which became effective on January 1, 2016. This quantitative requirement is designed to promote the short-term resilience of the liquidity risk profile of large and internationally active banking organizations in the United States. The rule requires covered banks to maintain an amount of high-quality liquid assets sufficient to cover projected net cash outflows during a prospective 30-day calendar period under an acute, hypothetical liquidity stress scenario. Given our current asset size, we are subject to a modified liquidity coverage ratio requirement which requires a lower

level of high-quality liquid assets to meet the minimum ratio requirement due to adjustments to the net cash outflow amount. Under the rule's transition period, we are required to maintain a liquidity ratio of 100% in 2017. As of June 30, 2017, our liquidity coverage ratio was in excess of the applicable regulatory requirement. On December 19, 2016, the Federal Reserve issued a final rule that will require banking institutions subject to the liquidity coverage ratio rule to publish quarterly public disclosures regarding the company’s

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liquidity risk profile and components of its liquidity coverage ratio calculation. Discover will be required to publish its first disclosure under the rule beginning the fourth quarter of 2018.

In April 2016, the federal banking agencies issued a notice of proposed rulemaking to implement, within the United States, the long-term liquidity standards previously issued at the international level by the Basel Committee on Banking Supervision. The proposed rule would impose a new quantitative liquidity requirement called the Net Stable Funding Ratio (“NSFR”) to ensure that covered banking organizations maintain stable funding to meet their funding needs over a one year time horizon. The NSFR is intended to complement the shorter-term liquidity coverage ratio requirement. Under the proposed rule, we would be subject to a less stringent “modified” NSFR requirement. If adopted as a final rule, the minimum NSFR requirements would take effect on January 1, 2018.

Segments

We manage our business activities in two segments: Direct Banking and Payment Services. In compiling the segment results that follow, our Direct Banking segment bears all corporate overhead costs that are not specifically associated with a particular segment and all costs associated with Discover Network marketing, servicing and infrastructure, with the exception of an allocation of direct and incremental costs driven by our Payment Services segment.

Direct Banking

Our Direct Banking segment includes Discover-branded credit cards issued to individuals on the Discover Network and other consumer products and services, including private student loans, personal loans, home equity loans, and other consumer lending and deposit products. The majority of Direct Banking revenues relate to interest income earned on the segment's loan products. Additionally, our credit card products generate substantially all of our revenues related to discount and interchange, protection products and loan fee income.

Payment Services

Our Payment Services segment includes PULSE, an automated teller machine, debit and electronic funds transfer network; Diners Club, a global payments network; and our Network Partners business, which provides payment transaction processing and settlement services on the Discover Network. The majority of Payment Services revenues relate to transaction processing revenue from PULSE and royalty and licensee revenue (included in other income) from Diners Club.

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The following table presents segment data (dollars in millions):

	For the Three Months Ended June 30,		For the Six Months Ended June 30,	
	2017	2016	2017	2016
Direct Banking				
Interest income				
Credit card	$1,916	$1,734	$3,792	$3,467
Private student loans	127	110	251	217
PCI student loans	41	47	82	96
Personal loans	207	171	405	338
Other	47	28	86	56
Total interest income	2,338	2,090	4,616	4,174
Interest expense	400	339	786	673
Net interest income	1,938	1,751	3,830	3,501
Provision for loan losses	639	411	1,233	834
Other income	408	396	783	802
Other expense	876	868	1,725	1,719
Income before income tax expense	831	868	1,655	1,750
Payment Services				
Provision for loan losses	1	1	(7)	2
Other income	73	69	145	137
Other expense	36	38	72	73
Income before income tax expense	36	30	80	62
Total income before income tax expense	$867	$898	$1,735	$1,812

The following table presents information on transaction volume (in millions):

	For the Three Months Ended June 30,		For the Six Months Ended June 30,	
	2017	2016	2017	2016
Network Transaction Volume				
PULSE Network	$38,848	$33,856	$74,914	$68,536
Network Partners	3,461	3,713	7,122	7,285
Diners Club[(1)]	7,800	7,198	15,182	13,936
Total Payment Services	50,109	44,767	97,218	89,757
Discover Network—Proprietary[(2)]	33,342	31,780	63,201	60,356
Total Volume	$83,451	$76,547	$160,419	$150,113
Transactions Processed on Networks				
Discover Network	551	538	1,054	1,024
PULSE Network	961	853	1,831	1,694
Total	1,512	1,391	2,885	2,718
Credit Card Volume				
Discover Card Volume[(3)]	$35,297	$33,409	$67,703	$63,413
Discover Card Sales Volume[(4)]	$32,172	$30,702	$61,306	$58,254

(1) Diners Club volume is derived from data provided by licensees for Diners Club branded cards issued outside North America and is subject to subsequent revision or amendment.

(2) Represents gross proprietary sales volume on the Discover Network.
(3) Represents Discover card activity related to net sales, balance transfers, cash advances and other activity.
(4) Represents Discover card activity related to net sales.

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Direct Banking

Our Direct Banking segment reported pretax income of $831 million and $1.7 billion for the three and six months ended June 30, 2017, respectively, as compared to pretax income of $868 million and $1.8 billion for the three and six months ended June 30, 2016, respectively.

Loan receivables increased to $78.0 billion at June 30, 2017 as compared to $77.3 billion at December 31, 2016 primarily due to growth in the credit card loans portfolio. Discover card sales volume was $32.2 billion and $61.3 billion for the three and six months ended June 30, 2017, respectively, which was an increase of 4.8% and 5.2%, respectively, as compared to the same periods in 2016. This volume growth was primarily driven by an increase in consumer spending.

Net interest margin increased for the three and six months ended June 30, 2017 as compared to the same periods in 2016 primarily driven by higher yields on credit card loans, partially offset by higher funding costs. The increase in yields on credit card loans was primarily due to the prime rate increase and a higher portion of revolving card receivables, partially offset by higher promotional balances in the card portfolio and higher interest charge-offs. Interest income increased during the three and six months ended June 30, 2017 as compared to the same periods in 2016 due to loan growth and yield expansion. Interest expense increased during the three and six months ended June 30, 2017 as compared to the same periods in 2016 primarily due to higher market rates, a change in funding mix and a larger funding base.

At June 30, 2017 and December 31, 2016, our delinquency rate for credit card loans over 30 days past due was 2.00% and 2.04%, respectively. For the three and six months ended June 30, 2017, our net charge-off rate on credit cards increased to 2.94% and 2.89%, respectively, as compared to 2.39% and 2.37% for the same periods in 2016. For the three and six months ended June 30, 2017, the provision for loan losses increased as compared to the same periods in 2016 primarily due to the higher levels of net charge-offs combined with a larger build of allowance for loan losses. For a detailed discussion on provision for loan losses, see "— Loan Quality — Provision and Allowance for Loan Losses."

Total other income increased in the three months ended June 30, 2017 and decreased in the six months ended June 30, 2017 as compared to the same periods in 2016. During the three and six months ended June 30, 2017, the change was due primarily to an increase in discount and interchange revenue driven by higher sales volume, which was more than offset by higher promotional rewards in the first quarter of 2017. In addition, the increase in loan fee income was primarily due to an increase in late fees.

Total other expense increased in the three and six months ended June 30, 2017 as compared to the same periods in 2016. During the three and six months ended June 30, 2017, the increase was primarily driven by an increase in employee compensation and benefits offset by a decrease in information processing and communications. The increase in employee compensation and benefits was primarily driven by the impact of added headcount for regulatory and compliance needs and higher average salaries. The decrease in information processing and communications was primarily the result of infrastructure efficiencies. For the six months ended June 30, 2017, the decrease in professional fees was driven primarily by the completion of a look back project related to anti-money laundering remediation in 2016, offset by higher spend in collection efforts and investments in technology and infrastructure in 2017.

Payment Services

Our Payment Services segment reported pretax income of $36 million and $80 million for the three and six months ended June 30, 2017, respectively, as compared to pretax income of $30 million and $62 million for the same periods in 2016. The increase in segment pretax income was primarily driven by an increase in transaction processing revenue due to higher point-of-sale transactions.

Downturns in the global economy or negative impacts in foreign currency may adversely affect our financial condition or results of operations in our Payment Services segment. We continue to work with our Diners Club licensees with regard to their ability to maintain financing sufficient to support business operations. We may continue to provide additional support in the future, including loans, facilitating transfer of ownership, or acquiring assets or licensees, which may cause us to incur losses. The licensees that we currently consider to be of concern accounted for approximately 4% of Diners Club revenues during the three and six months ended June 30, 2017.

