

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

FORM 20-F

(Mark One)

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

OR

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

For the fiscal year ended December 31, 2022

OR

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

OR

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

Date of event requiring this shell company report

For the transition period from _____ to _____

Commission file number 001-39151

EHang Holdings Limited

(Exact name of Registrant as specified in its charter)

N/A

(Translation of Registrant's name into English)

Cayman Islands

(Jurisdiction of incorporation or organization)

11/F Building One, EHang Technology Park
No. 29 Bishan Blvd., Huangpu District
Guangzhou, 510700

People's Republic of China

(Address of principal executive offices)

Richard Jian Liu, Chief Financial Officer

Telephone: +86 20 2902 8899

EHang Holdings Limited

11/F Building One, EHang Technology Park
No. 29 Bishan Blvd., Huangpu District
Guangzhou, 510700

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	Trading Symbol(s)	Name of each exchange on which registered
American depositary shares, each representing two Class A ordinary shares, par value US\$0.0001 per share	EH	The Nasdaq Global Market
Class A ordinary shares, par value US\$0.0001 per share*		The Nasdaq Global Market*

* Not for trading, but only in connection with the listing on the Nasdaq Global Market of American depositary shares, each representing two Class A ordinary shares

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

None

(Title of Class)

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

None

(Title of Class)

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.

As of December 31, 2022, there were 116,455,947 ordinary shares outstanding, comprised of (i) 77,429,387 Class A ordinary shares (excluding Class A ordinary shares issued to the depositary bank for bulk issuance of ADSs reserved for future issuances upon the exercise or vesting of awards granted under our share incentive plans), par value of US\$0.0001 per share, and (ii) 39,026,560 Class B ordinary shares outstanding, par value of US\$0.0001 per share.

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

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

Note – Checking the box above will not relieve any registrant required to file reports pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934 from their obligations under those Sections.

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

Indicate by check mark whether the registrant has submitted electronically every Interactive Data File required to be submitted 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 such files). Yes ☒ No ☐

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

Large accelerated filer ☐

Accelerated filer ☒

Non-accelerated filer ☐

Emerging growth company ☒

If an emerging growth company that prepares its financial statements in accordance with U.S. GAAP, indicate by check mark if the registrant has elected not to use the extended transition period for complying with any new or revised financial accounting standards† provided pursuant to Section 13(a) of the Exchange Act. ☐

† The term "new or revised financial accounting standard" refers to any update issued by the Financial Accounting Standards Board to its Accounting Standards Codification after April 5, 2012.

Indicate by check mark whether the registrant has filed a report on and attestation to its management's assessment of the effectiveness of its internal control over financial reporting under Section 404(b) of the Sarbanes-Oxley Act (15 U.S.C. 7262(b)) by the registered public accounting firm that prepared or issued its audit report. Yes ☐ No ☒

If securities are registered pursuant to Section 12(b) of the Act, indicate by check mark whether the financial statements of the registrant included in the filing reflect the correction of an error to previously issued financial statements. ☐

Indicate by check mark whether any of those error corrections are restatements that required a recovery analysis of incentive-based compensation received by any of the registrant's executive officers during the relevant recovery period pursuant to § 240.10D-1(b). ☐

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

U.S. GAAP ☒

International Financial Reporting Standards as issued
by the International Accounting Standards Board ☐

Other ☐

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

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

(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. Yes ☐ No ☐

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INTRODUCTION

Conventions Used in this Annual Report

In this annual report, unless otherwise indicated or the context otherwise requires:

- “AAVs” means autonomous aerial vehicles;
- “ADSs” means American depositary shares, each of which represents two of our Class A ordinary shares;
- “CAAC” means the Civil Aviation Administration of China;
- “China” and the “PRC” means the People’s Republic of China, and only in the context of describing the PRC laws, rules, regulations, regulatory authorities, and any PRC entities or citizens under such rules, laws and regulations and other legal or tax matters in this annual report, excludes Hong Kong, Macau and Taiwan;
- “Class A ordinary shares” means class A ordinary shares, par value US\$0.0001 per share, of EHang Holdings;
- “Class B ordinary shares” means class B ordinary shares, par value US\$0.0001 per share, of EHang Holdings;
- “Ehfly Technology” means Ehfly Technology Limited, a company incorporated in Hong Kong and a direct, wholly-owned subsidiary of EHang Holdings;
- “EHang,” “we,” “us,” “our company” and “our” means collectively EHang Holdings and its subsidiaries and only in the context of describing our consolidated financial information only, also includes the VIE and the VIE’s subsidiaries;
- “EHang Holdings” means EHang Holdings Limited, a company incorporated in the Cayman Islands;
- “eVTOL” means electric vertical takeoff and landing;
- “PCAOB” means Public Company Accounting Oversight Board of the United States.
- “RMB” and “Renminbi” means the legal currency of China;
- “shares” and “ordinary shares” means the Class A ordinary shares and/or the Class B ordinary shares;
- “UAM” means urban air mobility;
- “UAVs” means unmanned aerial vehicles;
- “US\$,” “U.S. dollars,” “\$,” and “dollars” means the legal currency of the United States;
- “VIE” means Guangzhou EHang Intelligent Technology Co., Ltd., a company incorporated in the PRC that has entered into a series of contractual arrangement with our wholly-owned PRC subsidiary. Under these contractual arrangements, EHang Holdings has a “controlling financing interest” as defined in FASB ASC 810 such that it is considered the primary beneficiary for accounting purposes only and thus consolidates each of the VIE and the VIE’s subsidiaries under U.S. GAAP; and

- “WFOE” means EHang Intelligent Equipment (Guangzhou) Co., Ltd., a company incorporated in the PRC and an indirect, wholly-owned subsidiary of EHang Holdings.

Our reporting currency is the Renminbi because our business is mainly conducted in China and substantially all of our revenues are denominated in Renminbi. This annual report contains translations of Renminbi amounts into U.S. dollars at specific rates solely for the convenience of the reader. The translations of Renminbi amounts into U.S. dollars in this annual report is based on the rate certified for customs purposes by the Federal Reserve Bank of New York. Unless otherwise noted, all translations from Renminbi amounts into U.S. dollars and from U.S. dollars to Renminbi amounts in this annual report were made at a rate of RMB6.8972 to US\$1.00, the noon buying rate in effect as of December 30, 2022 set forth in the H.10 statistical release of the U.S. Federal Reserve Board. We make no representation that any Renminbi or U.S. dollar amounts 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.

FORWARD-LOOKING INFORMATION

Special Note Regarding Forward-Looking Statements

This annual report contains forward-looking statements that reflect our current expectations and views of future events. These forward-looking statements are made under the “safe-harbor” provisions of the U.S. Private Securities Litigation Reform Act of 1995. Known and unknown risks, uncertainties and other factors, including those listed under “Item 3. Key Information—D. Risk Factors,” may cause our actual results, performance or achievements to be materially different from those expressed or implied by the forward-looking statements. 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.

You can identify these forward-looking statements by words or phrases such as “may,” “will,” “expect,” “anticipate,” “aim,” “estimate,” “intend,” “plan,” “believe,” “likely to,” “potential,” “continue” or other similar expressions. We have based these forward-looking statements largely on our current expectations and projections about future events and trends that we believe may affect our financial condition, results of operations, business strategies and financial needs. These forward-looking statements include, but are not limited to, statements about:

- our goals and strategies;
- our future business development, financial condition and results of operations;
- the trends in and expected growth of the UAV industry in the PRC and globally;
- our expectation regarding the regulatory approvals and certifications for our products and services;
- our expectations regarding the demand for and market acceptance of our products and services;
- our expectations regarding our relationships with distributors, customers, component suppliers, strategic partners and other stakeholders;
- our expectations regarding our capacity to develop, manufacture and delivery AAV products in fulfilment of our contractual commitments, including orders and pre-orders;
- competition in our industry;
- relevant government policies and regulations relating to our industry; and
- assumptions underlying or related to any of the foregoing.

These forward-looking statements involve various risks and uncertainties. You should read thoroughly this annual report and the documents that we refer to with the understanding that our actual future results may be materially different from, or worse than, what we expect. Other sections of this annual report include additional factors that could adversely impact our business and financial performance. Moreover, we operate in an evolving environment. New risk factors and uncertainties emerge from time to time and it is not possible for our management to predict all risk factors and uncertainties, nor can we assess the impact of all factors on our business or the extent to which any factor, or combination of factors, may cause actual results to differ materially from those contained in any forward-looking statements. We qualify all of our forward-looking statements by these cautionary statements.

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This annual report contains certain data and information that we obtained from various government and private publications. Statistical data in these publications also include projections based on a number of assumptions. The AAV industry may not grow at the rate projected by market data, or at all. Failure of this market to grow at the projected rate may have a material adverse effect on our business and the market price of the ADSs. In addition, the rapidly evolving nature of the AAV industry results in significant uncertainties for any projections or estimates relating to the growth prospects or future condition of our market. Furthermore, if any one or more of the assumptions underlying the market data are later found to be incorrect, actual results may differ from the projections based on these assumptions. You should not place undue reliance on these forward-looking statements.

You should not rely upon forward-looking statements as predictions of future events. We undertake no obligation to update or revise any forward-looking statements, whether as a result of new information, future events or otherwise, after the date 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 refer to in this annual report and have filed as exhibits to this annual report, of which this annual report is a part, completely and with the understanding that our actual future results may be materially different from, or worse than, what we expect.

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

Our Corporate Structure and Contractual Arrangements with the VIE and its Shareholders

EHang Holdings is not a PRC operating company but a Cayman Islands holding company conducting operations in China primarily through its subsidiaries incorporated in the PRC, including EHang Intelligent Equipment (Guangzhou) Co., Ltd., or the WFOE. PRC laws and regulations impose certain restrictions or prohibitions on foreign ownership of companies in the UAM industry. Pursuant to the latest version of the “negative list,” namely, the Special Management Measures (Negative List) for the Access of Foreign Investment (2021), which became effective on January 1, 2022, our principal business does not fall into the “restricted” or “prohibited” categories. However, foreign investment in commercial and general aviation is restricted under PRC laws and regulations. Accordingly, Guangzhou EHang Intelligent Technology Co., Ltd., or the VIE, and its subsidiaries conduct business operations in the PRC, which may not be conducted by EHang Holdings and/or its subsidiaries under PRC laws and regulations, and the WFOE, the VIE and the VIE’s shareholders have entered into a series of contractual arrangements. These agreements enable us to:

- have the power to direct significant activities of the VIE;
- receive economic benefits from the VIE that potentially could be significant to the VIE; and
- have an exclusive option to purchase all or part of the equity interests and assets in the VIE, when and to the extent permitted by PRC laws.

These contractual arrangements among the WFOE, the VIE and the VIE’s shareholders include shareholders voting proxy agreements, exclusive consulting and services agreements, exclusive option agreements, loan agreements, and share pledge agreements. Under the contractual arrangements, EHang Holdings has a “controlling financing interest” as defined in FASB ASC 810 such that EHang Holdings is considered the primary beneficiary of the VIE and the VIE’s subsidiaries for accounting purposes only and thus consolidates each of these entities under U.S. GAAP. For more details of these contractual arrangements, see “Item 4. Information on the Company—C. Organizational Structure—Contractual Arrangements with the VIE and its Shareholders.” Investors in the ADSs are not purchasing equity interest in the VIE or the VIE’s subsidiaries but instead are purchasing equity interest in EHang Holdings, a Cayman Islands holding company. Revenues contributed by the VIE and the VIE’s subsidiaries accounted for 19.6%, 0.4% and 0.01% of our consolidated revenues for the years ended December 31, 2020, 2021 and 2022, respectively.

However, the contractual arrangements may not be as effective as direct ownership in providing us with power to direct the activities of the VIE and we may incur substantial costs to enforce the terms of the agreements. If the VIE or the VIE’s shareholders fail to perform their respective obligations under the contractual arrangements, we could be limited in our ability to enforce the contractual arrangements that give us power to direct the activities of the VIE, and these agreements have not been tested in China courts. Furthermore, if we are unable to direct the activities of the VIE and the VIE’s subsidiaries, we would not be able to continue to consolidate the financial results of these entities in our financial statements. Please see “Item 3. Key Information—D. Risk Factors—Risks Relating to Our Corporate Structure—We rely on contractual arrangements with the VIE and the VIE’s shareholders for certain business operations in the PRC, which may not be as effective as direct ownership in providing operational control” and “Item 3. Key Information—D. Risk Factors—Risks Relating to Our Corporate Structure—The shareholders of the VIE may have potential conflicts of interest with us, which may materially and adversely affect our business and financial condition.”

There are also substantial uncertainties regarding the interpretation and application of current and future PRC laws, regulations and rules regarding the status of the rights of our Cayman Islands holding company with respect to the contractual arrangements with the VIE and the VIE's shareholders. It is uncertain whether any new PRC laws or regulations relating to variable interest entity structures will be adopted or if adopted, what they would provide. If we or the VIE is found to be in violation of any existing or future PRC laws or regulations, or fail to obtain or maintain any of the required permits or approvals, the relevant PRC regulatory authorities would have broad discretion in accordance with the applicable laws and regulations to take action in dealing with such violations or failures. Please see "Item 3. Key Information—D. Risk Factors—Risks Relating to Our Corporate Structure—If the PRC government finds that the contractual arrangements between the WFOE, the VIE and the VIE's shareholders do not comply with PRC regulations relating to the relevant industries, or if these regulations or the interpretation of existing regulations change in the future, we could be subject to severe penalties or be forced to relinquish our interests in those operations" and "Item 3. Key Information—D. Risk Factors—Risks Relating to Our Corporate Structure—Our business may be significantly affected by the Foreign Investment Law."

Our corporate structure is subject to risks associated with our contractual arrangements with the VIE. Investors may never have a direct ownership interest in the businesses that are conducted by the VIE. Uncertainties in the PRC legal system could limit our ability to enforce these contractual arrangements, and these contractual arrangements have not been tested in a court of law. If the PRC government finds that the agreements that establish the structure for operating our business in China do not comply with PRC laws and regulations, or if these regulations or the interpretation of existing regulations change or are interpreted differently in the future, we and the VIE could be subject to severe penalties or be forced to relinquish our interests in those operations. Our holding company, the WFOE, the VIE, and investors of our company face uncertainty about potential future actions by the PRC government that could affect the enforceability of the contractual arrangements with the VIE and, consequently, significantly affect the financial performance of the VIE and our company as a whole.

We and the VIE face various legal and operational risks and uncertainties related to doing business in China. Some of our business operations are conducted in China through the VIE, and we and the VIE are subject to complex and evolving PRC laws and regulations. For example, we and the VIE face risks associated with regulatory approvals on offshore offerings, the use of variable interest entities, anti-monopoly regulatory actions, and oversight on cybersecurity and data privacy, as well as the lack of inspection by the Public Company Accounting Oversight Board, or PCAOB, on our auditors, which may impact our ability to conduct certain businesses, accept foreign investments, or list on a U.S. or other foreign exchange. These risks could result in a material adverse change in our operations and the value of the ADSs, significantly limit or completely hinder our ability to offer or continue to offer securities to investors and cause such securities to significantly decline in value. For a detailed description of risks related to doing business in China, "Item 3. Key Information—D. Risk Factors—Risks Relating to Doing Business in China."

PRC government's significant authority in regulating our operations and its oversight and control over offerings conducted overseas by, and foreign investment in, China-based issuers could significantly limit or completely hinder our ability to offer or continue to offer securities to investors. Implementation of industry-wide regulations, including data security or anti-monopoly related regulations, in this nature may cause the value of such securities to significantly decline. For more details, see "Item 3. Key Information—D. Risk Factors—Risks Relating to Doing Business in China—The PRC government's significant oversight over our and the VIE's business operation could result in a material adverse change in our operations and the value of the ADSs."

Risks and uncertainties arising from the legal system in China, including risks and uncertainties regarding the enforcement of laws and quickly evolving rules and regulations in China, could result in a material adverse change in our operations and the value of the ADSs. For more details, see “Item 3. Key Information—D. Risk Factors—Risks Relating to Doing Business in China—Uncertainties in the interpretation and enforcement of PRC laws and regulations could limit the legal protections available to you and us.”

The Holding Foreign Companies Accountable Act

Pursuant to the Holding Foreign Companies Accountable Act, or the HFCAA, if the U.S. Securities and Exchange Commission, or the SEC, determines that we have filed audit reports issued by a registered public accounting firm that has not been subject to inspections by the PCAOB for two consecutive years, the SEC will prohibit our shares or the ADSs from being traded on a national securities exchange or in the over-the-counter trading market in the United States. On December 16, 2021, the PCAOB issued a report to notify the SEC of its determination that the PCAOB was unable to inspect or investigate completely registered public accounting firms headquartered in mainland China and Hong Kong, including our auditor. On May 26, 2022, the SEC conclusively listed us as a Commission-Identified Issuer under the HFCAA following the filing of the annual report on Form 20-F for the fiscal year ended December 31, 2021. On December 15, 2022, the PCAOB vacated its December 16, 2021 determination and removed mainland China and Hong Kong from the list of jurisdictions where it is unable to inspect or investigate completely registered public accounting firms. For this reason, we do not expect to be identified as a Commission-Identified Issuer under the HFCAA after we file this annual report on Form 20-F. Each year, the PCAOB will determine whether it can inspect and investigate completely audit firms in mainland China and Hong Kong, among other jurisdictions. If PCAOB determines in the future that it no longer has full access to complete inspection and investigation over accounting firms in mainland China and Hong Kong and we continue to use an accounting firm headquartered in one of these jurisdictions to issue an audit report on our financial statements filed with the SEC, we would be identified as a Commission-Identified Issuer following the filing of the annual report on Form 20-F for the relevant fiscal year. There can be no assurance that we would not be identified as a Commission-Identified Issuer for any future fiscal year, and if we were so identified for two consecutive years, we would become subject to the prohibition on trading under the HFCAA. See “Item 3. Key Information—D. Risk Factors—Risks Relating to Doing Business in China—The ADSs will be delisted and prohibited from trading in the U.S. under the Holding Foreign Companies Accountable Act, or the HFCAA, if the PCAOB is unable to inspect or fully investigate auditors located in China.”

Permissions Required from the PRC Authorities for Our Operations

The VIE and the VIE's subsidiaries currently conduct operations in the PRC and we consolidate the financial results of such operations under U.S. GAAP as a result of the contractual arrangements. Our operations in China are governed by PRC laws and regulations. As of the date of this annual report, our PRC subsidiaries, the VIE and the VIE's subsidiaries have obtained the requisite licenses and permits from the PRC government authorities that are material for the business operations of our subsidiaries and the VIE in China, including, among others, General Aviation Enterprise Operation Licenses required for using UAVs in aerial spraying, aerial photography, operator training, flight show, aerial media solutions and other purposes. Given the uncertainties of interpretation and implementation of relevant laws and regulations and the enforcement practice by relevant government authorities, we may be required to obtain additional licenses, permits, filings or approvals for our business operations in the future. See “Item 3. Key Information—D. Risk Factors—Risks Relating to Doing Business in China—Uncertainties exist with respect to the interpretation and implementation of the PRC Foreign Investment Law and its Implementation Regulations and how they may impact the viability of our current corporate structure, corporate governance and business operations” and “Item 3. Key Information—D. Risk Factors—Risks Relating to Doing Business in China—We may be adversely affected by the complexities, uncertainties and changes in PRC regulations on technology companies.”

Furthermore, in connection with our previous issuance of securities to foreign investors, under current PRC laws, regulations and regulatory rules, as of the date of this annual report, we, our PRC subsidiaries and the VIE, (i) are not required to obtain permissions from the China Securities Regulatory Commission, or the CSRC, for our listing, (ii) are not required to go through cybersecurity review by the Cyberspace Administration of China, or the CAC, and (iii) have not been asked to obtain such permissions by any PRC authority.

Cash and Asset Flows through Our Organization

Our offshore holding company is permitted under PRC laws and regulations to provide funding to our PRC subsidiary only through loans or capital contributions, subject to the approval of government authorities and limits on the amount of capital contributions and loans.

For the years ended December 31, 2020, 2021 and 2022, EHang Holdings made capital contributions of RMB66.6 million, RMB190.0 million and RMB58.9 million (US\$8.5 million), respectively, to its subsidiaries. No other transfers, dividends or distributions of cash or assets were made between EHang Holdings and EHang Holdings' subsidiaries, on the one hand, and the VIE and the VIE's subsidiaries, on the other hand, except for the foregoing capital contributions.

EHang Holdings is a Cayman Islands holding company with no material operations of its own. The VIE and the VIE's subsidiaries currently conduct operations in the PRC and we consolidate the financial results of such operations under U.S. GAAP as a result of the contractual arrangements. As a result, although other means are available for us to obtain financing at the holding company level, EHang Holdings' ability to pay dividends and to service any debt it may incur may depend upon dividends paid by its subsidiaries. Among them, our Hong Kong subsidiary Ehfly Technology's source of dividend depends on dividends paid by its PRC subsidiaries, which in part depends on payments from the VIE under the contractual arrangements with the VIE.

Current PRC regulations permit our PRC subsidiaries, such as the WFOE, to pay dividends to us only out of their accumulated profits, if any, determined in accordance with PRC accounting standards and regulations. In addition, the VIE and the WFOE are required to set aside at least 10% of their respective accumulated profits each year, if any, to fund certain reserve funds until the total amount set aside reaches 50% of their respective registered capital. The WFOE and the VIE may also allocate a portion of their after-tax profits based on PRC accounting standards to employee welfare and bonus funds at their discretion. These reserves are not distributable as cash dividends. Furthermore, if the WFOE incurs debt on its own behalf in the future, the instruments governing the debt may restrict its ability to pay dividends or make other payments to us. In addition, the PRC tax authorities may require us to adjust our taxable income under the contractual arrangements we currently have in place in a manner that would materially and adversely affect the WFOE's ability to pay dividends and other distributions to us. Any limitation on the ability of our subsidiary to distribute dividends to us or on the ability of the VIE to make payments to the WFOE may restrict our ability to satisfy our liquidity requirements. See "Item 4. Information on the Company—B. Business Overview—PRC Regulation—Dividend Distribution."

Additionally, the VIE receives substantially all of its revenues in RMB and the PRC government imposes controls on the convertibility of the RMB into foreign currencies and, in certain cases, the remittance of currency out of China. Under existing PRC foreign exchange regulations, payments of current account items, such as profit distributions and trade and service-related foreign exchange transactions, can be made in foreign currencies without prior approval from the State Administration of Foreign Exchange of the PRC, or the SAFE by complying with certain procedural requirements. Dividends payments to us by Ehfly Technology, our Hong Kong subsidiary, in foreign currencies are subject to the condition that the remittance of such dividends outside of the PRC complies with certain procedures under PRC foreign exchange regulations, such as the overseas investment registrations by our shareholders or the ultimate shareholders of our corporate shareholders who are PRC residents. Approval by or registration with appropriate government authorities is required where RMB is to be converted into foreign currency and remitted out of China to pay capital expenses such as the repayment of loans denominated in foreign currencies. The PRC government may also at its discretion restrict access in the future to foreign currencies for current account transactions. If the foreign exchange control system prevents us from obtaining sufficient foreign currencies to satisfy our foreign currency demands, the WFOE may not be able to pay dividends in foreign currencies to us and our access to cash generated from its operations will be restricted. See "Item 3. Key Information—D. Risk Factors—Risks Relating to Doing Business in China—Governmental control of currency conversion may limit our ability to utilize our operating revenues effectively and affect the value of your investment."

None of our subsidiaries has declared or paid any dividend or distribution to us. We have never declared or paid any dividend on our ordinary shares. We currently intend to retain most, if not all, of our available funds and any future earnings to fund the development and growth of our business. As a result, we do not expect to pay any cash dividends in the foreseeable future. See “Item 8. Financial Information—A. Consolidated Statements and Other Financial Information—Dividend Policy.” For the Cayman Islands, PRC and U.S. federal income tax considerations applicable to an investment in the ADSs or Class A ordinary shares, see “Item 10. Additional Information—E. Taxation.”

Under the current laws of the Cayman Islands, EHang Holdings is not subject to tax on income or capital gains. Upon payments of dividends to our shareholders, no Cayman Islands withholding tax will be imposed. For purposes of illustration, the following discussion reflects the hypothetical taxes that might be required to be paid in Mainland China and Hong Kong, assuming that: (i) the VIE has taxable earnings, and (ii) we determine to pay a dividend in the future.

	Tax Calculation ⁽¹⁾
Hypothetical pre-tax earnings in the VIE ⁽¹⁾	100
Tax on earnings at statutory rate of 25% at WFOE level ⁽²⁾	(25)
Amount to be distributed as dividend from WFOE to Ehfly Technology ⁽³⁾	75
Withholding tax at a treaty rate of 5%	(3.75)
Amount to be distributed as dividend at Ehfly Technology level and net distribution to EHang Holdings ⁽⁴⁾	71.25

Notes:

- (1) For purposes of this example, the tax calculation has been simplified. The hypothetical book pre-tax earnings amount is assumed to equal Chinese taxable income.
- (2) Certain of our subsidiaries and the VIE qualifies for a 15% preferential income tax rate in China. However, such rate is subject to qualification, is temporary in nature, and may not be available in a future period when distributions are paid. For purposes of this hypothetical example, the table above reflects a maximum tax scenario under which the full statutory rate would be effective.
- (3) China's Enterprise Income Tax Law imposes a withholding income tax of 10% on dividends distributed by a Foreign Invested Enterprise to its immediate holding company outside of Mainland China. A lower withholding income tax rate of 5% is applied if the Foreign Invested Enterprise's immediate holding company is registered in Hong Kong or other jurisdictions that have a tax treaty arrangement with Mainland China, subject to a qualification review at the time of the distribution. There is no incremental tax at Ehfly Technology level for any dividend distribution to EHang Holdings.
- (4) If a 10% withholding income tax rate is imposed, the withholding tax will be 7.5 and the amount to be distributed as dividend at Ehfly Technology level and net distribution to EHang Holdings will be 67.5.

The table above has been prepared under the assumption that all profits of the VIE will be distributed as fees to our PRC subsidiaries under tax neutral contractual arrangements. If, in the future, the accumulated earnings of the VIE exceed the service fees paid to our PRC subsidiaries (or if the current and contemplated fee structure between the intercompany entities is determined to be non-substantive and disallowed by Chinese tax authorities), the VIE could make a non-deductible transfer to our PRC subsidiaries for the amounts of the stranded cash in the VIE. This would result in such transfer being non-deductible expenses for the VIE but still taxable income for the PRC subsidiaries. Our management believes that there is only a remote possibility that this scenario would happen.

Should all tax planning strategies fail the VIE could, as a matter of last resort, make a non-deductible transfer to the WFOE for amounts of stranded cash in the VIE. This would result in the double taxation of earnings: once at the VIE level (non-deductible expense) and again at the WFOE level (for presumptive earnings on the transfer). This has the impact of reducing the amount available above from 71.25% to approximately 53% of pre-tax income, respectively. Management believes this scenario to be remote.

Financial Information Relating to the VIE

The following tables present the condensed consolidating schedule showing the results of operations, financial position and cash flows for our holding company, EHang Holdings, EHang Holdings' subsidiaries other than the WFOE, the WFOE, the VIE and the VIE's subsidiaries, eliminating adjustments and consolidated totals as of December 31, 2021 and 2022 and for the years ended December 31, 2020, 2021 and 2022.