Critical Accounting Estimates

In preparing our condensed consolidated financial statements in conformity with accounting principles generally accepted in the United States ("GAAP"), management must make judgments and use estimates and assumptions about the

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effects of matters that are uncertain. For estimates that involve a high degree of judgment and subjectivity, it is possible that different estimates could reasonably be derived for the same period. For estimates that are particularly sensitive to changes in economic or market conditions, significant changes to the estimated amount from period to period are also possible. Management believes the current assumptions and other considerations used to estimate amounts reflected in our condensed consolidated financial statements are appropriate. However, if actual experience differs from the assumptions and other considerations used in estimating amounts in our condensed consolidated financial statements, the resulting changes could have a material effect on our consolidated results of operations and, in certain cases, could have a material effect on our consolidated financial condition. Management has identified the estimates related to our allowance for loan losses, the evaluation of goodwill and other non-amortizable intangible assets for potential impairment, the accrual of income taxes and estimates of future cash flows associated with PCI loans as critical accounting estimates. These critical accounting estimates are discussed in greater detail in our annual report on Form 10-K for the year ended December 31, 2016. That discussion can be found within "Management's Discussion and Analysis of Financial Condition and Results of Operations" under the heading "— Critical Accounting Estimates." There have not been any material changes in the methods used to formulate these critical accounting estimates from those discussed in our annual report on Form 10-K for the year ended December 31, 2016.

Earnings Summary

The following table outlines changes in our condensed consolidated statements of income (dollars in millions):

	For the Three Months Ended June 30,		2017 vs. 2016 Increase (Decrease)		For the Six Months Ended June 30,		2017 vs. 2016 Increase (Decrease)	
	2017	2016	$	%	2017	2016	$	%
Interest income	$2,338	$2,090	$248	12 %	$4,616	$4,174	$442	11 %
Interest expense	400	339	61	18 %	786	673	113	17 %
Net interest income	1,938	1,751	187	11 %	3,830	3,501	329	9 %
Provision for loan losses	640	412	228	55 %	1,226	836	390	47 %
Net interest income after provision for loan losses	1,298	1,339	(41)	(3)%	2,604	2,665	(61)	(2)%
Other income	481	465	16	3 %	928	939	(11)	(1)%
Other expense	912	906	6	1 %	1,797	1,792	5	— %
Income before income tax expense	867	898	(31)	(3)%	1,735	1,812	(77)	(4)%
Income tax expense	321	282	39	14 %	625	621	4	1 %
Net income	$546	$616	$(70)	(11)%	$1,110	$1,191	$(81)	(7)%

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Net Interest Income

The table that follows this section has been provided to supplement the discussion below and provide further analysis of net interest income and net interest margin. Net interest income represents the difference between interest income earned on our interest-earning assets and the interest expense incurred to finance those assets. We analyze net interest income in total by calculating net interest margin (net interest income as a percentage of average total loan receivables) and net yield on interest-bearing assets (net interest income as a percentage of average total interest-earning assets). We also separately consider the impact of the level of loan receivables and the related interest yield and the impact of the cost of funds related to each of our funding sources, along with the income generated by our liquidity portfolio, on net interest income.

Our interest-earning assets consist of: (i) cash and cash equivalents primarily related to amounts on deposit with the Federal Reserve Bank of Philadelphia, (ii) restricted cash, (iii) other short-term investments, (iv) investment securities and (v) loan receivables. Our interest-bearing liabilities consist primarily of deposits, both direct-to-consumer and brokered, and long-term borrowings, including amounts owed to securitization investors. Net interest income is influenced by the following:

- The level and composition of loan receivables, including the proportion of credit card loans to other loans, as well as the proportion of loan receivables bearing interest at promotional rates as compared to standard rates;
- The credit performance of our loans, particularly with regard to charge-offs of finance charges, which reduce interest income;
- The terms of long-term borrowings and certificates of deposit upon initial offering, including maturity and interest rate;
- The level and composition of other interest-bearing assets and liabilities, including our liquidity portfolio;
- Changes in the interest rate environment, including the levels of interest rates and the relationships among interest rate indices, such as the prime rate, the Federal Funds rate and the London Interbank Offered Rate;
- The effectiveness of interest rate swaps in our interest rate risk management program; and
- The difference between the carrying amount and future cash flows expected to be collected on PCI loans.

Net interest margin increased for the three and six months ended June 30, 2017 as compared to the same periods in 2016 primarily driven by higher yields on credit card loans, partially offset by higher funding costs. The increase in yields on credit card loans was primarily due to the prime rate increase and a higher portion of revolving card receivables, partially offset by higher promotional balances in the card portfolio and higher interest charge-offs.

Interest income increased during the three and six months ended June 30, 2017 as compared to the same periods in 2016 due to loan growth and yield expansion. Interest expense increased during the three and six months ended June 30, 2017 as compared to the same periods in 2016 primarily due to higher market rates, a change in funding mix and a larger funding base.

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Average Balance Sheet Analysis
(dollars in millions)

	For the Three Months Ended June 30,					
	2017			2016		
	Average Balance	Rate	Interest	Average Balance	Rate	Interest
Assets						
Interest-earning assets						
Cash and cash equivalents	$12,921	1.05 %	$35	$10,750	0.50 %	$13
Restricted cash	559	0.89 %	1	263	0.41 %	—
Other short-term investments	—	— %	—	852	0.86 %	2
Investment securities	1,695	1.58 %	7	2,697	1.49 %	10
Loan receivables[1]						
Credit card[2]	60,700	12.66 %	1,916	56,124	12.42 %	1,734
Personal loans	6,820	12.22 %	208	5,608	12.25 %	171
Private student loans	6,634	7.71 %	127	5,915	7.41 %	109
PCI student loans	2,386	6.72 %	40	2,901	6.55 %	47
Other	314	5.59 %	4	262	5.04 %	4
Total loan receivables	76,854	11.98 %	2,295	70,810	11.72 %	2,065
Total interest-earning assets	92,029	10.19 %	2,338	85,372	9.84 %	2,090
Allowance for loan losses	(2,262)			(1,918)		
Other assets	4,147			4,502		
Total assets	$93,914			$87,956		
Liabilities and Stockholders’ Equity						
Interest-bearing liabilities						
Interest-bearing deposits						
Time deposits[3]	$26,054	1.90 %	123	$24,682	1.74 %	107
Money market deposits[4]	6,808	1.25 %	21	6,903	1.06 %	18
Other interest-bearing savings deposits	19,694	1.11 %	55	16,370	1.01 %	41
Total interest-bearing deposits[5]	52,556	1.52 %	199	47,955	1.39 %	166
Borrowings						
Short-term borrowings	2	1.06 %	—	2	0.64 %	—
Securitized borrowings[3][4]	16,141	2.31 %	93	16,635	2.06 %	85
Other long-term borrowings[3]	9,979	4.36 %	108	7,984	4.40 %	88
Total borrowings	26,122	3.09 %	201	24,621	2.82 %	173
Total interest-bearing liabilities	78,678	2.04 %	400	72,576	1.88 %	339
Other liabilities and stockholders’ equity	15,236			15,380		
Total liabilities and stockholders’ equity	$93,914			$87,956		
Net interest income			$1,938			$1,751
Net interest margin[6]		10.11 %			9.94 %	
Net yield on interest-bearing assets[7]		8.44 %			8.25 %	
Interest rate spread[8]		8.15 %			7.96 %	

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Average Balance Sheet Analysis
(dollars in millions)

	For the Six Months Ended June 30,					
	2017			2016		
	Average Balance	Rate	Interest	Average Balance[1]	Rate[1]	Interest
Assets						
Interest-earning assets						
Cash and cash equivalents	$13,304	0.92 %	$61	$10,602	0.50 %	$26
Restricted cash	689	0.78 %	3	532	0.40 %	1
Other short-term investments	—	— %	—	426	0.86 %	2
Investment securities	1,713	1.60 %	14	2,848	1.48 %	21
Loan receivables[2]						
Credit card[3]	60,413	12.66 %	3,792	56,124	12.42 %	3,467
Personal loans	6,702	12.20 %	405	5,555	12.23 %	338
Private student loans	6,656	7.62 %	251	5,918	7.36 %	216
PCI student loans	2,452	6.69 %	81	2,973	6.50 %	96
Other	298	5.50 %	9	253	5.11 %	7
Total loan receivables	76,521	11.96 %	4,538	70,823	11.71 %	4,124
Total interest-earning assets	92,227	10.09 %	4,616	85,231	9.85 %	4,174
Allowance for loan losses	(2,214)			(1,892)		
Other assets	4,157			4,478		
Total assets	$94,170			$87,817		
Liabilities and Stockholders’ Equity						
Interest-bearing liabilities						
Interest-bearing deposits						
Time deposits[4]	$26,335	1.88 %	245	$25,066	1.71 %	213
Money market deposits[5]	6,859	1.20 %	41	6,944	1.05 %	36
Other interest-bearing savings deposits	19,363	1.09 %	104	15,723	1.01 %	79
Total interest-bearing deposits[6]	52,557	1.50 %	390	47,733	1.38 %	328
Borrowings						
Short-term borrowings	2	0.89 %	—	2	0.64 %	—
Securitized borrowings[4][5]	16,548	2.24 %	184	16,792	2.05 %	171
Other long-term borrowings[4]	9,791	4.37 %	212	7,960	4.39 %	174
Total borrowings	26,341	3.03 %	396	24,754	2.80 %	345
Total interest-bearing liabilities	78,898	2.01 %	786	72,487	1.87 %	673
Other liabilities and stockholders’ equity	15,272			15,330		
Total liabilities and stockholders’ equity	$94,170			$87,817		
Net interest income			$3,830			$3,501
Net interest margin[7]		10.09 %			9.94 %	
Net yield on interest-bearing assets[8]		8.37 %			8.26 %	
Interest rate spread[9]		8.08 %			7.98 %	

(1) Average balances of loan receivables include non-accruing loans, which are included in the yield calculations. If the non-accruing loan balances were excluded, there would not be a material impact on the amounts reported above.
(2) Interest income on credit card loans includes $54 million and $48 million of amortization of balance transfer fees for the three months ended June 30, 2017 and 2016, respectively. Interest income on credit card loans includes $106 million and $93 million of amortization of balance transfer fees for the six months ended June 30, 2017 and

2016, respectively.