Selected Condensed Consolidated Statements of Operations Data

	For the year ended December 31,																	
	2020						2021						2022					
	EHang Holdings	Other subsidiaries	WFOE	VIE and VIE's subsidiaries	Eliminating adjustments	Consolidated totals	EHang Holdings	Other subsidiaries	WFOE	VIE and VIE's subsidiaries	Eliminating adjustments	Consolidated totals	EHang Holdings	Other subsidiaries	WFOE	VIE and VIE's subsidiaries	Eliminating adjustments	Consolidated totals
	(RMB in thousands)																	
Revenues	—	64	146,905	68,372	(35,248)	180,093	—	2,199	57,550	28,399	(31,341)	56,807	—	3,175	44,098	10,147	(13,103)	44,317
- Third-party revenues	—	64	144,749	35,280	—	180,093	—	2,199	54,378	230	—	56,807	—	2,595	41,716	6	—	44,317
- Inter-company revenues ⁽¹⁾	—	—	2,156	33,092	(35,248)	—	—	—	3,172	28,169	(31,341)	—	—	580	2,382	10,141	(13,103)	—
Costs of revenues	—	—	(99,530)	(10,239)	35,855	(73,914)	—	(1,616)	(49,098)	(720)	30,657	(20,777)	—	(1,496)	(24,655)	(836)	11,889	(15,098)
- Third-party cost of revenues	—	—	(66,438)	(7,476)	—	(73,914)	—	(48)	(20,069)	(660)	—	(20,777)	—	—	(14,516)	(582)	—	(15,098)
- Inter-company cost of revenues ⁽¹⁾	—	—	(33,092)	(2,763)	35,855	—	—	(1,568)	(29,029)	(60)	30,657	—	—	(1,496)	(10,319)	(254)	11,889	—
Gross profit	—	64	47,375	58,133	607	106,179	—	583	8,452	27,679	(684)	36,030	—	1,679	19,443	9,311	(1,214)	29,219
Sales and marketing expenses	—	(4,419)	(24,072)	(8,695)	—	(37,186)	—	(6,859)	(29,848)	(7,105)	583	(43,229)	—	(8,009)	(37,908)	(8,309)	1,110	(53,116)
General and administrative expenses	(1,144)	(3,537)	(44,442)	(12,490)	—	(61,613)	(5,668)	(1,383)	(166,531)	(13,889)	83	(187,388)	(13,630)	(1,554)	(116,451)	(19,380)	(50)	(151,065)
Research and development expenses	—	—	(91,967)	(13,337)	52	(105,252)	—	—	(115,141)	(22,123)	116	(137,148)	—	—	(114,692)	(20,428)	38	(135,082)
Total operating expenses	(1,144)	(7,956)	(160,481)	(34,522)	52	(204,051)	(5,668)	(8,242)	(311,520)	(43,117)	782	(367,765)	(13,630)	(9,563)	(269,051)	(48,117)	1,098	(339,263)
Other operating income	—	466	3,125	2,985	—	6,576	—	1,696	4,544	4,959	—	11,199	—	409	4,150	1,535	—	6,094
Operating loss	(1,144)	(7,426)	(109,981)	26,596	659	(91,296)	(5,668)	(5,963)	(298,524)	(10,479)	98	(320,536)	(13,630)	(7,475)	(245,458)	(37,271)	(116)	(303,950)
Share of losses from subsidiaries ⁽²⁾	(117,678)	(111,170)	—	—	229,378	—	(299,575)	(298,012)	—	—	597,587	—	(253,575)	(251,156)	—	—	504,731	—
Income (losses) from the VIEs ⁽²⁾	30,740	30,740	30,740	—	(92,220)	—	(8,730)	(8,730)	(8,730)	—	26,190	—	(37,603)	(37,603)	(37,603)	—	112,809	—
Interest and investment income	463	1,741	1,468	123	—	3,795	14	3,965	891	273	—	5,143	1	3,971	639	58	—	4,669
Interest expenses	—	—	(2,131)	(206)	—	(2,337)	—	—	(1,445)	(358)	—	(1,803)	—	—	(3,462)	(357)	—	(3,819)
Foreign exchange gain (loss)	—	144	(107)	(370)	—	(333)	—	(450)	(253)	(124)	—	(827)	—	(494)	(1,474)	480	—	(1,488)
Other income	—	820	318	89	—	1,227	—	742	2,735	2,610	(1)	6,086	—	1,182	393	369	—	1,944
Other expenses	—	(1,350)	(1,270)	(507)	—	(3,127)	—	(6)	(1,340)	(343)	140	(1,549)	(23,414)	—	(2,082)	(1,308)	—	(26,804)
Loss before income tax and income (loss) from equity method investment	(87,619)	(87,031)	(80,963)	25,725	137,817	(92,071)	(313,959)	(308,454)	(306,666)	(8,421)	624,014	(313,486)	(328,221)	(291,575)	(289,047)	(38,029)	617,424	(329,448)
Income tax expenses	—	—	—	(206)	—	(206)	—	(21)	—	(113)	—	(134)	—	(17)	—	(62)	—	(79)
Loss before income (loss) from equity method investment	(87,619)	(87,031)	(80,963)	25,519	137,817	(92,277)	(313,959)	(308,475)	(306,666)	(8,534)	624,014	(313,620)	(328,221)	(291,592)	(289,047)	(38,091)	617,424	(329,527)
Income (loss) from equity method investments	—	—	—	236	—	236	—	—	(276)	—	—	(276)	—	—	196	—	—	196
Net (loss) income	(87,619)	(87,031)	(80,963)	25,755	137,817	(92,041)	(313,959)	(308,475)	(306,942)	(8,534)	624,014	(313,896)	(328,221)	(291,592)	(288,851)	(38,091)	617,424	(329,331)
Net income (loss) attributable to non-controlling interest	—	93	3	4,326	—	4,422	—	170	135	(368)	—	(63)	—	414	218	478	—	1,110
Net loss attributable to ordinary shareholders	(87,619)	(86,938)	(80,960)	30,081	137,817	(87,619)	(313,959)	(308,305)	(306,807)	(8,902)	624,014	(313,959)	(328,221)	(291,178)	(288,633)	(37,613)	617,424	(326,221)

Selected Condensed Consolidated Balance Sheets Data

	As of December 31,											
	EHang Holdings	Other subsidiaries	WFOE	2021 VIE and VIE's subsidiaries	Eliminating adjustments	Consolidated totals	EHang Holdings	Other subsidiaries	WFOE	2022 VIE and VIE's subsidiaries	Eliminating adjustments	Consolidated totals
	(RMB in thousands)											
Cash and cash equivalents	72,998	137,200	28,651	8,014	—	246,863	362	52,226	185,318	11,404	—	249,310
Restricted cash	—	—	160	—	—	160	—	—	—	—	—	—
Short-term investments	—	65,108	—	—	—	65,108	—	—	—	—	—	—
Accounts receivable, net	—	66	45,164	10,959	—	56,189	—	105	19,991	202	—	20,298
Inventories	—	1,729	76,836	839	(1,329)	78,075	—	1,915	71,067	837	(1,455)	72,364
Prepayments and other current assets	—	1,529	23,564	4,302	—	29,395	—	2,268	39,262	3,653	—	45,183
Amount due from a related party	—	—	1,360	—	—	1,360	—	—	—	—	—	—
Amounts due from subsidiaries, the VIE and the VIE's subsidiaries ⁽³⁾	—	98,375	10,550	25,774	(134,699)	—	13,697	67,980	28,770	6,911	(117,358)	—
Property and equipment, net and intangible assets, net	—	350	32,158	2,109	(51)	34,566	—	219	45,609	1,273	(41)	47,060
Right-of-use assets, net	—	—	—	—	—	—	—	36	72,647	799	—	73,482
Investment in subsidiaries ⁽²⁾	290,462	1,943	—	—	(292,405)	—	213,579	111,169	—	—	(324,748)	—
Others	—	4,784	18,837	97	—	23,718	—	4,899	18,003	268	—	23,170
Total assets	363,460	311,084	237,280	52,094	(428,484)	535,434	227,638	240,817	480,667	25,347	(443,602)	530,867
Short-term bank loans	—	—	10,000	—	—	10,000	—	—	49,794	—	—	49,794
Short-term debt	—	—	—	—	—	—	—	—	57,838	—	—	57,838
Amounts due to the Company, subsidiaries, the VIE and the VIE's subsidiaries ⁽³⁾	—	10,419	78,289	45,991	(134,699)	—	11,230	12,941	37,736	55,451	(117,358)	—
Accounts payables	—	—	42,535	3,025	—	45,560	—	—	32,356	3,100	—	35,456

	As of December 31,											
	EHang Holdings	Other subsidiaries	WFOE	2021 VIE and VIE's subsidiaries	Eliminating adjustments	Consolidated totals	EHang Holdings	Other subsidiaries	WFOE	2022 VIE and VIE's subsidiaries	Eliminating adjustments	Consolidated totals
	(RMB in thousands)											
Accrued expenses and other liabilities	3,744	1,040	39,014	18,053	—	61,851	27,432	3,223	47,396	19,712	—	97,763
Contract liabilities	—	906	12,248	1,677	—	14,831	—	—	17,294	2,027	—	19,321
Long-term loans	—	—	8,000	9,000	—	17,000	—	—	—	3,846	—	3,846
Lease liabilities	—	—	—	—	—	—	—	36	74,597	800	—	75,433
Net interest of the VIEs ⁽²⁾	27,115	27,115	27,115	—	(81,345)	—	64,718	64,718	64,718	—	(194,154)	—
Others	—	8,498	42,060	1,588	—	52,146	—	11,607	49,389	5,742	—	66,738
Total liabilities	30,859	47,978	259,261	79,334	(216,044)	201,388	103,380	92,525	431,118	90,678	(311,512)	406,189
Total shareholders' equity (deficit)⁽²⁾	332,601	263,106	(21,981)	(27,240)	(212,440)	334,046	124,258	148,292	49,549	(65,331)	(132,090)	124,678

Selected Condensed Consolidated Cash Flows Data

	For the year ended December 31,																
	2020					2021					2022						
	EHang Holdings	Other subsidiaries	WFOE	VIE and VIE's subsidiaries	Eliminating adjustments	Consolidated totals	EHang Holdings	Other subsidiaries	WFOE	VIE and VIE's subsidiaries	Eliminating adjustments	Consolidated totals	EHang Holdings	Other subsidiaries	WFOE	VIE and VIE's subsidiaries	Eliminating adjustments
	(RMB in thousands)																
Net cash (used in) provided by operating activities ⁽⁴⁾	(681)	2,331	(148,228)	(5,118)	—	(151,696)	(4,874)	(5,792)	(107,481)	(3,482)	—	(121,629)	(13,738)	(24,239)	(140,108)	4,627	—
Cash flows from investing activities																	
Capital contribution	(66,599)	(90,000)	—	—	156,599	—	(190,026)	(109,000)	—	—	299,026	—	(58,898)	(208,484)	—	—	267,3
Proceeds from maturities of short-term investments	—	18,596	32,200	21,200	—	71,996	—	—	—	—	—	—	—	141,388	—	10,000	—
Purchase of short-term investments	—	(61,964)	(32,200)	(21,200)	—	(115,364)	—	—	—	—	—	—	—	(66,807)	—	(10,000)	—
Loans to third parties	—	(1,900)	(52,000)	—	—	(53,900)	—	—	—	—	—	—	—	—	—	—	—
Repayment of loan to a third party	—	—	40,000	—	—	40,000	—	—	—	—	—	—	—	—	—	—	—
Other investing activities	(484)	(1,538)	(6,812)	(107)	—	(8,941)	150	(17,062)	(15,611)	(878)	—	(33,401)	—	1,580	(19,524)	(237)	—
Net cash (used in) provided by investing activities	(67,083)	(136,806)	(18,812)	(107)	156,599	(66,209)	(189,876)	(126,062)	(15,611)	(878)	299,026	(33,401)	(58,898)	(132,323)	(19,524)	(237)	267,3
Cash flows from financing activities																	
Capital contribution	—	66,599	90,000	—	(156,599)	—	—	190,026	109,000	—	(299,026)	—	—	58,898	208,484	—	(267,3
Proceeds from mandatorily redeemable non-controlling interests of a subsidiary	—	—	40,000	—	—	40,000	—	—	—	—	—	—	—	—	—	—	—
Proceeds from short-term bank loans	—	—	15,000	—	—	15,000	—	—	—	—	—	—	—	—	49,794	—	—
Repayment of a short-term bank loan	—	—	(5,000)	—	—	(5,000)	—	—	—	—	—	—	—	—	(9,000)	(1,000)	—
Other financing activities	(7,343)	—	23	—	—	(7,320)	256,947	—	5,000	5,000	—	266,947	—	85	66,861	—	—

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	For the year ended December 31,																
	2020					2021					2022						
	EHang Holdings	Other subsidiaries	WFOE	VIE and subsidiaries	Eliminating adjustments	Consolidated totals	EHang Holdings	Other subsidiaries	WFOE	VIE and subsidiaries	Eliminating adjustments	Consolidated totals	EHang Holdings	Other subsidiaries	WFOE	VIE and subsidiaries	Eliminating adjustments
	(RMB in thousands)																
Net cash (used in) provided by financing activities	(7,343)	66,599	140,023	—	(156,599)	42,680	256,947	190,026	114,000	5,000	(299,026)	266,947	—	58,983	316,139	(1,000)	(267,382)
Effect of exchange rates on cash, cash equivalents and restricted cash ⁽⁵⁾	—	(6,264)	—	—	—	(6,264)	—	(5,067)	—	—	—	(5,067)	—	12,605	—	—	—
Net (decrease) increase in cash, cash equivalents and restricted cash	(75,107)	(74,140)	(27,017)	(5,225)	—	(181,489)	62,197	53,105	(9,092)	640	—	106,850	(72,636)	(84,974)	156,507	3,390	—
Cash, cash equivalents and restricted cash at the beginning of the year	85,908	158,235	64,920	12,599	—	321,662	10,801	84,095	37,903	7,374	—	140,173	72,998	137,200	28,811	8,014	—
Cash, cash equivalents and restricted cash at the end of the year	10,801	84,095	37,903	7,374	—	140,173	72,998	137,200	28,811	8,014	—	247,023	362	52,226	185,318	11,404	—

Notes:

- (1) Represents the elimination of the intercompany transactions at the consolidation level.
- (2) Represents the elimination of the investment among the EHang Holdings, EHang Holdings' subsidiaries other than the WFOE, WFOE, and the VIE and the VIE's subsidiaries.
- (3) Represents the elimination of intercompany balances among the EHang Holdings, EHang Holdings' subsidiaries other than the WFOE, WFOE, and the VIE and the VIE's subsidiaries.
- (4) For the years ended December 31, 2020, 2021 and 2022, the WFOE did not charge any service fee from the VIE as the VIE was in cumulative loss position.

For the years ended December 31, 2020, 2021 and 2022, cash paid by WFOE to VIE and VIE's subsidiaries were RMB14.8 million, RMB3.2 million and RMB45.5 million, respectively, which represented purchase of software and inventories.

For the years ended December 31, 2020, 2021 and 2022, cash paid by WFOE to other subsidiaries were nil, nil, and RMB0.6 million, respectively, which represented purchase of inventories.

For the years ended December 31, 2020, 2021 and 2022, cash paid by other subsidiaries to WFOE were nil, nil, and nil, respectively, which represented purchase of inventories.

A. Reserved

B. Capitalization and Indebtedness

Not applicable.

C. Reasons for the Offer and Use of Proceeds

Not applicable.

D. Risk Factors

Below please find a summary of the principal risks we face, organized under relevant headings.

Risks Relating to Our Business and Industry

- Our future growth depends on the demand for, and customers' willingness to adopt, our AAVs and air mobility solutions.
- In the jurisdictions where we, the VIE and the VIE's subsidiaries sell and plan to sell products, the commercial use of AAVs is subject to an uncertain or lengthy approval process; we cannot predict when regulations will change, and any new regulations may impose onerous requirements and restrictions with which we, the VIE and the VIE's subsidiaries, the AAVs and potential customers may be unable to comply. As a result, we, the VIE and the VIE's subsidiaries may be limited in, or completely restricted from, growing business in the foreseeable future.
- We may be unable to make timely product deliveries due to limited production capacity.
- Our framework and conditional agreements may not result in material sales of our products.
- We have substantial customer concentration and we have experienced a significant increase in accounts receivable.
- Our technology platform may not perform in line with customer specifications or expectations; and
- We are a relatively young company with a short operating history, and we may not be able to sustain our rapid growth, effectively manage our growth or implement our business strategies.

Risks Relating to Our Corporate Structure

- If the PRC government finds that the contractual arrangements between the WFOE, the VIE and the VIE's shareholders do not comply with PRC regulations relating to the relevant industries, or if these regulations or the interpretation of existing regulations change in the future, we could be subject to severe penalties or be forced to relinquish our interests in those operations.
- We rely on contractual arrangements with the VIE and the VIE's shareholders for certain business operations in the PRC, which may not be as effective as direct ownership in providing operational control.
- Any failure by the VIE or the VIE's shareholders to perform their obligations under our contractual arrangements with them would have a material and adverse effect on our business.
- The shareholders of the VIE may have potential conflicts of interest with us, which may materially and adversely affect our business and financial condition.

- We may lose the ability to use and enjoy assets held by the VIE that are material to certain business operations in the PRC if the VIE goes bankrupt or becomes subject to a dissolution or liquidation proceeding.
- Our dual-class share structure with different voting rights will limit your ability to influence corporate matters and could discourage others from pursuing any change of control transactions that holders of our Class A ordinary shares and ADSs may view as beneficial.

Risks Relating to Doing Business in China

- Changes in China's economic, political or social conditions or government policies could have a material adverse effect on our business, financial condition and results of operation.
- Uncertainties in the interpretation and enforcement of PRC laws and regulations could limit the legal protections available to you and us.
- We may be adversely affected by the complexities, uncertainties and changes in PRC regulations on technology companies.
- The approval of and the filing with the CSRC or other PRC governmental authorities may be required in connection with our future offshore offerings under PRC law and if required, we cannot predict whether or how soon we will be able to obtain such approval or complete such filing.
- The ADSs will be delisted and prohibited from trading in the U.S. under the Holding Foreign Companies Accountable Act, or the HFCAA, if the PCAOB is unable to inspect or fully investigate auditors located in China.
- Increases in labor costs and enforcement of stricter labor laws and regulations in the PRC may adversely affect our business and our profitability.
- We rely on dividends and other distributions on equity paid by our PRC subsidiaries to fund any cash and financing requirements we may have, and any limitation on the ability of our PRC subsidiaries to make payments to us could have a material adverse effect on our ability to conduct our business.
- The PCAOB had historically been unable to inspect our auditor in relation to their audit work performed for our financial statements and the inability of the PCAOB to conduct inspections of our auditor in the past has deprived our investors with the benefits of such inspections.

Risks Relating to the ADSs and Trading Market

- The trading price of the ADSs is likely to be volatile, which could result in substantial losses to investors.
- If securities or industry analysts do not publish research or reports about our business, or if they adversely change their recommendations regarding the ADSs, the market price for the ADSs and trading volume could decline.
- The sale or availability for sale of substantial amounts of the ADSs could adversely affect their market price.
- We are a "controlled company" within the meaning of the Nasdaq Stock Market Rules and, as a result, may rely on exemptions from certain corporate governance requirements that provide protection to shareholders of other companies.

Risks Relating to Our Business and Industry

Our future growth depends on the demand for, and customers' willingness to adopt, our AAVs and air mobility solutions.

We operate in the new and evolving AAV industry. Our business and operating results depend in large part on the acceptance of and demand for our AAVs and air mobility solutions. The success of these products and services are and will be subject to risks, including with respect to:

- the extent of market reception and adoption of AAVs as transportation and logistics solutions;
- our navigating a new and evolving regulatory environment;
- our timely fulfillment of product orders;
- our ability to produce safe, high-quality and cost-effective AAVs on an ongoing basis;
- the performance of our AAVs relative to customer expectations and customers' interest in and demand for our AAVs and air mobility solutions; and
- our building a well-recognized and respected brand.

Our failure to manage the risks described above may discourage current or potential customers from purchasing our AAVs or using our AAV commercial solutions, and there may be downward price pressure on our AAVs and commercial solutions. If the market for AAVs or air mobility solutions does not develop as we expect or develops more slowly than we expect, our business, prospects, financial condition and operating results will be materially and adversely affected.

In the jurisdictions where we, the VIE and the VIE's subsidiaries sell and plan to sell products, the commercial use of AAVs is subject to an uncertain or lengthy approval process; we cannot predict when regulations will change, and any new regulations may impose onerous requirements and restrictions with which we, the VIE and the VIE's subsidiaries, the AAVs and potential customers may be unable to comply. As a result, we, the VIE and the VIE's subsidiaries may be limited in, or completely restricted from, growing business in the foreseeable future.

We operate in a new and rapidly evolving industry, which is subject to extensive legal and regulatory requirements. As described below, in the jurisdictions relevant to us, the commercial use and delivery of our AAVs are, and in the near future are expected to continue to be, subject to an uncertain or lengthy approval process. Without obtaining all applicable regulatory approvals, our AAVs are currently mainly operated on a limited trial basis by our customers in tourism locations in China and are not in broad, mainstream commercial operations. We are unable to estimate the average length of time required to obtain the applicable regulatory approvals due to the nascent nature of AAV-related regulations and the lack of relevant precedents. For example, we are not aware of any operator having been granted all required approvals for the commercial operations of passenger-carrying AAVs in China, the United States or elsewhere. In addition, PRC and U.S. regulations impose significant restrictions on our non-passenger-carrying AAVs. We cannot predict when these regulations will change, and any new regulations may impose onerous requirements and restrictions.

In China, the Civil Aviation Administration of China, or CAAC, published the Guidance on UAV Airworthiness Assessment Based on Operation Risks, or the UAV Airworthiness Guidance, on January 25, 2019, which is based on the assessment, classification and management of operational risks of UAVs. On May 26, 2020, the Department of Aircraft Airworthiness Certification of the CAAC issued the Administrative Procedures for Airworthiness Assessment of Civil Unmanned Aerial Vehicle Systems (Trial), or the Airworthiness Assessment Procedures, effective on June 1, 2020, with a one-year trial period. According to the Airworthiness Assessment Procedures, enterprises shall apply for the approval letter of design and manufacture from the CAAC if they plan to design and manufacture civil unmanned aerial vehicle systems. The holder of an approval letter of design and manufacture shall set up an airworthiness examination agency, which shall, in accordance with the Administrative Procedures for the Real-name Registration of Civil UAVs (Draft), complete the pre-registration of the civil unmanned aerial vehicle systems it manufactures and, at the time of a customer's completing the real-name registration and applying for airworthiness approval, conduct verification and inspection and give suggestion to the CAAC as to whether or not to issue the airworthiness approval. The airworthiness approval for a private UAV system shall be completed simultaneously with the real-name registration. We may be required to comply with these regulatory requirements and to obtain relevant licenses, permits, registrations or certificates under such regulatory requirements. However, since the Airworthiness Assessment Procedures is newly enacted, uncertainties still exist in relation to its interpretation and implementation, and there is no detailed rule regarding when and how we should apply for the relevant approvals mentioned therein. Additional rules and regulations with respect to the airworthiness of AAVs are still under discussion by the CAAC. We are making contributions as a member of the CAAC Special Expert Taskforce. On October 29, 2021, the CAAC further published the Civil Unmanned Aircraft System Airworthiness Certification Management Procedures (Draft for Comments), Civil Unmanned Aircraft System Safety Analysis Guidelines (Draft for Comment), and Civil Unmanned Aircraft Registration Management Procedures (Draft for Comment). Such draft UAV rules mainly cover the medium UAVs weigh between 25 kilograms and 150 kilograms, and large UAVs exceed 150 kilograms in weight. We submitted an application for the EH216-S Type Certification to the CAAC in December 2020, which was accepted by the CAAC in January 2021. Our EH216-S AAVs, as a special category aircraft under Section 21.17 of Certification Procedures for Civil Aviation Products and Parts, or CCAR-21, will be required to meet the criteria set forth in *Special Conditions for Type Certification of EH216-S Unmanned Aircraft System*, or Special Conditions, promulgated by the CAAC on February 9, 2022. The Special Conditions provided clear safety requirements for the certification of EH216-S with respect to flight performance, aircraft structures, design and manufacture, propulsion system, data link, ground control station, etc. Having passed through the Type Certification phases of Concept Design, Requirements Definition, and Compliance Planning, we are in the final phase of Demonstration and Verification of Compliance to conduct tests, including laboratory tests, ground tests and inspections, flight tests and data analysis. As of the date of this annual report, we have completed 75% of the compliance tests of the EH216-S type certification project with the CAAC, which means more than 90% of the entire Type Certification processes have been completed. However, we cannot assure you that we will be able to obtain any of the certificates of design and manufacture or airworthiness as required under the detailed rules and regulations in a timely manner or that we can satisfy the relevant requirements or standards under the detailed rules or regulations to be promulgated in the future, which may materially and adversely affect our business and future prospects.

Under the *Pilot Operation Rules (Interim) for Specific Unmanned Aircraft* issued by the CAAC on February 1, 2019, or Interim Rules, to start any specific trial operation, the prospective operator of certain classes of UAVs must submit an application and be approved by the CAAC. In February 2019, we submitted an application to the CAAC for trial operation in relation to a customer's use of our EH216-S, a model of our passenger-carrying AAVs, for aerial logistics purpose. In May 2020, we obtained the trial operation approval from the CAAC, which expired on May 31, 2021. There can be no assurance that similar approval will be granted to the operations of other customers.

Further, the VIE and the VIE's subsidiaries are required to obtain approvals from local divisions of the People's Liberation Army Air Force, or PLAAF, for proposed flight routes in connection with our business. As the approvals from the PLAAF are usually granted on a one-off basis or are only valid for a limited period of time and the local divisions of PLAAF may exercise air traffic control under certain circumstances which may restrict us from operating our AAVs from time to time, we cannot assure you that the VIE and the VIE's subsidiaries will be able to obtain such approval for each matter on which we will work on with our customers or partners in the future. If such approval is not granted in a timely manner, we, the VIE and the VIE's subsidiaries, as well as our and their customers or partners will not be able to fly the AAVs in the proposed flight routes.

As we sell our AAV products internationally, we face challenges in quickly and sufficiently familiarizing ourselves with foreign regulatory environments and policy frameworks. If any new regulation is put in place, or a different interpretation of existing regulation is adopted, our ability to manufacture, market, sell or operate our AAVs or to advertise or deliver air mobility solutions in general may be limited or otherwise affected. Failure to comply with applicable regulations or to obtain, maintain or renew the necessary permits, licenses, registrations or certificates could cause delays in, or prevent us from, manufacturing, marketing, selling and operating our AAV products, meeting product demand and expectations, introducing new products or expanding our service coverage, and could materially and adversely affect our operation results. If we are found to be in violation of applicable laws or regulations, we could be subject to administrative punishment, including fines, injunctions, recalls or asset seizures, as well as potential criminal sanctions, any of which could have a material adverse effect on our business, financial condition, results of operations and prospects.

We may be unable to make timely product deliveries due to limited production capacity.

As of December 31, 2022, we had unfilled pre-orders for more than 1,200 units of the EH216 series and the VT-30 AAVs. Commercial production of our AAVs requires timely and adequate supply of various types of raw materials and components, as well as mass production capacity and efficient manufacturing and assembly. We have limited experience in high-volume manufacturing of our AAVs. We cannot assure you that we will be able to expand our production capacity efficiently and cost-effectively, or to procure sufficient raw materials and components to meet our production volume. While we are looking into expanding our manufacturing capacity through partnerships, such partnerships may not be successful, or we may not be able to do so in a timely manner to fulfill our backlog orders. While we obtain components from multiple sources whenever possible, some of the components used in our AAVs are currently selected to be purchased from a single source to improve cost-efficiency. Disruption in the supply of components, whether or not from a single-source supplier, could temporarily disrupt commercial production of our AAVs. We also outsource certain manufacturing activities to third party contract manufacturers. We may experience operational difficulties with our contract manufacturers, including reductions in the availability of production capacity, failure to comply with product specifications, insufficient quality control, failure to meet production deadlines, increases in manufacturing costs and longer lead time.

Any of the foregoing could result in our failure to make timely deliveries to our customers. Such failure would materially and adversely affect our business, results of operations, financial condition and prospects.

Our framework and conditional agreements may not result in material sales of our products.

We have entered into a number of long-term agreements with customers and partners relating to the sale of our AAVs. Some of these agreements are conditional, and our counterparty is not obligated to purchase our products unless a number of conditions are satisfied. Under our agreement with a U.S. biotechnology customer, the customer is not required to purchase our AAVs unless our AAVs achieve a number of performance milestones and it obtains required approvals from the Federal Aviation Administration, or the FAA, and the Food and Drug Administration, or the FDA, for the commercial operation of our AAVs. As of December 31, 2022, we had delivered five units of passenger-carrying AAVs to this customer for their trial operations conducted in Canada. We have yet to achieve the performance milestones, and the customers are allowed to terminate the agreements before that happens. Further, it may be time-consuming for the customer to obtain the required approvals, if they are able to do so at all. Some other agreements are framework agreements containing sales targets, but that does not obligate our counterparties to purchase our products at all. We expect the number of orders and pre-orders we receive under these framework agreements to depend on a number of factors, including changes in the regulatory environment, customers' acceptance of and demand for our products and services and our production capacity. For the foregoing reasons, we may not receive substantial orders from our current or potential customers. As our long-term agreements may not result in material sales of our products, our future results of operations may not scale or otherwise meet our current expectations.

We have substantial customer concentration.