(3) Includes the impact of interest rate swap agreements used to change a portion of fixed-rate funding to floating-rate funding.

(4) Includes the impact of interest rate swap agreements used to change a portion of floating-rate funding to fixed-rate funding.

(5) Includes the impact of FDIC insurance premiums and Large Institution Surcharge.

(6) Net interest margin represents net interest income as a percentage of average total loan receivables.

(7) Net yield on interest-bearing assets represents net interest income as a percentage of average total interest-earning assets.

(8) Interest rate spread represents the difference between the rate on total interest-earning assets and the rate on total interest-bearing liabilities.

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Loan Quality

Loan receivables consist of the following (dollars in millions):

	June 30, 2017	December 31, 2016
Loan receivables		
Credit card loans	$61,797	$ 61,522
Other loans		
Personal loans	6,955	6,481
Private student loans	6,594	6,393
Other	329	274
Total other loans	13,878	13,148
PCI loans[1]	2,322	2,584
Total loan receivables	77,997	77,254
Allowance for loan losses	(2,384)	(2,167)
Net loan receivables	$75,613	$ 75,087

(1) Represents PCI private student loans. See Note 3: Loan Receivables to our condensed consolidated financial statements for more information regarding PCI loans.

Provision and Allowance for Loan Losses

Provision for loan losses is the expense related to maintaining the allowance for loan losses at an appropriate level to absorb the estimated probable losses in the loan portfolio at each period end date. While establishing the estimate for probable losses requires management judgment, the factors that influence the provision for loan losses include:

- The impact of current and predictive general economic conditions on the consumer, including unemployment levels, bankruptcy trends and interest rate movements;
- Changes in consumer spending and payment behaviors;
- Changes in our loan portfolio, including the overall mix of accounts, products and loan balances within the portfolio and maturation of the loan portfolio;
- The level and direction of historical and anticipated loan delinquencies and charge-offs;
- The credit quality of the loan portfolio, which reflects, among other factors, our credit granting practices and effectiveness of collection efforts; and
- Regulatory changes or new regulatory guidance.

In determining the allowance for loan losses, we estimate probable losses separately for segments of the loan portfolio that have similar risk characteristics. We use a migration analysis to estimate the likelihood that a loan will progress through the various stages of delinquency. We use other analyses to estimate losses incurred from non-delinquent accounts, which adds to the identification of loss emergence. We use these analyses together as a basis for determining our allowance for loan losses.

The provision for loan losses is the amount of expense realized after considering the level of net charge-offs in the period and the required amount of allowance for loan losses at the balance sheet date. For the three and six months ended June 30, 2017, the provision for loan losses increased by $228 million, or 55%, and $390 million, or 47%, respectively, as compared to the same periods in 2016. The increase was primarily due to higher levels of net charge-offs combined with a larger reserve build for the three and six months ended June 30, 2017 as compared to the same periods in 2016.

The allowance for loan losses was $2.4 billion at June 30, 2017, which reflects a $217 million reserve build over the amount of the allowance for loan losses at December 31, 2016. The reserve build was due to seasoning of loan growth and increasing consumer leverage.

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The following tables provide changes in our allowance for loan losses (dollars in millions):

	For the Three Months Ended June 30, 2017				
	Credit Card	Personal Loans	Student Loans(1)	Other	Total
Balance at beginning of period	$1,892	$ 207	$ 156	$ 9	$2,264
Additions					
Provision for loan losses	533	82	23	2	640
Deductions					
Charge-offs	(561)	(61)	(22)	(1)	(645)
Recoveries	116	7	2	—	125
Net charge-offs	(445)	(54)	(20)	(1)	(520)
Balance at end of period	$1,980	$ 235	$ 159	$ 10	$2,384

	For the Three Months Ended June 30, 2016				
	Credit Card	Personal Loans	Student Loans(1)	Other	Total
Balance at beginning of period	$1,590	$ 165	$ 148	$ 18	$1,921
Additions					
Provision for loan losses	347	44	20	1	412
Deductions					
Charge-offs	(448)	(38)	(19)	—	(505)
Recoveries	114	5	2	—	121
Net charge-offs	(334)	(33)	(17)	—	(384)
Balance at end of period	$1,603	$ 176	$ 151	$ 19	$1,949

	For the Six Months Ended June 30, 2017				
	Credit Card	Personal Loans	Student Loans(1)	Other	Total
Balance at beginning of period	$1,790	$ 200	$ 158	$ 19	$2,167
Additions					
Provision for loan losses	1,057	140	35	(6)	1,226
Deductions					
Charge-offs	(1,096)	(118)	(39)	(3)	(1,256)
Recoveries	229	13	5	—	247
Net charge-offs	(867)	(105)	(34)	(3)	(1,009)
Balance at end of period	$1,980	$ 235	$ 159	$ 10	$2,384

	For the Six Months Ended June 30, 2016				
	Credit Card	Personal Loans	Student Loans(1)	Other	Total
Balance at beginning of period	$1,554	$ 155	$ 143	$ 17	$1,869
Additions					
Provision for loan losses	709	88	37	2	836
Deductions					
Charge-offs	(887)	(77)	(34)	—	(998)
Recoveries	227	10	5	—	242
Net charge-offs	(660)	(67)	(29)	—	(756)
Balance at end of period	$1,603	$ 176	$ 151	$ 19	$1,949

(1) Includes both PCI and non-PCI private student loans.

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Net Charge-offs

Our net charge-offs include the principal amount of losses charged off less principal recoveries and exclude charged-off and recovered interest and fees and fraud losses. Charged-off and recovered interest and fees are recorded in interest income and loan fee income, respectively, which is effectively a reclassification of the provision for loan losses, while fraud losses are recorded in other expense. Credit card loan receivables are charged off at the end of the month during which an account becomes 180 days contractually past due. Personal loans and private student loans, which are closed-end consumer loan receivables, are generally charged off at the end of the month during which an account becomes 120 days contractually past due. Generally, customer bankruptcies and probate accounts are charged off at the end of the month 60 days following the receipt of notification of the bankruptcy or death but not later than the 180-day or 120-day contractual time frame.

The following table presents amounts and rates of net charge-offs of key loan products (dollars in millions):

	For the Three Months Ended June 30,				For the Six Months Ended June 30,			
	2017		2016		2017		2016	
	$	%	$	%	$	%	$	%
Credit card loans	$445	2.94%	$334	2.39%	$867	2.89%	$660	2.37%
Personal loans	$54	3.18%	$33	2.38%	$105	3.17%	$67	2.41%
Private student loans (excluding PCI[1])	$20	1.15%	$17	1.10%	$34	0.99%	$29	0.98%

(1) Charge-offs for PCI loans did not result in a charge to earnings during any of the periods presented and are therefore excluded from the calculation. See Note 3: Loan Receivables to our condensed consolidated financial statements for more information regarding the accounting for charge-offs on PCI loans.

The net charge-off rate on our credit card loans increased by 55 and 52 basis points for the three and six months ended June 30, 2017, respectively, when compared to the same periods in 2016. The net charge-off rate on our personal loans increased by 80 and 76 basis points for the three and six months ended June 30, 2017, respectively, when compared to the same periods in 2016. The increase for both credit card loans and personal loans was driven by seasoning of loan growth and increasing consumer leverage. The net charge-off rate on our private student loans excluding PCI remained relatively flat for the three and six months ended June 30, 2017 when compared to the same periods in 2016.

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Delinquencies

Delinquencies are an indicator of credit quality at a point in time. A loan balance is considered delinquent when contractual payments on the loan become 30 days past due.

The following table presents the amounts and rates of key loan products that are 30 and 90 days or more delinquent, loan receivables that are not accruing interest, regardless of delinquency and restructured loans (dollars in millions):

	June 30, 2017		December 31, 2016	
	$	%	$	%
Loans 30 or more days delinquent				
Credit card loans	$1,237	2.00%	$1,252	2.04%
Personal loans	$78	1.14%	$74	1.12%
Private student loans (excluding PCI loans[1])	$140	2.12%	$141	2.22%
Loans 90 or more days delinquent				
Credit card loans	$603	0.98%	$597	0.97%
Personal loans	$21	0.30%	$19	0.29%
Private student loans (excluding PCI loans[1])	$42	0.63%	$35	0.55%
Loans not accruing interest	$226	0.30%	$216	0.29%
Restructured loans				
Credit card loans[2]	$1,148	1.86%	$1,085	1.76%
Personal loans[3]	$92	1.32%	$81	1.25%
Private student loans (excluding PCI loans[1])[4]	$115	1.74%	$86	1.35%

(1) Excludes PCI loans which are accounted for on a pooled basis. Since a pool is accounted for as a single asset with a single composite interest rate and aggregate expectation of cash flows, the past-due status of a pool, or that of the individual loans within a pool, is not meaningful. Because we are recognizing interest income on a pool of loans, it is all considered to be performing.

(2) Restructured credit card loans include $63 million and $60 million at June 30, 2017 and December 31, 2016, respectively, that are also included in loans over 90 days delinquent or more.

(3) Restructured personal loans include $3 million and $2 million at June 30, 2017 and December 31, 2016, respectively, that are also included in loans over 90 days delinquent or more.

(4) Restructured private student loans include $5 million and $3 million at June 30, 2017 and December 31, 2016, that are also included in loans over 90 days delinquent or more.

The 30-day delinquency rate for credit card loans at June 30, 2017 decreased as compared to December 31, 2016 primarily due to seasonality while the 90-day delinquency rate remained relatively flat at June 30, 2017 as compared to December 31, 2016. Personal loans 30-day and 90-day delinquency rates at June 30, 2017 remained relatively stable as compared to December 31, 2016. The 30-day delinquency rate for private student loans at June 30, 2017 decreased while the 90-day delinquency rate increased compared to December 31, 2016 as a result of seasonality of the portfolio.

The restructured credit card and personal loan balances at June 30, 2017 increased as compared to December 31, 2016 due to continued loan growth and seasoning. At June 30, 2017, the restructured private student loan balance increased as compared to December 31, 2016 as a result of greater utilization of programs available as more loans have entered into repayment.

Modified and Restructured Loans

We have loan modification programs that provide for temporary or permanent hardship relief for our credit card loans to borrowers experiencing financial difficulties. The temporary hardship program primarily consists of a reduced

minimum payment and an interest rate reduction, both lasting for a period no longer than 12 months. The permanent modification program involves changing the structure of the loan to a fixed payment loan with a maturity no longer than 60 months and reducing the interest rate on the loan. The permanent modification program does not normally provide for the forgiveness of unpaid principal, but may allow for the reversal of certain unpaid interest or fee assessments. We also make permanent loan modifications for customers who request financial assistance through external sources, such as a consumer credit counseling agency program. These loans continue to be subject to the original minimum payment terms and do not normally include waiver of unpaid principal, interest or fees. Credit card loans included in temporary and permanent programs are accounted for as troubled debt restructurings. For additional information regarding the accounting treatment for these loans as well as

amounts recorded in the financial statements related to these loans, see Note 3: Loan Receivables to our condensed consolidated financial statements.

For personal loan customers, in certain situations we offer various payment programs, including temporary and permanent programs. The temporary programs normally consist of a reduction of the minimum payment for a period of no longer than 12 months with the option of a final balloon payment required at the end of the loan term or an extension of the maturity date with the total term not exceeding nine years. Further, in certain circumstances, the interest rate on the loan is reduced. The permanent programs involve changing the terms of the loan in order to pay off the outstanding balance over a longer term and also in certain circumstances reducing the interest rate on the loan. Similar to the temporary programs, the total term may not exceed nine years. We also allow permanent loan modifications for customers who request financial assistance through external sources, similar to our credit card customers discussed above. Payments are modified based on the new terms agreed upon with the credit counseling agency. Personal loans included in temporary and permanent programs are accounted for as troubled debt restructurings.

At June 30, 2017, there was $5.7 billion of private student loans in repayment, which includes both PCI and non-PCI loans to students who are not in deferment. To assist student loan borrowers who are experiencing temporary financial difficulties but are willing to resume making payments, we may offer hardship forbearance or programs that include payment deferral, temporary payment reduction, temporary interest rate reduction or extended terms. A modified loan typically meets the definition of a troubled debt restructuring based on the cumulative length of the concession period and an evaluation of the credit quality of the borrower based on FICO scores. Prior to the third quarter of 2016, only a second forbearance when the borrower was 30 days or greater delinquent was considered a troubled debt restructuring. As a result, the student loan balances being accounted for as troubled debt restructuring increased, although it did not lead to significant changes in the balance of overall allowance for loan losses.

Borrower performance after using payment programs or forbearance is monitored and we believe the programs help to prevent defaults and are useful in assisting customers experiencing financial difficulties. We plan to continue to use payment programs and forbearance and, as a result, we expect to have additional loans classified as troubled debt restructurings in the future.

Other Income

The following table presents the components of other income (dollars in millions):

	For the Three Months Ended June 30,		2017 vs. 2016 Increase (Decrease)		For the Six Months Ended June 30,		2017 vs. 2016 (Decrease) Increase	
	2017	2016	$	%	2017	2016	$	%
Discount and interchange revenue[1]	$278	$265	$13	5 %	$511	$538	$(27)	(5)%
Protection products revenue	56	59	(3)	(5)%	114	120	(6)	(5)%
Loan fee income	83	79	4	5 %	172	159	13	8 %
Transaction processing revenue	42	39	3	8 %	81	75	6	8 %
Other income	22	23	(1)	(4)%	50	47	3	6 %
Total other income	$481	$465	$16	3 %	$928	$939	$(11)	(1)%

(1) Net of rewards, including Cashback Bonus rewards, of $388 million and $371 million for the three months ended June 30, 2017 and 2016, respectively, and of $751 million and $663 million for the six months ended June 30, 2017 and 2016, respectively.

Total other income increased in the three months ended June 30, 2017 by $16 million and decreased in the six months ended June 30, 2017 by $11 million, respectively, as compared to the same periods in 2016. During the three and six months ended June 30, 2017, the change was due primarily to an increase in discount and interchange revenue driven by higher sales volume, which was more than offset by higher promotional rewards in the first quarter of 2017. In addition, the increase in loan fee income was primarily due to an increase in late fees.

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Other Expense

The following table represents the components of other expense (dollars in millions):

	For the Three Months Ended June 30,		2017 vs. 2016 Increase (Decrease)		For the Six Months Ended June 30,		2017 vs. 2016 Increase (Decrease)	
	2017	2016	$	%	2017	2016	$	%
Employee compensation and benefits	$367	$340	$27	8 %	$730	$685	$45	7 %
Marketing and business development	192	198	(6)	(3)%	360	360	—	— %
Information processing and communications	77	89	(12)	(13)%	157	177	(20)	(11)%
Professional fees	156	150	6	4 %	303	310	(7)	(2)%
Premises and equipment	23	23	—	— %	48	47	1	2 %
Other expense	97	106	(9)	(8)%	199	213	(14)	(7)%
Total other expense	$912	$906	$6	1 %	$1,797	$1,792	$5	— %

Total other expense increased in the three and six months ended June 30, 2017 by $6 million and $5 million, respectively, as compared to the same periods in 2016. During the three and six months ended June 30, 2017, the increase was primarily driven by an increase in employee compensation and benefits offset by a decrease in information processing and communications. The increase in employee compensation and benefits was primarily driven by the impact of added headcount for regulatory and compliance needs and higher average salaries. The decrease in information processing and communications was primarily the result of infrastructure efficiencies. For the six months ended June 30, 2017, the decrease in professional fees was driven primarily by the completion of a look back project related to anti-money laundering remediation in 2016, offset by higher spend in collection efforts and investments in technology and infrastructure in 2017.

Income Tax Expense

The following table presents the calculation of the effective income tax rate (dollars in millions, except effective income tax rate):

	For the Three Months Ended June 30,		For the Six Months Ended June 30,	
	2017	2016	2017	2016
Income before income tax expense	$867	$898	$1,735	$1,812
Income tax expense	$321	$282	$625	$621
Effective income tax rate	37.1 %	31.4 %	36.0 %	34.3 %

Income tax expense increased $39 million and $4 million for the three and six months ended June 30, 2017, respectively, compared to the same periods in 2016. The effective tax rates for the three and six months ended June 30, 2017 of 37.1% and 36.0%, respectively, increased from 31.4% and 34.3% for the same periods in 2016. The increase in rates is primarily due to the settlement with the United States Congress Joint Committee on Taxation that occurred in the second quarter of 2016.

Liquidity and Capital Resources

Funding and Liquidity

We seek to maintain stable, diversified and cost-effective funding sources and a strong liquidity profile in order to fund our business and repay or refinance our maturing obligations under both normal operating conditions and periods of economic or financial stress. In managing our liquidity risk, we seek to maintain a prudent liability maturity profile and ready access to an ample store of primary and contingent liquidity sources. Our primary funding sources include direct-to-consumer and brokered deposits, public term asset-backed securitizations and other short-term and long-term borrowings. Our primary liquidity sources include a liquidity portfolio comprised of highly liquid, unencumbered

assets, including cash and cash equivalents and investment securities, and borrowing capacity through private term asset-backed securitizations. In addition, we have unused capacity with the Federal Reserve discount window which provides another source of contingent liquidity.