In 2020, 2021 and 2022, our largest customer accounted for 51%, 35% and 21% of our revenues, respectively. There are inherent risks whenever a large percentage of revenues are concentrated with a limited number of customers that mainly operate our AAVs in tourism locations in China, rather than in broad, mainstream commercial operations. We are unable to predict the future level of demand for our products and/or services that will be generated by these customers. If our major customers were to cease purchasing our products or services, cancel existing orders or fail to make payments to us in a timely fashion, our business and results of operations will be materially and adversely affected.

Our technology platform may not perform in line with customer specifications or expectations.

Our technology platform, consisting of our AAVs, in-flight operating systems and on-the-ground infrastructure, may not perform in line with customers' expectations. For example, our AAVs may not be as easy to operate or maintain as customers expect. In addition, certain orders and pre-orders of our AAVs are conditioned on their meeting defined technical specifications (such as a specified cruising speed, operational range and payload capacity) according to agreed-upon delivery timetables. See "Item 4. Information on the Company—B. Business Overview—Our Business Lines" for further details. Future customers may also require performance specifications that we are unable to deliver. Some of these target specifications, such as those dependent on battery technology, are constrained by the pace of general technological advancement and the capabilities of our suppliers, which are largely beyond our control.

Our technology platform may contain design or manufacturing defects that result in unsatisfactory performance or require repair. Our technology platform uses a substantial amount of algorithms and software to operate. Software products are inherently complex and often contain defects and errors, especially when first introduced. While we have performed extensive internal testing on our AAV software and hardware systems, we have a limited frame of reference by which to evaluate the long-term performance of our technology platform. There can be no assurance that we will be able to detect and fix any defects in our technology platform before we, the VIE and the VIE's subsidiaries sell products and services to customers.

If our technology platform is defective or otherwise fails to perform as expected or in accordance with prescribed technical specifications and timetable, our AAVs may experience accidents and we may suffer adverse publicity, order cancellations, revenue declines, delivery delays, product recalls, product liability claims, and significant warranty and other expenses. These consequences could have a material adverse impact on our business, financial condition, operating results and prospects.

Our reputation and the trading price of the ADSs may be negatively affected by adverse publicity or detrimental conduct against us.

Adverse publicity concerning our failure or perceived failure to comply with legal and regulatory requirements, alleged accounting or financial reporting irregularities, regulatory scrutiny and further regulatory action or litigation could harm our reputation and cause the trading price of the ADSs to decline and fluctuate significantly. For example, after Wolfpack Research, an entity unrelated to us, issued a report containing various allegations about us in February 2021, the trading price of the ADSs declined sharply. The negative publicity and the resulting decline of the trading price of the ADSs also led to the filing of three putative shareholder class action lawsuits against us and some of our senior executive officers. Though unsuccessful, these lawsuits had further negative impact on the market price of the ADSs and diverted management's attention from the day-to-day operations of our company. See "Item 8. Financial Information—A. Consolidated Statements and Other Financial Information—Legal Proceedings." Our management and audit committee conducted additional procedures and actions to mitigate risks of the short seller allegations. However, we may be constrained in the manner in which we can proceed against the relevant short sellers by principles of freedom of speech, applicable state law or issues of commercial confidentiality.

We may continue to be the target of adverse publicity and detrimental conduct against us, including complaints, anonymous or otherwise, to regulatory agencies regarding our operations, accounting, revenues and regulatory compliance. Additionally, allegations against us may be posted on the internet by any person or entity which identifies itself or on an anonymous basis. We, the VIE and the VIE's subsidiaries may be subject to government or regulatory investigation or inquiries, or shareholder lawsuits, as a result of such third-party conduct and may be required to incur significant time and substantial costs to defend ourselves, and there is no assurance that we, the VIE and the VIE's subsidiaries will be able to conclusively refute each of the allegations within a reasonable period of time or at all. Our reputation may also be negatively affected as a result of the public dissemination of allegations or malicious statements about us, which in turn may materially and adversely affect the trading price of the ADSs.

We are a relatively young company with a short operating history, and we may not be able to sustain our rapid growth, effectively manage our growth or implement our business strategies.

We, the VIE and the VIE's subsidiaries have been providing AAV commercial solutions since 2014. Although we have experienced growth, our historical performance may not be indicative of our future performance due to our limited operating history. We are currently commercializing our AAVs and air mobility solutions, and have a short history of accepting orders for our AAVs and delivering them to customers for testing, training and demonstration purposes. There is only a limited historical basis for making judgments on the demand for our products and services or our ability to produce and deliver AAVs and air mobility solutions, or to become profitable in the future.

You should consider our business and future prospects in light of the risks and challenges we face as a new entrant to a nascent industry and to overseas markets, including risks and challenges associated with our ability to:

- provide safe, convenient and effective air mobility solutions;
- maintain reliable, secure, high-performance and scalable infrastructure;
- identify suitable facilities to expand manufacturing capacity;
- navigate the evolving and complex regulatory environment across all the markets in which we operate;
- anticipate and adapt to changing market conditions, including technological developments and changes in the competitive landscape, and adjust, manage and execute our marketing and sales activities to cater to local economic and demographic conditions, cultural differences and customer preferences across all our current and future markets;
- successfully market our AAV commercial solutions;
- improve and maintain our operational efficiency; and
- attract, retain and motivate talented employees.

If we fail to address any or all of these risks and challenges, our business may be materially and adversely affected.

As our business grows, we, the VIE or the VIE's subsidiaries may adjust our product and service offerings. These adjustments may not bring about expected results and may instead have a material and adverse impact on our financial condition and results of operations. For example, we and the VIE historically manufactured and sold consumer drones while we and the VIE were developing our AAVs and AAV commercial solutions. Our consumer drone business was not successful. We and the VIE gradually phased out this business to focus on more innovative products and services. Our revenue structure may continue to evolve in response to market demand. In particular, we expect the relative revenue contribution from air mobility solutions to increase and that from aerial media solutions to decrease in the foreseeable future. Our growth is dependent on the development of such new products and services. We may not accurately identify market needs before we invest in the development of a new product or a new service. In addition, we might face difficulties or delays in the development process, which may result in losses in our market share and competitive advantages.

In pursuit of our growth strategy, we, the VIE or the VIE's subsidiaries may enter into new strategic relationships to further penetrate our targeted markets. For example, we cooperated with local partners for developing UAM businesses and received pre-orders for our AAVs from partners in Japan, Indonesia, Malaysia, etc. Should these relationships fail to materialize and develop into demand or orders for our products and services, or should we fail to work effectively with these companies, we may lose opportunities to generate sales growth and our business, results of operations and financial condition could be adversely affected.

Our AAVs and AAV commercial solutions are subject to safety standards, and the failure to satisfy such mandated safety standards or failure to design, manufacture and operate safe and high-performance AAVs and related operating systems and infrastructure would have a material adverse effect on our business and operating results.

Sales of our AAVs must comply with applicable standards in the market where they are sold, including standards on design, manufacturing and operation. In China, for example, certain components of our AAVs must pass various tests and undergo a certification process and be affixed with a China Compulsory Certificate, or CCC, before they can be installed on our AAVs. We cannot assure you that we have obtained the CCC for all the components of our AAVs that are listed in the CCC Product Catalogue. Failure to install components with a CCC may prevent us from selling the affected products and negatively affect our manufacturing and sales of AAVs. See "Item 4. Information on the Company—B. Business Overview—PRC Regulation" for further details. In the United States, the FAA oversees the safety of aircraft operations in the national airspace system and has the authority to grant airworthiness certificates and related exemptions to unmanned aircraft systems. If we fail to have our AAVs satisfy applicable aerial vehicle standards in any jurisdiction where we operate, our business and operating results would be adversely affected. To achieve a high level of safety assurance, we have also established our own AAV safety standards. While we are committed to producing safe and high-quality products, there can be no assurance that our safety technology will be effective in preventing incidents related to product safety, such as accidents involving our AAVs. Failure to ensure the safe operation of our AAVs will affect our reputation and the sales of our AAVs, which will ultimately adversely affect our business operation and financial results.

We have incurred, and in the future may continue to incur, net losses.

We have incurred net losses in the past. In 2020, 2021 and 2022, we had net losses of RMB92.0 million, RMB313.9 million and RMB329.3 million (US\$47.7 million), respectively, and we had net operating cash outflows of RMB151.7 million, RMB121.6 million, and RMB173.5 million (US\$25.1 million), respectively, in the same years. We expect our net losses to increase in future periods as we continue to expand our business and operations. See "Item 5. Operating and Financial Review Prospect—B. Liquidity and Capital Resources" for more information on our liquidity and capital resources. We also expect to incur substantial costs and expenses as a result of being a public company.

We cannot assure you that we will be able to generate net profits or positive operating cash flows in the future. Our ability to achieve profitability depends in large part on, among other factors, our ability to increase orders and sales of our AAVs, AAV commercial solutions and services, achieve economies of scale, establish effective pricing strategies, effectively navigate the regulatory environments in different jurisdictions, and increase operational efficiency. If we are unable to generate adequate revenues or effectively manage our expenses, we may continue to incur significant losses in the future and may not be able to achieve or subsequently maintain profitability.

We may not be successful in competing in the UAV industry.

We operate in the UAV industry and provide various commercial solutions, including air mobility (consisting of passenger transportation and logistics), smart city management and aerial media solutions. In addition to competing with other UAV companies, we compete with traditional industry players providing similar solutions, such as aircraft and ground transportation service providers. Many of our current and potential competitors, particularly international competitors, have significantly greater financial, technical, manufacturing, marketing and other resources than we do and may be able to devote greater resources to the design, development, manufacturing, distribution, promotion, sale and support of their products.

We expect competition in our industry to intensify in the future in light of increased demand for alternative transportation, continuing globalization and consolidation in the global UAV industry. Factors affecting competition include, among others, ability to innovate, development speed, product quality, reliability, safety and features, pricing and customer service. Increased competition may lead to lower AAV unit sales and increased inventory, which may result in downward price pressure and adversely affect our business, financial condition, operating results and prospects.

Our ability to successfully compete in our industry will be fundamental to our future success in existing and new markets and will affect our market share. If our competitors introduce AAVs or services that are superior in quality or performance and/or lower in price compared with our offerings, we may lose existing customers or be unable to attract new customers at prices that would allow us to generate attractive rates of return on our investment, if at all.

Any significant cybersecurity incident or disruption to our operating systems or our command-and-control centers could subject us to significant reputational, financial, legal and operational consequences.

We depend on our and the VIE's integrated in-flight operating systems and on-the-ground infrastructure to operate our products and services. Any material disruption to or slowdown of our operating systems or infrastructure could cause our AAVs to malfunction or result in outages or delays in our services, which could harm our brand and adversely affect our operating results.

Our command-and-control centers rely on our proprietary cloud database, which can store all of the data collected under our clients' approvals. Problems with our command-and-control centers or our telecommunications network providers could adversely affect our services and products. Our telecommunications network providers could decide to cease providing services to us without adequate notice. Any change in service levels of our telecommunications network or any errors, defects, disruptions or other performance problems with our operating systems or infrastructure could harm our brand and potentially affect our user data. If changes in technology cause our operating systems or infrastructure to become obsolete, or if our operating systems or command-and-control centers are inadequate to support our growth, we could lose customers, and our business and operating results could be adversely affected.

We could be subject to breaches of security by hackers. Although we proactively employ multiple measures to defend our systems against intrusions and attacks, our measures may not prevent unauthorized access or use of sensitive data. A breach of our AAV operating systems or command-and-control systems may result in product damages, data losses and, in extreme cases, AAV accidents or hijacking of our AAVs to perform unlawful activities.

A cybersecurity breach could harm our reputation and deter our customers and potential customers from using our AAVs. In addition, any such breach could cause us to incur costs to correct the breaches or failures, expose us to uninsured liability, increase our risk of regulatory scrutiny, subject us to lawsuits and result in the imposition of material penalties and fines.

An accident involving an AAV provided by us or another manufacturer could harm the AAV industry.

An accident involving an AAV provided by us or another manufacturer could cause regulatory agencies around the world to tighten restrictions on the use of AAVs, particularly over-populated areas, and could cause the public to lose confidence in our products and AAVs generally. There are risks associated with autopilot, flight control, communications and other advanced technologies, and, from time to time, there have been accidents associated with these technologies. The safety of certain cutting-edge technologies depends in part on user interaction, and users may not be accustomed to using such technologies. We, the VIE or the VIE's subsidiaries could face unfavorable and tightened regulatory control and intervention on the use of autopilot and other advanced technologies and be subject to liability and government scrutiny to the extent accidents associated with our autonomous navigation systems occur. Should a high-profile accident occur resulting in substantial casualty or damages, either involving our AAVs or products offered by other companies, public confidence in and regulatory attitudes toward AAVs could deteriorate. Any of the foregoing could materially and adversely affect our results of operations, financial condition and growth prospects.

We may be compelled to undertake product recalls or take other actions, which could adversely affect our brand image and results of operations.

Our AAVs may not perform in line with customers' expectations. Any product defects, accidents or any other failure of our AAVs to perform as expected could harm our reputation and result in adverse publicity, revenue loss, delivery delays and product recalls, which could harm our brand and reputation. Any product recall or lawsuit seeking significant monetary damages either in excess of or outside of our insurance coverage may have a material adverse effect on our business and financial condition. In the future, we may, voluntarily or involuntarily, initiate a recall if any of our AAVs, including any systems or components sourced from our suppliers, prove to be defective or noncompliant with applicable laws and regulations. Such recalls, whether voluntary or involuntary and whether caused by systems or components engineered or manufactured by us or our suppliers, could incur significant expenses and adversely affect our brand image in our target markets. They may also inhibit or prevent commercialization of our current and future product candidates.

We may become subject to product liability claims or warranty claims, which could harm our financial condition and liquidity if we are not able to successfully defend or insure against such claims.

We may be exposed to significant product liability claims if our AAVs do not perform as expected or malfunction. Any defects, errors, or failures in our products or the misuse of our AAVs, operating systems and infrastructure could also result in injury, death or property damage. Our risks in this area are particularly pronounced given we have limited field experience in the operation of our AAVs. A successful product liability claim against us could require us to pay a substantial monetary award. Moreover, a product liability claim could generate substantial negative publicity about our AAVs and business and inhibit or prevent commercialization of our current and future AAV models. Our insurance coverage might not be sufficient to cover all potential product liability claims. In addition, the same level of insurance coverage may not be available in the future at economical prices, or at all. Even if we are fully insured as it relates to a claim, the claim could nevertheless diminish our brand and divert management's attention and resources, which could have a negative impact on our business, financial condition and result of operations.