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Funding Sources

Deposits

We offer deposit products to customers through two channels: (i) through direct marketing, internet origination and affinity relationships (“direct-to-consumer deposits”); and (ii) indirectly through contractual arrangements with securities brokerage firms (“brokered deposits”). Direct-to-consumer deposits include certificates of deposit, money market accounts, online savings and checking accounts, and IRA certificates of deposit, while brokered deposits include certificates of deposit and sweep accounts. At June 30, 2017, we had $37.7 billion of direct-to-consumer deposits and $15.2 billion of brokered and other deposits.

Credit Card Securitization Financing

We use the securitization of credit card receivables as a source of funding. We access the asset-backed securitization market using the Discover Card Master Trust I ("DCMT") and the Discover Card Execution Note Trust ("DCENT"), through which we issue DCENT DiscoverSeries notes both publicly and through private transactions. From time to time, we may add credit card receivables to these trusts to create sufficient funding capacity for future securitizations while managing the seller’s interest. We retain significant exposure to the performance of trust assets through holdings of the seller's interest and subordinated security classes of DCENT.

The securitization structures include certain features designed to protect investors. The primary feature relates to the availability and adequacy of cash flows in the securitized pool of receivables to meet contractual requirements, the insufficiency of which triggers early repayment of the securities. We refer to this as "economic early amortization," which is based on excess spread levels. Excess spread is the amount by which income received by a trust during a collection period, including interest collections, fees and interchange, exceeds the fees and expenses of the trust during such collection period, including interest expense, servicing fees and charged-off receivables. In the event of an economic early amortization, which would occur if the excess spread fell below 0% on a three-month rolling average basis, we would be required to repay the affected outstanding securitized borrowings using available collections received by the trust (the period of ultimate repayment would be determined by the amount and timing of collections received). An early amortization event would negatively impact our liquidity and require us to utilize our available non-securitization related contingent liquidity or rely on alternative funding sources, which may or may not be available at the time. As of June 30, 2017, the DiscoverSeries three-month rolling average excess spread was 12.68%.

We may elect to add receivables to the restricted pool of receivables subject to certain requirements. Through our wholly-owned indirect subsidiary, Discover Funding LLC, we are required to maintain a contractual minimum level of receivables in the trust in excess of the face value of outstanding investors’ interests. This excess is referred to as the minimum seller’s interest. The required minimum seller’s interest in the pool of trust receivables, which is included in credit card loan receivables restricted for securitization investors, is set at approximately 7% in excess of the total investors’ interests (which includes interests held by third parties as well as those interests held by us). If the level of receivables in the trust was to fall below the required minimum, we would be required to add receivables from the unrestricted pool of receivables, which would increase the amount of credit card loan receivables restricted for securitization investors. A decline in the amount of the excess seller’s interest could occur if balance repayments and charge-offs exceeded new lending on the securitized accounts or as a result of changes in total outstanding investors’ interests. Seller's interest is impacted by seasonality as higher balance repayments tend to occur in the first calendar year quarter. If we could not add enough receivables to satisfy the requirement, an early amortization (or repayment) of investors’ interests would be triggered. No accounts were added to those restricted for securitization investors for the three or six months ended June 30, 2017.

At June 30, 2017, we had $16.1 billion of outstanding public asset-backed securities and $5.1 billion of outstanding subordinated asset-backed securities that had been issued to our wholly-owned subsidiaries.

The following table summarizes expected contractual maturities of the investors’ interests in credit card securitizations excluding those that have been issued to our wholly-owned subsidiaries (dollars in millions):

At June 30, 2017	Total	Less Than One Year	One Year Through	Four Years Through	After Five Years

			Three Years	Five Years	
Scheduled maturities of long-term borrowings - owed to credit card securitization investors	$16,030	$3,949	$ 8,634	$ 2,128	$1,319

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The triple-A rating of DCENT Class A Notes issued to date has been based, in part, on an FDIC rule which created a safe harbor that provides that the FDIC, as conservator or receiver, will not, using its power to disaffirm or repudiate contracts, seek to reclaim or recover assets transferred in connection with a securitization, or recharacterize them as assets of the insured depository institution, provided such transfer satisfies the conditions for sale accounting treatment under previous GAAP. Although the implementation of the Financial Accounting Standards Board Accounting Standards Codification Topic 860, Transfers and Servicing, no longer qualified certain transfers of assets for sale accounting treatment, the FDIC approved a final rule that preserved the safe-harbor treatment applicable to revolving trusts and master trusts, including DCMT, so long as those trusts would have satisfied the original FDIC safe harbor if evaluated under GAAP pertaining to transfers of financial assets in effect prior to December 1, 2009. Other legislative and regulatory developments may, however, impact our ability and/or desire to issue asset-backed securities in the future.

Other Long-Term Borrowings—Student Loans

At June 30, 2017, we had $728 million of remaining principal balance outstanding on securitized debt assumed as part of the acquisition of The Student Loan Corporation. Principal and interest payments on the underlying student loans will reduce the balance of these secured borrowings over time.

Other Long-Term Borrowings - Corporate and Bank Debt

The following table provides a summary of Discover Financial Services (Parent Company) and Discover Bank outstanding fixed-rate debt (dollars in millions):

At June 30, 2017	Principal Amount Outstanding
Discover Financial Services (Parent Company) fixed-rate senior notes, maturing 2019-2027	$ 2,900
Discover Financial Services (Parent Company) fixed-rate retail notes, maturing 2017-2031	$ 232
Discover Bank fixed-rate senior bank notes, maturing 2018-2026	$ 6,150
Discover Bank fixed-rate subordinated bank notes, maturing 2019-2020	$ 700

Certain Discover Financial Services senior notes require us to offer to repurchase the notes at a price equal to 101% of their aggregate principal amount plus accrued and unpaid interest in the event of a change of control involving us and a corresponding ratings downgrade to below investment grade.

Short-Term Borrowings

As part of our regular funding strategy, we may from time to time borrow short-term funds in the Federal Funds market or the repurchase (“repo”) market through repurchase agreements. Federal Funds are short-term, unsecured loans between banks or other financial entities with a Federal Reserve account. Funds borrowed in the repo market are short-term, collateralized loans usually secured with highly-rated investment securities such as U.S. Treasury bills or notes, or federal agency mortgage bonds or debentures. At June 30, 2017 and December 31, 2016, there were no outstanding balances under the Federal Funds market or repurchase agreements.

Additional Funding Sources

Private Asset-Backed Securitizations

We have access to committed, undrawn borrowing capacity through privately placed asset-backed securitizations. At June 30, 2017, we had total committed capacity of $6.0 billion, none of which was drawn. While we may utilize funding from these private securitizations from time to time for normal business operations, their committed nature also makes them a reliable contingency funding source. Therefore, we reserve some undrawn capacity, based upon our liquidity stress testing results, for potential contingency funding needs. We also seek to ensure the stability and reliability of these securitizations by staggering their maturity dates and renewing them approximately one year prior to their scheduled maturity dates.

Federal Reserve

Discover Bank has access to the Federal Reserve Bank of Philadelphia’s discount window. As of June 30, 2017, Discover Bank had $25.9 billion of available borrowing capacity through the discount window based on the amount and type

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of assets pledged. We have no borrowings outstanding under the discount window and reserve this capacity as a source of contingency funding.

Funding Uses

Our primary uses of funds include the extensions of loans and credit, primarily through Discover Bank, the purchase of investment securities for our liquidity portfolio, working capital, and debt and capital service. We assess funding uses and liquidity needs under stressed or normal conditions, considering primary uses of funding, such as on-balance sheet loans, and contingent uses of funding, such as the need to post additional collateral for derivatives positions. In order to anticipate funding needs under stress, we conduct liquidity stress testing to assess the impact of idiosyncratic, market-wide, and hybrid scenarios with varying levels of liquidity risk reflecting a range of stress severity.

Credit Ratings

Our borrowing costs and capacity in certain funding markets, including securitizations and unsecured senior and subordinated debt, may be affected by the credit ratings of DFS, Discover Bank and the securitization trusts. Downgrades in these credit ratings could result in higher interest expense on our unsecured debt and asset securitizations, as well as higher collateral enhancement requirements for both our public and private asset securitizations. In addition to increased funding costs, deterioration in credit ratings could reduce our borrowing capacity in the unsecured debt and asset securitization capital markets.

We also maintain agreements with certain of our derivative counterparties that contain provisions that require DFS and Discover Bank to maintain an investment grade credit rating from specified major credit rating agencies. At June 30, 2017, Discover Bank's credit rating met specified thresholds set by its counterparties. However, if Discover Bank's credit ratings were reduced by one ratings notch, Discover Bank would be required to post additional collateral, which, as of June 30, 2017, would have been $38 million. DFS (Parent Company) had no outstanding derivatives as of June 30, 2017, therefore, no collateral was required.

A credit rating is not a recommendation to buy, sell or hold securities, may be subject to revision or withdrawal at any time by the assigning rating organization, and each rating should be evaluated independently of any other rating. Our credit ratings are summarized in the following table:

	Moody’s Investors Service	Standard & Poor’s	Fitch Ratings
Discover Financial Services			
Senior unsecured debt	Ba1	BBB-	BBB+
Outlook for Discover Financial Services senior unsecured debt	Stable	Stable	Stable
Discover Bank			
Senior unsecured debt	Baa3	BBB	BBB+
Outlook for Discover Bank senior unsecured debt	Stable	Stable	Stable
Subordinated debt	Ba1	BBB-	BBB
Discover Card Execution Note Trust			
Class A[1]	Aaa(sf)	AAA(sf)	AAA(sf)

(1) An “sf” in the rating denotes rating agency identification for structured finance product ratings.

Liquidity

We seek to ensure that we have adequate liquidity to sustain business operations, fund asset growth and satisfy debt obligations under stressed or normal conditions. In addition to the funding sources discussed in the previous section, we also maintain highly liquid, unencumbered assets in our liquidity portfolio that we expect to be able to convert to cash quickly and with little loss of value using either the repo market or outright sales.

We maintain a liquidity risk and funding management policy which outlines the overall framework and general principles for managing liquidity risk across our business. The policy is approved by the Board of Directors with the implementation responsibilities delegated to the Asset and Liability Management Committee (the “ALCO”). We seek to balance the trade-offs between maintaining too much liquidity, which may be costly, with having too little liquidity, which could cause financial distress. Liquidity risk is centrally managed by the ALCO, which is chaired by our Treasurer and has cross-functional membership. The ALCO monitors the liquidity risk profiles of DFS and Discover

Bank and oversees any

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actions Corporate Treasury may take to ensure that we maintain ready access to our funding sources and sufficient liquidity to meet current and projected needs. In addition, the ALCO and our Board of Directors regularly review our compliance with our liquidity limits at DFS and Discover Bank, which are established in accordance with the liquidity risk appetite set by our Board of Directors.

We employ a variety of metrics to monitor and manage liquidity. We utilize early warning indicators ("EWIs") to detect the initial phases of liquidity stress events and a reporting and escalation process that is designed to be consistent with regulatory guidance. The EWIs include both idiosyncratic and systemic measures, and are monitored on a daily basis and reported to the ALCO regularly. A warning from one or more of these indicators triggers prompt review and decision-making by our senior management team, and in certain instances may lead to the convening of a senior-level response team and activation of our contingency funding plan.

In addition, we conduct liquidity stress testing regularly and ensure contingency funding is in place to address potential liquidity shortfalls. We evaluate a range of stress scenarios that are designed in accordance with regulatory requirements, including idiosyncratic, systemic and a combination of such events that could impact funding sources and our ability to meet liquidity needs. These scenarios measure the projected liquidity position at DFS and Discover Bank across a range of time horizons by comparing estimated contingency funding needs to available contingent liquidity.

Our primary liquidity sources include our liquidity portfolio and private securitizations with unused borrowing capacity, which we could utilize to satisfy liquidity needs during stressed or normal conditions. We seek to maintain sufficient liquidity to be able to satisfy all maturing obligations and fund business operations for at least 12 months in a severe stress environment. In addition, we have unused capacity with the Federal Reserve discount window which provides a source of contingent liquidity.

At June 30, 2017, our liquidity portfolio is comprised of highly liquid, unencumbered assets, including cash and cash equivalents and investment securities. Cash and cash equivalents were primarily in the form of deposits with the Federal Reserve. Investment securities primarily included debt obligations of the U.S. Treasury and residential mortgage-backed securities issued by U.S. government housing agencies. These investments are considered highly liquid, and we expect to have the ability to raise cash by selling them, utilizing repurchase agreements or pledging certain of these investments to access secured funding. The size and composition of our liquidity portfolio may fluctuate based upon the size of our Statement of Financial Condition as well as operational requirements and market conditions.

At June 30, 2017, our liquidity portfolio and undrawn credit facilities were $45.7 billion, which was $2.9 billion higher than the balance at December 31, 2016. During the three and six months ended June 30, 2017, the average balance of our liquidity portfolio was $15.0 billion.

	June 30, 2017	December 31, 2016
	(dollars in millions)	
Liquidity portfolio		
Cash and cash equivalents[1]	$ 12,403	$ 11,103
Investment securities[2]	1,462	1,532
Total liquidity portfolio	13,865	12,635
Private asset-backed securitizations[3]	6,000	6,000
Primary liquidity sources	19,865	18,635
Federal Reserve discount window[3]	25,877	24,194
Total liquidity portfolio and undrawn credit facilities	$ 45,742	$ 42,829

(1) Cash in the process of settlement and restricted cash are excluded from cash and cash equivalents for liquidity purposes.

(2) Excludes $37 million and $73 million of U.S. Treasury securities that have been pledged as swap collateral in lieu of cash as of June 30, 2017 and December 31, 2016, respectively.

(3) See "— Additional Funding Sources" for additional information.

Bank Holding Company Liquidity

The primary uses of funds at the unconsolidated DFS level include debt service obligations (interest payments and return of principal) and capital management activities, which include dividends on capital instruments and the periodic repurchase of shares of our common stock. Our primary sources of funds at the bank holding company level include the

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proceeds from the issuance of unsecured debt and preferred stock in the capital markets, as well as dividends from our subsidiaries, particularly Discover Bank. Under periods of idiosyncratic or systemic stress, the bank holding company could lose or experience impaired access to the capital markets. In addition, our regulators have the discretion to restrict dividend payments from Discover Bank to the bank holding company.

We utilize a measure referred to as Number of Months of Pre-Funding to determine the length of time Discover Financial Services can meet upcoming funding obligations including common and preferred dividend payments and debt service obligations using existing cash resources. At June 30, 2017, Discover Financial Services had sufficient cash resources to fund the dividend and debt service payments for more than 18 months.

We structure our debt maturity schedule to minimize the amount of debt maturing at the bank holding company within a short period of time. See Note 6: Long-Term Borrowings to our condensed consolidated financial statements for further information regarding our debt. Our ALCO and board of directors regularly review our compliance with our liquidity limits as a bank holding company, which are established in accordance with the liquidity risk appetite articulated by our Board of Directors.

Capital

Our primary sources of capital are from the earnings generated by our businesses and common and preferred stock issuances in the capital markets. We seek to manage capital to a level and composition sufficient to support the risks of our businesses, meet regulatory requirements, meet rating agency targets and debt investor expectations and support future business growth. Within these constraints, we are focused on deploying capital in a manner that provides attractive returns to our stockholders. The level, composition and utilization of capital are influenced by changes in the economic environment, strategic initiatives, and legislative and regulatory developments.

Under regulatory capital requirements adopted by the Federal Reserve and the FDIC, Discover Financial Services, along with Discover Bank, must maintain minimum levels of capital. Failure to meet minimum capital requirements can result in the initiation of certain mandatory and possibly additional discretionary actions by regulators that, if undertaken, could limit our business activities and have a direct material effect on our financial position and results. We must meet specific capital requirements that involve quantitative measures of assets, liabilities and certain off-balance sheet items, as calculated under regulatory guidance and regulations. Current or future legislative or regulatory initiatives may require us to hold more capital in the future.

In 2013, the Federal Reserve, the Office of the Comptroller of the Currency, and the FDIC issued the Basel III rules applicable to Discover Financial Services and Discover Bank. Under those rules, Discover Financial Services and Discover Bank are classified as "Standardized Approach" entities, defined as U.S. banking organizations with consolidated total assets over $50 billion but not exceeding $250 billion and consolidated total on-balance sheet foreign exposures less than $10 billion. Additional phase-in requirements related to components of the final capital rules will become effective through 2019. The Basel III rules include new minimum and "well-capitalized" risk-based capital and leverage ratios, effective January 1, 2015, and refine the definition of what constitutes "capital" for purposes of calculating those ratios of which certain requirements are subject to phase-in periods through the end of 2018 (the "transition period"). During the transition period, the effects of the changes to capital (i.e., certain deductions and adjustments) are recognized in 20% increments from 2015 through 2018. For example, one of the deductions from CET1 capital, goodwill and intangibles, was subject to a 40% of total deduction in 2015 that increased to 60% in 2016 and so on, until reaching 100% deduction of total in 2018. For additional information regarding the risk-based capital and leverage ratios, see Note 10: Capital Adequacy to our condensed consolidated financial statements.