We generally provide standard warranties on our AAVs. The term of a warranty is between six months to three years, depending on the product line and the specific part or component. The occurrence of any material defects in our AAVs could make us liable for damages and warranty claims. In addition, we could incur significant costs to correct any defects or other problems, including costs related to product recalls. Warranty claims may also lead to litigation. Any negative publicity related to the perceived quality of our AAVs could affect our brand image, decrease retailer, distributor and customer demand, and adversely affect our operating results and financial condition.

If we fail to successfully develop and commercialize new products, services and technologies that are well received by customers, our operating results may be materially and adversely affected.

Our future growth depends on whether we can continually develop and introduce new generations of our existing AAV product lines and update our operating systems and infrastructure with enhanced functionalities and value-added services. This is particularly important in the current industry landscape where technologies and consumer preferences evolve rapidly, which may shorten the lifecycles of our existing products. We plan to upgrade our current AAV models and introduce new models in order to continue to provide AAVs with the latest technologies. As technological advancements can be complex and costly, we could experience delays in the development and introduction of new products and services in the future.

Our ability to roll out new and innovative products and services depends on a number of factors, including significant investments in research and development, quality control of our products and services and effective management of our supply chain. We may need to devote more resources to the research and development of new or enhanced products, services and technologies, which may reduce our profitability. In addition, our research and development efforts may not yield the benefits we expect to achieve in a timely manner, or at all. To the extent that we are unable to execute our strategy of continuously introducing new and innovative products, diversifying our product portfolio and satisfying consumers' changing preferences, we may not be able to grow our user base, and our competitive position and results of operations may be adversely affected. Even if we are able to keep up with technological changes and develop new models, our prior models may as a result become obsolete sooner than expected, potentially reducing our return on investment.

We have limited experience in managing sales to multiple countries and we are subject to a variety of costs and risks due to our continued international expansion.

We delivered seven, two and four EH216 series AAVs abroad in 2020, 2021 and 2022, respectively. We have entered into sales contracts with customers outside China. In 2020, we delivered our EH216 series AAVs to customers in Canada, Mexico, Japan, Korea, etc. In 2021, we delivered our EH216 series AAVs to customers in Korea and Indonesia. In 2022, we delivered our EH216 series AAVs to customers in Sweden, Mexico and Israel. As international expansion is one of our core strategies, we expect our international sales to increase in the future. In markets outside China, we generally have less experience in marketing, selling and deploying our AAVs. International expansion has required and will continue to require us to invest significant capital and other resources, and our efforts may not be successful. International sales and operations are subject to risks such as:

- limited brand recognition;
- costs associated with establishing new distribution networks;
- difficulty in finding qualified partners for overseas distribution;
- inability to anticipate changes in local market conditions, economic landscapes, and consumers' preferences and customs;
- difficulties in staffing and managing foreign operations;
- lack of familiarity with and understanding of the local legal, regulatory and policy frameworks, as well as burdens of complying with a wide variety of local laws and regulations, including those governing personal data protection and safety control;
- political and economic instability;
- trade restrictions;
- differing employment laws and practices, as well as potential labor disruptions;
- the imposition of government controls;
- lesser degrees of intellectual property protection;

- tariffs and customs duties and the classifications of our goods by applicable governmental bodies; and
- a legal system subject to undue influence or corruption.

Additionally, to export our AAVs to certain jurisdictions, we may face challenges in coordinating with both PRC and the applicable foreign governments and regulatory authorities. If we cannot export our AAVs to such jurisdictions, our business, prospects, financial condition and operating results may be materially and adversely impacted.

The failure to manage any of these risks could negatively affect our international business and consequently our overall business and operating results. In addition, the concern over these risks may also prevent us from entering into, or marketing, selling or releasing certain of our AAVs and AAV commercial solutions and related services in, certain markets.

We may rely on some third-party distributors for sales, marketing and distribution activities relating to our AAVs.

Currently we do not rely on any third-party distributors for sales, marketing and distribution activities relating to our AAVs. However, some of our business partners may act as third-party distributors that sell, market and distribute our AAVs to their customers in the future. Accordingly, we may be subject to a number of risks associated with third-party distributors, including a lack of day-to-day control over the activities of third-party distributors selling or using our products and solutions; third-party distributors may terminate their arrangements with us on limited or no notice, or may change the terms of these arrangements in a manner that is unfavorable to us for reasons outside of our control; and any disagreements with our third-party distributors could lead to costly and time-consuming litigation or arbitration. If we fail to establish and maintain satisfactory relationships with our third-party distributors, we may not be able to sell, market and distribute our AAVs according to our internal budget and plans, our future revenues and market share may not grow at a pace that we expect, and we could be subject to increases in sales and marketing and other costs which would harm our results of operations and financial condition.

Our operations may be interrupted by production difficulties or delays due to mechanical failures, utility shortages or stoppages, fire, natural disaster or other calamities at or near our facilities.

Production difficulties, such as capacity constraints, mechanical and systems failures and the need for equipment upgrades, may suspend our production and/or reduce our output. There can be no assurance that we will not experience problems with our production facilities in the future or that we will be able to address any such problems in a timely manner. Problems with key equipment in one or more of our production facilities may affect our ability to produce our AAVs or cause us to incur significant expenses to repair or replace such equipment. Scheduled and unscheduled maintenance programs may affect our production output. Any of these could have a material adverse effect on our business, financial condition, results of operations and prospects.

We depend on a continuous supply of utilities, such as electricity and water, to operate our production facilities. Any disruption to the supply of electricity or other utilities may disrupt our production, or cause the deterioration or loss of our inventory. This could adversely affect our ability to fulfill our sales orders and consequently may have an adverse effect on our business and results of operations.

In addition, we are vulnerable to natural disasters and other calamities such as hurricanes, tornadoes, floods, earthquakes and other adverse weather and climate conditions. Although we have servers that are hosted in an offsite location, our backup system does not capture data on a real-time basis, and we may be unable to recover certain data in the event of a server failure. We cannot assure you that any backup systems will be adequate to protect us from the effects of fire, floods, typhoons, earthquakes, power loss, telecommunications failures, break-ins, war, riots, terrorist attacks or similar events. Any of the foregoing events may give rise to interruptions, breakdowns, system failures, technology platform failures or internet failures, which could cause the loss or corruption of data or malfunctions of software or hardware as well as adversely affect our ability to provide services on our platform.

Our customers may experience service failures or interruptions due to defects in the software, infrastructure, components or engineering system that compromise our products and services, or due to errors in product installation, any of which could harm our business.

Our products and services may contain undetected defects in the software, infrastructure, components or engineering system. Sophisticated software and applications, such as those adopted and offered by us, often contain “bugs” that can unexpectedly interfere with the software and applications’ intended operations. Our internet services may from time to time experience outages, service slowdowns or errors. Defects may also occur in components or processes used in our products or for our services.

There can be no assurance that we will be able to detect and fix all defects in the hardware, software and services we offer. Failure to do so could result in decreases in sales of our products and services, lost revenues, significant warranty and other expenses, decreases in customer confidence and loyalty, losing market share to our competitors, and harm to our reputation.

Our success depends on the continuing efforts of our key employees, including our senior management members and other key personnel. If we fail to hire, retain and motivate our key employees, we could lose the innovation, collaboration and focus that contribute to our business.

We believe that our success depends substantially on the continued efforts of our key employees, including our senior management members and other qualified and key personnel. We rely on our executive officers, senior management and key employees to generate business and execute programs successfully. In addition, the relationships and reputation that members of our management and key employees have established and maintain with government personnel contribute to our ability to maintain good customer relations and to identify new business opportunities. The loss of any key personnel or our failure to attract additional talent could reduce our employee retention, disrupt our research and development activities and operations, and impair our revenue growth and competitiveness. If one or more of our executive officers or key employees were unable or unwilling to continue their services with us, we might not be able to replace them easily, in a timely manner, or at all, and we might lose the innovation, collaboration and focus that contribute to our business.

Our business and prospects depend significantly on our ability to build our EHang brand.

Our business and prospects are heavily dependent on our ability to build, maintain and strengthen the EHang brand. If we do not continue to establish, maintain and strengthen our brand, we may lose the opportunity to build a critical mass of customers. Promoting and positioning our brand will likely depend significantly on our ability to provide high-quality AAVs and AAV commercial solutions and engage with our customers as intended. In addition, we expect that our ability to develop, maintain and strengthen the EHang brand will also depend heavily on the success of our user development and branding efforts. Such efforts mainly include building a community of engaged online and offline users as well as other branding initiatives, such as AAV shows and events. To promote our brand, we may be required to change our user development and branding practices, which could result in substantially increased expenses. If we do not develop and maintain a strong brand, our business, prospects, financial condition and operating results will be materially and adversely impacted.

Our EHang brand could be subject to adverse publicity if incidents related to our products occur or are perceived to have occurred, whether or not we are at fault. In particular, given the popularity of social media, including WeChat and Weibo in China, any negative publicity, regardless of its truthfulness, could quickly proliferate and harm consumer perceptions of and confidence in our brand. Furthermore, we may be affected by adverse publicity related to our manufacturing or other partners, whether or not such publicity is related to their collaboration with us. Our ability to successfully position our brand could also be adversely affected by perceptions of the quality of our partners’ products and services. In addition, from time to time, our AAVs and AAV commercial solutions are evaluated and reviewed by third parties. Any unfavorable reviews could adversely affect consumer perceptions of our AAVs and AAV commercial solutions.

Weather and seasonality may have a material adverse effect on our operations.

Our sales of AAVs and AAV commercial solutions may be affected by weather and seasonality. Our AAV commercial solutions are mainly delivered outdoor. Customers may choose alternative transportation in severe weather conditions in consideration of safety factors, even if our AAVs are able to endure such conditions. As a result, our business, financial condition and operating results may be materially and adversely impacted by the weather conditions. Our operating results may vary from period to period due to many factors, including seasonal factors that may have an effect on the demand for our AAV commercial solutions in the future. As a result, our quarterly results of operations and financial position at the end of a particular quarter may not necessarily be representative of the results we expect at year-end or in other quarters of a year. Our operating results would suffer if we did not achieve revenues consistent with our expectations due to seasonal demand and weather changes because many of our expenses are based on anticipated levels of annual revenues.

Any decline in the business of our business partners or the deterioration of our relationship with them could have a material adverse effect on our operating results.

We collaborate with various business partners to promote our AAVs and AAV commercial solutions. There can be no guarantee that those business partners will continue to collaborate with us in the future. If we are unable to maintain good relationships with our business partners, or the business of our business partners declines, the reach of our products and services may be adversely affected and our ability to maintain and expand our user base may decrease.

Most of the agreements with our business partners do not prohibit them from working with our competitors or from offering competing services. If our partners change their standard terms and conditions in a manner that is detrimental to our business, or if our business partners decide not to continue working with us, or choose to devote more resources to supporting our competitors or their own competing products, we may not be able to find a substitute on commercially favorable terms, or at all, and our competitive advantages may diminish.

We rely on external suppliers for raw materials and certain key externally sourced components and parts used in the assembly of our AAVs, and have limited control over the quality of these components and parts.

We purchase certain key externally sourced components and raw materials, such as computers chips, batteries, motors and electronic displays, from external suppliers for use in our assembly, production and operations of AAVs. A continuous and stable supply of components and raw materials that meet our standards is crucial to our assembly, production and operations. We cannot assure you that we will be able to maintain our existing relationships with our suppliers and continue to be able to stably source key components and raw materials at reasonable prices, or at all. We have integrated our suppliers' technologies within our products such that having to change to an alternative supplier may cause significant disruption to our operations. The supply of key components could be interrupted for any reason, or there could be significant increases in the prices of these key components. Additionally, changes in business conditions, force majeure, governmental changes and other factors beyond our control, or that we do not presently anticipate, could also affect our suppliers' ability to deliver components to us on a timely basis. If any of these events occurs, our business, financial condition, results of operations and prospects may be materially and adversely affected.

We cannot guarantee that the quality of components and parts manufactured by external suppliers will be consistent and maintained at a high standard. Any defects of or quality issues with these components or any noncompliance incidents associated with these third-party suppliers could result in quality issues with our AAVs and hence compromise our brand image and results of operations. In extreme situations, we may be exposed to liabilities as a result of significant damages caused by certain components from external suppliers and we cannot assure you that we will be able to obtain sufficient insurance coverage at an acceptable cost in the future. A successful claim brought against us in excess of our available insurance coverage may have a material adverse effect on our business, financial condition and operating results.

Safety issues or public perceptions of safety issues concerning lithium-ion batteries could have a material adverse impact on our business.

The battery packs installed on our AAVs make use of lithium-ion cells. On rare occasions, lithium-ion cells can rapidly release the energy they contain by venting smoke and flames in a manner that can ignite nearby materials as well as other lithium-ion cells. While the battery packs used for our AAVs are designed to passively contain any single cell's release of energy without spreading to neighboring cells, a field or testing failure of our AAVs could occur, which could result in accidents, casualty or damages, and subject us to lawsuits, product recalls, and/or redesign efforts. Also, negative public perceptions regarding the suitability of lithium-ion cells for AAV applications or any future incident involving lithium-ion cells, even if such incident does not involve our AAVs, could seriously harm our business. In addition, we store a significant number of lithium-ion cells at our facilities. Any mishandling of battery cells may cause disruption to the operation of our facilities. While we have implemented safety procedures related to the handling of the cells, a safety issue or fire related to the cells could disrupt our operations. Such damage or injury could lead to adverse publicity and potentially a safety recall.

We rely on third-party logistics providers to deliver our domestic sales orders and certain overseas orders. Inadequate third-party logistics services or failure to mitigate the risks of damage or disruption to our distribution logistics could adversely affect our business.

Our ability to transport and sell our AAVs is critical to our success across our operations. We typically rely on third-party logistics service providers to deliver our domestic sales orders and certain overseas orders. Damage or disruption to our distribution logistics due to disputes, weather, natural disasters, fire, explosions, terrorism, pandemics or labor strikes could impair our ability to distribute or sell our AAVs. Inadequate third-party logistics services could also potentially disrupt our distribution and sales and compromise our business reputation. Failure to take adequate steps to mitigate the likelihood or potential impact of such events, or to effectively manage such events if they occur, could adversely affect our business, financial condition and results of operations, as well as require additional resources to restore our supply chain.