The Basel III rules also introduced a capital conservation buffer on top of the minimum risk-weighted asset ratios. The buffer is designed to absorb losses during periods of economic stress. The calculation of the buffer started to phase in beginning on January 1, 2016 at the rate of 0.625% and increases by 0.625% on each subsequent January 1 until it reaches the maximum 2.5% on January 1, 2019. When the capital conservation buffer is fully phased-in on January 1, 2019, this will effectively result in minimum ratios of (i) CET1 to risk-weighted assets of at least 7.0%, (ii) Tier 1 capital to risk-weighted assets of at least 8.5% and (iii) Total capital to risk-weighted assets of at least 10.5%. Banking institutions with a capital ratio below the required amount will face constraints on dividends, equity repurchases and compensation based on the amount of the shortfall.

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Another main component of the Basel III rules is a prescribed standardized approach for calculating risk-weighted assets that expands the risk-weight range from 0% to 100% (under Basel I) to 0% to 1,250% (under Basel III). The new range is intended to be more risk-sensitive and the risk-weight assigned depends on the nature of the asset in question.

The Basel III rules provide for a number of the deductions from and adjustments to CET1, to the extent that any one such category exceeds 10% of CET1 or all such categories in the aggregate exceed 15%.

Basel III also requires disclosures relating to market discipline. This series of disclosures is commonly referred to as "Pillar 3." The objective is to increase transparency of capital requirements for banking organizations. We are required to make prescribed regulatory disclosures on a quarterly basis regarding our capital structure, capital adequacy, risk exposures and risk-weighted assets. The Pillar 3 disclosures are made publicly available, on our website, as a stand-alone report called "Basel III Regulatory Capital Disclosures."

At June 30, 2017, Discover Financial Services and Discover Bank met the requirements for "well-capitalized" status under Regulation Y and the prompt corrective action rules, respectively, exceeding the regulatory minimums to which they were subject under the applicable rules.

As discussed in Note 10: Capital Adequacy to our condensed consolidated financial statements, we are subject to a CET1 capital ratio requirement under the Basel III rules. We believe that providing an estimate of our capital position based on the Basel III fully phased-in rules is important to complement the existing capital ratios and for comparability to other financial institutions. In addition, we disclose tangible common equity, which represents common equity less goodwill and intangibles. Management believes that common stockholders' equity excluding goodwill and intangibles is a more meaningful measure to investors of our true net asset value. As of June 30, 2017, the CET1 capital ratio calculated under Basel III fully phased-in rules and tangible common equity are not formally defined by U.S. GAAP or codified in the federal banking regulations and, as such, they are considered to be non-GAAP financial measures. Other financial services companies may also disclose this ratio and metric and definitions may vary, so we advise users of this information to exercise caution in comparing this ratio and metric for different companies.

The following table provides a reconciliation of total common stockholders' equity (a U.S. GAAP financial measure) to tangible common equity (dollars in millions):

	June 30, 2017	December 31, 2016
Total common stockholders' equity[1]	$10,699	$ 10,763
Less: Goodwill	(255)	(255)
Less: Intangible assets, net	(164)	(166)
Tangible common equity	$10,280	$ 10,342

(1) Total common stockholders' equity is calculated as total stockholders' equity less preferred stock.

The following table provides a reconciliation of CET1 capital calculated under Basel III transition rules to CET1 capital and risk-weighted assets calculated under fully phased-in Basel III rules (dollars in millions):

	June 30, 2017
Common equity Tier 1 capital (Basel III transition)	$10,492
Adjustments related to capital components during transition[1]	(25)
Common equity Tier 1 capital (Basel III fully phased-in)	$10,467
Risk-weighted assets (Basel III fully phased-in)[2]	$80,417
Common equity Tier 1 capital ratio (Basel III fully phased-in)	13.0 %

(1)

Adjustments related to capital components for fully phased-in Basel III include the phase-in of the intangible asset exclusion.

(2) Key differences under fully phased-in Basel III rules in the calculation of risk-weighted assets include higher risk weighting for past-due loans and unfunded commitments.

Additionally, we are required to submit an annual capital plan to the Federal Reserve that includes an assessment of our expected uses and sources of capital over a nine quarter planning horizon. We submitted our annual capital plan to the Federal Reserve under the Federal Reserve's CCAR program and received notice in June 2017 that the Federal Reserve does not object to our proposed capital plan, including planned quarterly capital distributions through June 30, 2018. Our ability to

make capital distributions, including our ability to pay dividends on or repurchase shares of our common stock, will continue to be subject to the Federal Reserve's review and non-objection of the actions that we propose each year in our annual capital plan.

Also in June 2017, the Federal Reserve published the results of its annual supervisory stress tests for bank holding companies with $50 billion or more in total consolidated assets, including Discover Financial Services. At that same time, we published company-run stress test results for Discover Financial Services and Discover Bank. Discover Financial Services is required to publish company-run stress tests results twice each year in accordance with Federal Reserve rules and Discover Bank is required to publish bank-run stress test results under FDIC rules.

We recently declared a quarterly cash dividend on our common stock of $0.35 per share, payable on September 7, 2017 to holders of record on August 24, 2017, which is an increase from $0.30 per share paid in each of the last four quarters. We also recently declared a quarterly cash dividend on our preferred stock of $16.25 per share, equal to $0.40625 per depositary share, payable on September 1, 2017, to holders of record on August 15, 2017, which was the same as the amount paid on our preferred stock in the prior quarter.

On July 25, 2017, our Board of Directors approved a share repurchase program authorizing the repurchase of up to $2.8 billion of our outstanding shares of common stock. The program expires on October 31, 2018 and may be terminated at any time. This program replaced the prior $2.5 billion share repurchase program, which had $562 million of remaining authorization. During the three months ended June 30, 2017, we repurchased approximately 7 million shares, or 2%, of our outstanding common stock for $450 million. We expect to continue to make share repurchases under our repurchase program from time to time based on market conditions and other factors, subject to legal and regulatory requirements and restrictions, including approval from the Federal Reserve described above. Share repurchases under the program may be made through a variety of methods, including open market purchases, privately negotiated transactions or other purchases, including block trades, accelerated share repurchase transactions, or any combination of such methods.

The amount and size of any future dividends and share repurchases will depend upon our results of operations, financial condition, capital levels, cash requirements, future prospects and other factors. The declaration and payment of future dividends, as well as the amount thereof, are subject to the discretion of our Board of Directors. Holders of our shares of common stock are subject to the prior dividend rights of holders of our preferred stock or the depositary shares representing such preferred stock outstanding, and if full dividends have not been declared and paid on all outstanding shares of preferred stock in any dividend period, no dividend may be declared or paid or set aside for payment on our common stock. In addition, as noted above, banking laws and regulations and our banking regulators may limit our ability to pay dividends and make share repurchases, including limitations on the extent to which our banking subsidiaries can provide funds to us through dividends, loans or otherwise. Further, also noted above, current or future regulatory initiatives may require us to hold more capital in the future. There can be no assurance that we will declare and pay any dividends or repurchase any shares of our common stock in the future.

Certain Off-Balance Sheet Arrangements

Guarantees

Guarantees are contracts or indemnification agreements that contingently require us to make payments to a guaranteed party based on changes in an underlying asset, liability, or equity security of a guaranteed party, rate or index. Also included in guarantees are contracts that contingently require the guarantor to make payments to a guaranteed party based on another entity's failure to perform under an agreement. Our guarantees relate to transactions processed on the Discover Network and certain transactions processed by PULSE and Diners Club. See Note 11: Commitments, Contingencies and Guarantees to our condensed consolidated financial statements for further discussion regarding our guarantees.

Contractual Obligations and Contingent Liabilities and Commitments

In the normal course of business, we enter into various contractual obligations that may require future cash payments. Contractual obligations at June 30, 2017, which include deposits, long-term borrowings, operating and capital lease obligations, interest payments on fixed-rate debt, purchase obligations and other liabilities were $83.2 billion. For a description of our contractual obligations, see our annual report on Form 10-K for the year ended December 31, 2016 under "Management's Discussion and Analysis of Financial Condition and Results of Operations — Contractual

Obligations and Contingent Liabilities and Commitments."

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We extend credit for consumer loans, primarily arising from agreements with customers for unused lines of credit on certain credit cards, provided there is no violation of conditions established in the related agreement. At June 30, 2017, our unused commitments were approximately $184.3 billion. These commitments, substantially all of which we can terminate at any time and which do not necessarily represent future cash requirements, are periodically reviewed based on account usage, customer creditworthiness and loan qualification. In addition, in the ordinary course of business, we guarantee payment on behalf of subsidiaries relating to contractual obligations with external parties. The activities of the subsidiaries covered by any such guarantees are included in our condensed consolidated financial statements.

Item 3. Quantitative and Qualitative Disclosures About Market Risk

Market risk refers to the risk that a change in the level of one or more market prices, rates, indices, correlations or other market factors will result in losses for a position or portfolio. We are exposed to market risk primarily from changes in interest rates.