If we fail to comply with environmental protection and work safety laws and regulations, we could become subject to fines or penalties or incur costs that could harm our business.

We are subject to numerous environmental protection and work safety laws and regulations. For more details, see "Item 4. Information on the Company—B. Business Overview—PRC Regulation—Environmental Protection and Work Safety." We also could incur significant costs associated with civil or criminal fines and penalties for failure to comply with such laws and regulations. Environmental and social laws and regulations have tended to become increasingly stringent. There has been increased global focus on environmental and social issues and it is possible that China may potentially adopt more stringent standards or new regulations in these areas. To the extent regulatory changes occur in the future, they could result in, among other things, increased costs to our company. In addition, we may incur substantial costs in order to comply with current or future environmental protection and work safety laws and regulations. These current or future laws and regulations may impair our research, development or production efforts. Our failure to comply with these laws and regulations also may result in substantial fines, penalties or other sanctions.

If our business partners, contractors, suppliers, sales agents, dealers or third-party logistics services providers fail to use ethical business practices and comply with applicable laws and regulations, our brand image could be harmed due to negative publicity beyond our own control.

Our reputation is sensitive to allegations of unethical business practices. We do not control the business practices of our business partners, independent contractors and suppliers, sales agents, dealers or third-party logistics services providers. Accordingly, we cannot guarantee their compliance with ethical business practices, such as environmental responsibilities, fair wage practices, and compliance with child labor laws, among others. A lack of demonstrated compliance could lead us to seek alternative suppliers, sales agents or dealers, which could increase our costs and result in delayed delivery of our products, product shortages or other disruptions of our operations. Violation of labor or other laws by our suppliers, business partners, sales agent, dealers or third-party logistics services suppliers or the divergence of their labor or other practices from those generally accepted as ethical in the markets in which we do business could also attract negative publicity, diminish our brand image and reduce demand for our AAVs and AAV commercial solutions.

If customers modify our AAVs or operating systems, the AAVs may not operate properly, which may cause damage, create negative publicity and harm our business.

Our customers may try to modify our AAVs or operating systems for various reasons, which could compromise the performance and safety of our AAVs, as well as the safety of their passengers. During such modifications, they may use third-party parts that may not be compatible with our products. We do not test, nor do we endorse, such modification. In addition, the use of improper external cabling or unsafe charging outlets can expose our customers to injury from AAV malfunctioning. Any injuries or damages resulting from such modifications or misuses could result in adverse publicity, which would negatively affect our brand and harm our business, prospects, financial condition and operating results.

A new health epidemic could significantly disrupt our operations and adversely affect our results of operations.

Our business could be significantly affected by public health epidemics that may hit China and/or other countries where we sell our products, such as the outbreak of coronavirus, avian influenza, severe acute respiratory syndrome, or SARS, Zika virus, Ebola virus or other disease. For example, the severity of the past COVID-19 pandemic resulted in lock-downs, travel restrictions and quarantines imposed by governments across the world and materially affected general commercial activities on a global scale. In 2022, we experienced delayed fulfillments from suppliers as well as reduced demand for our AAVs from the tourism sector, which suffered disproportionately from the pandemic. The majority of our revenue generated from sales of the EH216 series AAVs are from a limited number of customers that mainly operate our AAVs in tourism locations in China, rather than in broad, mainstream commercial operations. Therefore, in 2021 and 2022, we faced delayed collection of our accounts receivable from some of our customers later than the due dates. A COVID-19 outbreak may result in these customers ceasing purchases, canceling or reducing orders for our products or services, or failing to make payments owed to us in a timely manner or at all, which may materially and adversely impact our business and result of operations. The COVID-19 pandemic had caused an economic downturn in many countries. Such general economic slowdown may reduce the demand for our products and services. Any future outbreak of a contagious disease, and other adverse public health developments may restrict economic activities in affected regions, resulting in reduced business volume, temporary closure of our production facilities and offices or otherwise disrupt our business operations and adversely affect our results of operations.

We could be adversely affected by security-related concerns of the United States and other countries against Chinese companies and products and political tensions between the United States and China.

Due to security-related concerns, U.S. government actions targeting exports of certain technologies to China are becoming more pervasive. The U.S. government has in the past issued export restrictions that effectively banned U.S. companies from selling products to ZTE Corporation, and in May 2019 imposed a similar ban on sales of all products to Huawei. In 2018, the U.S. adopted new laws designed to address concerns about the export of emerging and foundational technologies to China. In May 2019, former U.S. President Donald J. Trump issued an executive order that invoked national emergency economic powers to implement a framework to regulate the acquisition or transfer of information communications technology in transactions that imposed undue national security risks. In October 2022, the Biden Administration issued extensive new restrictions on the export to China of advanced semiconductors, as well as design software and manufacturing equipment, without a special license. These actions could lead to additional restrictions on the export of products that include or enable technologies on which we rely. Such restrictions imposed by the United States or any other countries may make it more difficult for us to procure or license technological products from these countries, or affect the ability of our PRC suppliers to manufacture and provide us with advanced components, which may increase our costs, impair our products' competitiveness, and have a material adverse effect on our business.

Similar security-related concerns may affect our ability to export our products to the United States and other countries. In May 2019, the U.S. Department of Homeland Security advised American companies about the inherent security risks associated with Chinese-made drones. In a related development, the U.S. government was also reportedly considering placing Chinese surveillance systems providers, including Hikvision Digital Technology and Dahua Technology, on a trade blacklist that would cut off their access to American hi-tech suppliers. We cannot assure you that our AAVs will not be placed on such trade blacklist in the future. If that event occurs, our ability to export our products to the United States will be adversely affected.

In addition, political tensions between the United States and China have escalated due to, among other things, the COVID-19 outbreak, the PRC National People's Congress' passage of Hong Kong national security legislation, sanctions imposed by the U.S. Department of Treasury on certain officials of the Hong Kong Special Administrative Region and the central government of the PRC and the executive orders issued by former U.S. President Donald J. Trump in August 2020 that prohibit certain transactions with ByteDance Ltd., Tencent Holdings Ltd. and the respective subsidiaries of such companies. Rising political tensions could reduce levels of trades, investments, technological exchanges and other economic activities between the two major economies, which would have a material adverse effect on global economic conditions and the stability of global financial markets. Any of these factors could have a material adverse effect on our business, prospects, financial condition and results of operations.

We, the VIE and the VIE's subsidiaries may need to defend ourselves against claims of intellectual property infringement, which may be time-consuming and costly.

Companies, organizations or individuals, including our competitors, may hold or obtain patents, trademarks or other proprietary rights that would prevent, limit or interfere with our ability to make, use, develop, sell or market our AAVs, AAV operating systems and infrastructure or their components, which could make it more difficult for us to operate our business. Companies holding patents or other intellectual property rights may bring suits alleging infringement of such rights by us, the VIE or the VIE's subsidiaries or otherwise assert their rights against us, the VIE or the VIE's subsidiaries. Moreover, our, the VIE's or its subsidiaries' applications and uses of trademarks relating to design, software or artificial intelligence technologies could be found to infringe upon existing trademark ownership and rights. We, the VIE or the VIE's subsidiaries may also fail to apply for key trademarks in a timely manner. For example, there are some precedent registrations by several other Chinese companies of the trademark “EH” (the Chinese characters for our brand, “EHang”) for vehicles and bicycles, which fall into the same class of products as remote aerial vehicles and aerospace transportation. Although we received a favorable judgement in a proceeding relating to such precedent registrations, we may continue to face intellectual property infringement claims in the future.

If we, the VIE or the VIE's subsidiaries are determined to have infringed upon a third party's intellectual property rights, the VIE or the VIE's subsidiaries may be required to do one or more of the following:

- cease selling, incorporating certain components into, or using AAVs or offering goods or services that incorporate or use the challenged intellectual property;
- pay substantial damages;
- seek a license from the holder of the infringed intellectual property right, which license may not be available on reasonable terms or at all;

- redesign our, the VIE's or its subsidiaries' AAVs, AAV operating systems and infrastructure, components or services; or
- establish and maintain alternative branding for our, the VIE's or its subsidiaries' products and services.

In the event of a successful claim of infringement against us, the VIE or the VIE's subsidiaries and our, the VIE's or its subsidiaries' failure or inability to obtain a license to the infringed technology or other intellectual property right, our business, prospects, operating results and financial condition could be materially and adversely affected. In addition, any litigation or claims, even if frivolous, could result in substantial costs, negative publicity and diversion of resources and management attention.

Our or the VIE's intellectual property rights may not protect us effectively.

As of March 31, 2023, we and the VIE together owned 331 issued patents, 302 pending patent applications, 371 registered trademarks, and 24 registered copyrights in China in relation to our and the VIE's technologies. We cannot assure you that our or the VIE's pending patent applications will be granted. Even if our or the VIE's applications are successful, patents may be contested, circumvented or invalidated in the future.

In addition, the rights granted under any issued patents may not provide us with proprietary protection or competitive advantages. The claims under any patents that are issued from our or the VIE's patent applications may not be broad enough to prevent others from developing technologies that are similar or that achieve results similar to ours or the VIE's. It is also possible that the intellectual property rights of others could bar us or the VIE from licensing and exploiting any patents that are issued from our or the VIE's pending applications. Numerous patents and pending patent applications owned by others exist in the fields in which we and the VIE have developed and are developing our technologies. These patents and patent applications might have priority over our or the VIE's patent applications and could subject our or the VIE's patent applications to invalidation. Finally, in addition to those who may claim priority, any of our or the VIE's existing or pending patents may also be challenged by others on the basis that they are otherwise invalid or unenforceable.

Implementation and enforcement of PRC laws on intellectual property rights have historically been deficient and ineffective. Accordingly, protection of intellectual property rights in China may not be as effective as in the United States or other developed countries. Furthermore, policing unauthorized use of proprietary technologies is difficult and expensive. We and the VIE rely on a combination of patent, copyright, trademark and trade secret laws and restrictions on disclosure to protect our and the VIE's intellectual property rights. Despite our efforts to protect our and the VIE's proprietary rights, third parties may attempt to copy or otherwise obtain and use our or the VIE's intellectual property or seek court declarations that they do not infringe upon our or the VIE's intellectual property rights. Any unauthorized use of our or the VIE's intellectual property by third parties may adversely affect our current and future revenues and our reputation. Monitoring unauthorized use of our and the VIE's intellectual property is difficult and costly, and we cannot assure you that the steps we or the VIE have taken or will take will prevent misappropriation of our and the VIE's intellectual property. From time to time, we or the VIE may have to resort to litigation to enforce our and the VIE's intellectual property rights, which could result in substantial costs and diversion of our resources.

Failure to safeguard personal information could subject us to penalties, damage our reputation and brand, and harm our business and results of operations.

Through our AAVs, app and command-and-control systems, we log information about each AAV's use, such as charge time, battery usage, mileage and location information, in order to aid us in vehicle diagnostics, repair and maintenance, as well as to help us customize and optimize the flying experience. Images and videos captured by cameras attached to our AAVs are stored on our servers, servers of third-party cloud storage providers or other servers designated by our customers. We, therefore, process, including but not limited to collect, store, process, use, transfer, provide, disclose and delete, personal data from our users in order to better understand and serve our users. Such personal data processing also enables our content feeds recommendation. Possession and use of our users' flying behavior and data in conducting our business may subject us to legislative and regulatory oversight in China and other jurisdictions, such as the European Union and the United States. For example, in January 2018, the European Union promulgated the General Data Protection Regulation to further protect fundamental rights in privacy and personal information so that members of the general public have more control over their personal information. Regulations in relevant jurisdictions may require us to obtain user consent for the collection of personal information, restrict our use of such personal information and hinder our ability to expand our user base. In the event of a data breach or other unauthorized access to our user data, we may have obligations to notify users about the incident and we may need to provide some form of remedy for the individuals affected by the incident.

Concerns or claims about our practices with regard to the processing of personal information or other privacy-related matters, even if unfounded, could damage our reputation and results of operations. In the PRC, governmental authorities have enacted a series of laws and regulations to enhance the protection of privacy and data. The PRC Constitution, the PRC Criminal Law, the Civil Code of the PRC, the Cybersecurity Law of the PRC and relevant regulations require network operators, which may include us, to ensure the security and stability of the services provided via network and protect individual privacy and the security of personal data in general by requiring the consent of internet users prior to the processing of their personal data. Under the Cybersecurity Law, the owners and administrators of networks and network service providers are subject to various personal information security protection obligations, including restrictions on the collection and use of personal information of users, and they are required to take steps to prevent personal data from being divulged, stolen, or tampered with. Regulatory requirements regarding the protection of personal information are constantly evolving and can be subject to differing interpretations or significant changes, making the extent of our responsibilities in that regard uncertain. For example, on June 10, 2021, the Standing Committee of the National People's Congress, or SCNPC, promulgated the *Data Security Law of the People's Republic of China*, or the Data Security Law, effective from September 1, 2021. The Data Security Law provides that data processing activities that affects or may affect national security shall be subject to a data security review procedure. On July 6, 2021, the General Office of the CPC Central Committee and the General Office of the State Council jointly promulgated the Opinions on Strictly Cracking Down on Illegal Securities Activities, which called for a heightened scrutiny over overseas-listed China-based companies of their compliance with the laws and regulations regarding data security, cross-border data flow and management of confidential information, and such laws and regulations are expected to undergo further changes, which may require increased information security responsibilities and stronger cross-border information management mechanism and process. We may need to adjust our business to comply with data security requirements and other laws and regulations from time to time.

On August 20, 2021, the SCNPC promulgated the *Personal Information Protection Law of the People's Republic of China*, or the Personal Information Protection Law, which integrates the scattered rules with respect to personal information rights and privacy protection and took effect on November 1, 2021. We may be required to make further adjustments to our business practices to comply with the personal information protection laws and regulations.

On November 14, 2021, the CAC publicly solicited opinions on *the Administration Regulations on Cyber Data Security (Draft for Comments)*, or the Draft Data Security Regulations. The Draft Data Security Regulations stipulates that data processors processing personal information of more than one million users shall be subject to the various requirements that apply to important data processors, including but not limited to: (a) important data processors shall specify the person in charge of data security and establish a data security management organization; (b) important data processors shall file with competent authorities within 15 working days after the identification of important data; (c) important data processors shall develop a data security training program for its employees; (d) important data processors shall carry out annual data security assessment and file such report with competent authorities annually. Uncertainties exist with respect to its enactment timetable, final content, interpretation and implementation. We cannot assure you that relevant governmental authorities will not interpret the laws and regulations in ways that may negatively affect us. At this stage, we are unable to predict the possible consequences of these drafts, if any, and we are monitoring and assessing the rulemaking process closely. Any failure, or perceived failure to maintain the security of our user data or to comply with applicable PRC or foreign privacy, data security and personal information protection laws and obligations may result in civil or regulatory liability, including governmental or data protection authority enforcement actions and investigations, fines, penalties, enforcement orders requiring us to cease operating in a certain way, litigation, or adverse publicity, and may require us to expend significant resources in responding to and defending allegations and claims.