Interest Rate Risk

We borrow money from a variety of depositors and institutions in order to provide loans to our customers, as well as invest in other assets and our business. These loans and other assets earn interest, which we use to pay interest on the money borrowed. Our net interest income and, therefore, earnings, will be negatively affected if the interest rate earned on assets increases at a slower pace than increases to the interest rate we owe on our borrowings. Changes in interest rates and competitor responses to those changes may influence customer payment rates, loan balances or deposit account activity. We may face higher-cost alternative sources of funding as a result, which has the potential to decrease earnings.

Our interest rate risk management policies are designed to measure and manage the potential volatility of earnings that may arise from changes in interest rates by having a financing portfolio that reflects the mix of variable and fixed-rate assets. To the extent that asset and related financing repricing characteristics of a particular portfolio are not matched effectively, we may utilize interest rate derivative contracts, such as swap agreements, to achieve our objectives. Interest rate swap agreements effectively convert the underlying asset or liability from fixed to floating rate or from floating to fixed rate. See Note 14: Derivatives and Hedging Activities to our condensed consolidated financial statements for information on our derivatives activity.

We use an interest rate sensitivity simulation to assess our interest rate risk exposure. For purposes of presenting the possible earnings effect of a hypothetical, adverse change in interest rates over the 12-month period from our reporting date, we assume that all interest rate sensitive assets and liabilities will be impacted by a hypothetical, immediate 100 basis point increase in interest rates relative to market consensus expectations as of the beginning of the period. The sensitivity is based upon the hypothetical assumption that all relevant types of interest rates that affect our results would increase instantaneously, simultaneously and to the same degree.

Our interest rate sensitive assets include our variable rate loan receivables and the assets that make up our liquidity portfolio. We have restrictions on our ability to mitigate interest rate risk by adjusting rates on existing balances and competitive actions may restrict our ability to increase the rates that we charge to customers for new loans. At June 30, 2017, the majority of our credit card and student loans were at variable rates. Assets with rates that are fixed at period end but which will mature, or otherwise contractually reset to a market-based indexed rate or other fixed rate prior to the end of the 12-month period, are considered to be rate sensitive. The latter category includes certain revolving credit card loans that may be offered at below-market rates for an introductory period, such as balance transfers and special promotional programs, after which the loans will contractually reprice in accordance with our normal market-based pricing structure. For purposes of measuring rate sensitivity for such loans, only the effect of the hypothetical 100 basis point change in the underlying market-based indexed rate has been considered. For assets that have a fixed interest rate but which contractually will, or are assumed to, reset to a market-based indexed rate or other fixed rate during the next 12 months, earnings sensitivity is measured from the expected repricing date. In addition, for all interest rate sensitive assets, earnings sensitivity is calculated net of expected loan losses, which for purposes of this analysis are assumed to remain unchanged relative to our baseline expectations over the analysis horizon.

Interest rate sensitive liabilities are assumed to be those for which the stated interest rate is not contractually fixed for the next 12-month period. Thus, liabilities that vary with changes in a market-based index, such as Federal Funds or

LIBOR, which will reset before the end of the 12-month period, or liabilities whose rates are fixed at the fiscal period end, but which will mature and are assumed to be replaced with a market-based indexed rate prior to the end of the 12-month period, also are

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considered to be rate sensitive. For these fixed-rate liabilities, earnings sensitivity is measured from the expected maturity date.
Net interest income sensitivity requires assumptions to be made regarding market conditions, consumer behavior, and the overall growth and composition of the balance sheet. These assumptions are inherently uncertain and, as a result, actual earnings may differ from the simulated earnings presented above. Our actual earnings are dependent on multiple factors including, but not limited to, the direction and timing of changes in interest rates, the movement of short-term versus long-term rates, balance sheet design, competitor actions, which may affect pricing decisions in our loans and deposits, and strategic actions undertaken by management.

Assuming an immediate 100 basis point increase in the interest rates affecting all interest rate sensitive assets and liabilities at June 30, 2017, we estimate that net interest income over the following 12-month period would increase by approximately $190 million, or 2%. Assuming an immediate 100 basis point increase in the interest rates affecting all interest rate sensitive assets and liabilities at December 31, 2016, we estimated that net interest income over the following 12-month period would increase by approximately $201 million, or 3%. Should an immediate 100 basis point interest rate decrease occur, we estimate that the impact would be approximately the opposite of the result of an immediate 100 basis point increase. However, at current interest rates there is a higher level of uncertainty in the assumptions used to derive this estimate because a decline of that magnitude would result in a near zero interest rate environment.

Item 4. Controls and Procedures

Evaluation of Disclosure Controls and Procedures

Under the supervision and with the participation of our management, including our Chief Executive Officer and Chief Financial Officer, we conducted an evaluation of the effectiveness of our disclosure controls and procedures (as defined in Rule 13a-15(e) and 15d-15(e) of the Securities Exchange Act of 1934, as amended (the “Exchange Act”)), which are designed to ensure that information required to be disclosed by us in the reports that we file or submit under the Exchange Act is recorded, processed, summarized and reported within the time periods specified by the SEC’s rules and forms. Disclosure controls and procedures include, without limitation, controls and procedures designed to ensure that information required to be disclosed by us in the reports that we file or submit under the Exchange Act is accumulated and communicated to our management, including our Chief Executive Officer and Chief Financial Officer, as appropriate to allow timely decisions regarding required disclosure. Based on this evaluation, our Chief Executive Officer and Chief Financial Officer concluded that our disclosure controls and procedures were effective as of the end of the period covered by this report.

Changes in Internal Control over Financial Reporting

There have been no changes in our internal control over financial reporting (as such term is defined in Exchange Act Rule 13a-15(f) and 15d-15(f)) that occurred during the period covered by this report that have materially affected, or are reasonably likely to materially affect, our internal control over financial reporting.

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Part II. OTHER INFORMATION

Item 1. Legal Proceedings

For a description of legal proceedings, see Note 12: Litigation and Regulatory Matters to our condensed consolidated financial statements.

Item 1A. Risk Factors

There have been no material changes to the risk factors disclosed in our annual report on Form 10-K for the year ended December 31, 2016.

Item 2. Unregistered Sales of Equity Securities and Use of Proceeds

Issuer Purchases of Equity Securities

The table below sets forth information regarding purchases of our common stock related to our share repurchase program and employee transactions that were made by us or on our behalf during the most recent quarter.

Period	Total Number of Shares Purchased	Average Price Paid Per Share	Total Number of Shares Purchased as Part of Publicly Announced Plan or Program[1]	Maximum Dollar Value of Shares that may yet be purchased under the Plans or Programs [1]
April 1 - 30, 2017				
Repurchase program[1]	2,160,830	$ 66.49	2,160,830	$ 868,283,316
Employee transactions[2]	—	$ —	N/A	N/A
May 1 - 31, 2017				
Repurchase program[1]	2,720,004	$ 60.88	2,720,004	$ 702,676,053
Employee transactions[2]	1,796	$ 62.80	N/A	N/A
June 1 - 30, 2017				
Repurchase program[1]	2,345,576	$ 59.99	2,345,576	$ 561,959,418
Employee transactions[2]	314	$ 58.91	N/A	N/A
Total				
Repurchase program[1]	7,226,410	$ 62.27	7,226,410	$ 561,959,418
Employee transactions[2]	2,110	$ 62.22	N/A	N/A

(1) On July 25, 2017, our board of directors approved a share repurchase program authorizing the purchase of up to $2.8 billion of our outstanding shares of common stock. This share repurchase program expires on October 31, 2018 and may be terminated at any time.

(2) Reflects shares withheld (under the terms of grants under employee stock compensation plans) to offset tax withholding obligations that occur upon the delivery of outstanding shares underlying restricted stock units or upon the exercise of stock options.

Item 3. Defaults Upon Senior Securities

None.

Item 4. Mine Safety Disclosures

None.

Item 5. Other Information

None.

Item 6. Exhibits

See "Exhibit Index" for documents filed herewith and incorporated herein by reference.

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Signature

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

Discover Financial Services
(Registrant)

By: /s/ R. MARK GRAF
R. Mark Graf
Executive Vice President and Chief Financial Officer

Date: August 1, 2017

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Exhibit Index

Exhibit Number	Description
12.1	Statement regarding computation of ratio of earnings to fixed charges and computation of ratio of earnings to fixed charges and preferred stock dividends.
31.1	Certification of Chief Executive Officer pursuant to Rule 13a-14(a) under the Securities Exchange Act of 1934.
31.2	Certification of Chief Financial Officer pursuant to Rule 13a-14(a) under the Securities Exchange Act of 1934.
32.1	Certification of Chief Executive Officer and Chief Financial Officer pursuant to Section 1350 of Chapter 63 of Title 18 of the United States Code.
101.INS	XBRL Instance Document.
101.SCH	XBRL Taxonomy Extension Schema Document.
101.CAL	XBRL Taxonomy Extension Calculation Linkbase Document.
101.DEF	XBRL Taxonomy Extension Definition Linkbase Document.
101.LAB	XBRL Taxonomy Extension Label Linkbase Document.
101.PRE	XBRL Taxonomy Extension Presentation Linkbase Document.