On December 31, 2021, the CAC, together with other regulatory authorities, published the *Administrative Provisions on Algorithm Recommendation for Internet Information Services*, or the Administrative Provisions on Algorithm Recommendation, effective on March 1, 2022. Pursuant to the Administrative Provisions on Algorithm Recommendation, users should be given an option to easily turn off algorithm recommendation services, and service providers shall, among others, establish and improve the management systems and technical measures for algorithm driven recommendation mechanism and regularly review, evaluate and verify the principle, models, data and application results of algorithms. The Company will closely monitor the regulatory development and adjust its business operation from time to time to comply with the regulations over algorithm.

Pursuant to the National Security Law issued by SCNPC on July 1, 2015, the state 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 national security of China. On December 28, 2021, the CAC together with other regulatory authorities officially announced the Cybersecurity Review Measures, which is consistent with the Cybersecurity Review Measures (Revision Draft for Comment) announced by the CAC on July 10, 2021. Pursuant to the Cybersecurity Review Measures, the procurement of network products and services by critical information infrastructure operators and the data processing activities conducted by network platform operators which affects or may affect national security shall be subject to cybersecurity review. Network platform operators mastering personal information of more than one million users must apply to the Cybersecurity Review Office for cybersecurity review if they intend to be listed abroad. On July 30, 2021, the State Council promulgated the *Regulations on Security Protection of Critical Information Infrastructure*, or the CIIO Regulations, which became effective on September 1, 2021. Pursuant to the CII Regulations, critical information infrastructure refers to any important network facilities or information systems of an important industry or field such as public communication and information service, energy, transport, water conservation, finance, public services, e-government affairs, science and technology industry for national defense and other industries and sectors that may seriously endanger national security, people's livelihood and public interest in case of damage, function loss or data leakage. In addition, relevant administration departments of each critical industry and sector are responsible for formulating eligibility criteria and determining the critical information infrastructure in the respective industry or sector. The operators will be informed about the final determination as to whether they are categorized as critical information infrastructure operators, or CIIOs. As of the filing of this annual report on Form 20-F, no detailed rules or interpretations have been issued and we have not been informed as a CIIO by any governmental authorities. Furthermore, the exact scope of CIIOs, under the current regulatory regime remains unclear, and the PRC governmental authorities may have discretion in the interpretation and enforcement of these laws and regulations. Therefore, it is uncertain whether we would be deemed as a CIIO under PRC law. If we are identified as CIIO, we will be subject to stricter requirements on business operations and cybersecurity compliance, and we may need to follow cybersecurity review procedure and apply with Cybersecurity Review Office before making certain purchases of network products and services, and if a cybersecurity review is applicable, we may be required to suspend providing any existing or new services to our users, and we may experience other disruptions of our operations.

In addition, the PRC regulatory authorities have recently taken steps to strengthen the regulations on data protection and conducted several rounds of relevant inspections. We have not been informed by the CAC of any further requirements of rectification. As laws and regulations in China on the protection of privacy and data are constantly evolving, complying with new laws and regulations could cause us to incur substantial costs or require us to change our business practices in a manner materially adverse to our business.

Despite our efforts to comply with applicable laws, regulations and other obligations relating to privacy, data protection and information security, it is possible that our practices, offerings or platform could fail to meet certain requirements imposed on us by such laws, regulations or obligations. Any failure on our part to comply with applicable laws or regulations or any other obligations relating to privacy, data protection or information security, or any compromise of security that results in unauthorized access, collection, transfer, use or release of personally identifiable information or other data, or the perception or allegation that any of the foregoing types of failure or compromise has occurred, could damage our reputation, discourage new and existing users from using our platform or result in investigations, fines, suspension of our app, or other penalties by government authorities and private claims or litigation, any of which could materially adversely affect our business, financial condition and results of operations. In addition, the interpretation and application of the aforementioned laws and regulations are often uncertain and in flux. Our practice may become inconsistent with these laws and regulations.

Our platform and internal systems depend on the ability of software and hardware developed and maintained internally and/or by third parties to store, retrieve, process and manage immense amounts of data, including personal information or other privacy-related matters. The software and hardware on which we rely may now or in the future contain undetected programming errors, bugs, or vulnerabilities which may result in errors or compromise our ability to protect the data of our users and in turn adversely affect our business, financial condition and operation results. Any systems failure or compromise of security that results in the unauthorized access to or release of the data, photo or messaging history of our users could significantly limit the adoption of our services, as well as harm our reputation and brand, result in litigation or regulatory investigations against us, and we could be subject to material liability or penalties. Additionally, we connect our platform with software development kit provided by third parties who may also process users' data. The integrity of our user data also depends on their ability to secure and protect the data they process. The risk that these types of events could seriously harm our business is likely to increase as we expand the scope of services we offer and as we increase the size of our user base.

We may also become subject to laws and regulations affecting data protection, data privacy and/or information security in other jurisdictions by virtue of having users who reside in these jurisdictions, even if we do not have a physical presence there. Many jurisdictions have in the past adopted, and may in the future adopt, new laws and regulations, or amendments to existing laws and regulations, affecting data protection, data privacy and/or information security, such as the General Data Protection Regulation, or the GDPR, adopted by the European Union that became fully effective on May 25, 2018. The interpretation and application of these laws or regulations are often uncertain and in flux. We cannot guarantee you that our practice is consistent with these laws and regulations and our practice may become inconsistent with these laws and regulations; if so, we could be subject to fines and orders requiring that we change our practices, which could have an adverse effect on our business and results of operations. Complying with new data laws and regulations could cause us to incur substantial costs or require us to change our business practices in a manner materially adverse to our business.

If users allege that we have improperly used, released or disclosed their personal information, we could face legal claims and reputational damage. We may incur significant expenses to comply with privacy, consumer protection and security standards and protocols imposed by law, regulation, industry standards or contractual obligations. A major breach of our network security and systems could create serious negative consequences for our business and future prospects, including possible fines, penalties, reduced customer demand for our AAVs, and harm to our reputation and brand. See "Item 4. Information on the Company—B. Business Overview—PRC Regulation" for further details.

The execution of our business plans requires a significant amount of capital. In addition, our future capital needs may require us to sell additional equity or debt securities that may dilute the equity interests of our shareholders or introduce covenants that may restrict our operations or our ability to pay dividends.

We will need significant capital to, among other things, conduct research and development, expand our manufacturing capacity, roll out new products and solutions and provide commercial services. We may also need significant capital to maintain our existing property and equipment. We believe that our cash and cash equivalents and our anticipated cash flows from operations will be sufficient to meet our anticipated working capital requirements and material cash requirements, including capital expenditures, for at least the 12 months after the date of this annual report. Our expected sources of capital include both equity and debt financing. However, financing might not be available to us in a timely manner or on acceptable terms, or at all.

Our ability to obtain the necessary financing to carry out our business plan is subject to a number of factors, including general market conditions and investor acceptance of our business plans. These factors may make the timing, amount, terms and conditions of such financing unattractive or unavailable to us. If we are unable to raise sufficient funds, we will have to significantly reduce our spending, delay or cancel our planned activities, substantially change our current corporate structure, or even curtail or discontinue our operations.

In addition, our future capital needs and other business concerns could require us to sell additional equity or debt securities or obtain a credit facility. The sale of additional equity or equity-linked securities could dilute the equity interests of our shareholders. Additional indebtedness would increase our debt-service obligations and may be accompanied by covenants that would restrict our operations or our ability to pay dividends to our shareholders.

We are subject to risks associated with strategic alliances or acquisitions. If we cannot manage the growth of our business or execute our strategies effectively, our business and prospects may be materially and adversely affected.

We have entered into strategic alliances with various business partners, and may in the future enter into joint research and development agreements or co-branding agreements with third parties to further our business purpose from time to time. These alliances could subject us to a number of risks, including risks associated with sharing proprietary information, non-performance by the third parties and increased expenses in establishing new strategic alliances, any of which may materially and adversely affect our business. We may have limited ability to monitor or control the actions of these third parties. If any of these strategic third parties suffers negative publicity or harm to their reputation from events relating to their business, we may also suffer negative publicity or harm to our reputation by virtue of our association with any such third party.

Although we currently do not have any specific acquisition plans, if appropriate opportunities arise, we may acquire additional assets, products, technologies or businesses that are complementary to our existing business. In addition to any required shareholders' approval, we may also have to obtain approvals and licenses from relevant government authorities for the acquisitions and to comply with any applicable PRC laws and regulations, which could result in delays and increased costs, and may derail our business strategies if we fail to do so. Furthermore, past and future acquisitions and the subsequent integration of new assets and businesses into our own require significant attention from our management and could result in a diversion of resources from our existing business, which in turn could have an adverse effect on our business operations. Acquired assets or businesses may not generate the financial results we expect. Acquisitions could result in the use of substantial amounts of cash, potentially dilutive issuances of equity securities, the occurrence of significant goodwill impairment charges, amortization expenses for other intangible assets and exposure to potential unknown liabilities of the acquired business. Moreover, the costs of identifying and consummating acquisitions may be significant.

Our business could be adversely affected by trade tariffs or other trade barriers.

Starting from early 2018, the U.S. President announced the imposition of tariffs on certain Chinese goods entering the United States and both China and the United States have each imposed additional tariff since then. The United States may also in the future impose tariffs on the importation of consumer products related to our business, such as AAVs. In addition, the European Union has imposed tariffs on imports of AAVs originating from the PRC. We plan to export our AAVs to the United States and the European Union. Any new tariffs on AAVs or other relevant products imposed by the United States or the European Union may significantly increase our costs. It is not yet clear what impact these tariffs may have or what actions other governments, including the Chinese government, may take in retaliation. In addition, these developments could have a material adverse effect on global economic conditions and the stability of global financial markets. Any of these factors could have a material adverse effect on our business, financial condition and results of operations.

We, the VIE and the VIE's subsidiaries have limited insurance coverage, which could subject us to significant costs and business disruption.

We, the VIE and the VIE's subsidiaries have limited liability insurance coverage for our products and business operations. We may not be able to secure additional product liability insurance coverage on acceptable terms or at reasonable costs when needed. A successful liability claim against us, the VIE or the VIE's subsidiaries due to injuries or damages suffered by our users could materially and adversely affect our financial condition, results of operations and reputation. Even if unsuccessful, such a claim could cause us adverse publicity, require substantial costs to defend, and divert the time and attention of our management. In addition, we do not have any business disruption insurance. Any business disruption could result in substantial cost to us and diversion of our resources. Furthermore, China, the United States or any other jurisdiction relevant to our business may impose requirements for maintaining certain minimum liability or other insurance relating to the operation of AAVs. Such insurance policies could be costly, which would reduce the demand for our AAVs. Alternatively, certain insurance products that would be desirable to AAV operators may not be commercially available, which would increase the risks of operating our AAVs and also reduce the demand for them.

We are subject to anti-corruption, anti-bribery, anti-money laundering, financial and economic sanctions and similar laws, and noncompliance with such laws can subject us to administrative, civil and criminal fines and penalties, collateral consequences, remedial measures and legal expenses, all of which could adversely affect our business, results of operations, financial condition and reputation.

We are subject to anti-corruption, anti-bribery, anti-money laundering, financial and economic sanctions and similar laws and regulations in various jurisdictions in which we conduct our business or sell our products, including the PRC anti-corruption laws and regulations, the U.S. Foreign Corrupt Practices Act, or the FCPA, the U.K. Bribery Act 2010, and other anti-corruption laws and regulations. The FCPA and the U.K. Bribery Act 2010 prohibit us and our officers, directors, employees and business partners acting on our behalf, including agents, from corruptly offering, promising, authorizing or providing anything of value to a "foreign official" for the purposes of influencing official decisions or obtaining or retaining business or otherwise obtaining favorable treatment. The FCPA also requires companies to make and keep books, records and accounts that accurately reflect transactions and dispositions of assets and to maintain a system of adequate internal accounting controls. The U.K. Bribery Act 2010 also prohibits non-governmental "commercial" bribery and soliciting or accepting bribes. The PRC anti-corruption laws and regulations prohibit bribery to government agencies, state or government owned or controlled enterprises or entities, to government officials or officials that work for state or government owned enterprises or entities, as well as bribery to non-government entities or individuals. There is uncertainty in connection with the implementation of PRC anti-corruption laws. A violation of these laws or regulations could adversely affect our business, results of operations, financial condition and reputation.

We have direct or indirect interactions with officials and employees of government agencies and state-owned affiliated entities in the ordinary course of business. We have also entered into joint ventures and/or other business partnerships with government agencies and state-owned or affiliated entities. These interactions subject us to an increased level of compliance-related concerns. We are in the process of implementing policies and procedures designed to ensure compliance by us and our directors, officers, employees, representatives, consultants, agents and business partners with applicable anti-corruption, anti-bribery, anti-money laundering, financial and economic sanctions and similar laws and regulations. However, our policies and procedures may not be sufficient, and our directors, officers, employees, representatives, consultants, agents, and business partners could engage in improper conduct for which we may be held responsible.

Non-compliance with anti-corruption, anti-bribery, anti-money laundering or financial and economic sanctions laws could subject us to whistleblower complaints, adverse media coverage, investigations, and severe administrative, civil and criminal sanctions, collateral consequences, remedial measures and legal expenses, all of which could materially and adversely affect our business, results of operations, financial condition and reputation. In addition, changes in economic sanctions laws in the future could adversely impact our business and investments in our shares.

We are involved in litigation from time to time and, as a result, we could incur substantial judgments, fines, legal fees or other costs.

We may be the subject of complaints or litigation from customers, suppliers, employees or other third parties for various actions. For example, we received a judgment against us in a dispute with a former employee and entered into a settlement with the former employee in April 2023. The damages sought against us in some of these litigation proceedings could be substantial. We cannot assure you that we will always have meritorious defenses to the plaintiffs' claims. While the ultimate effect of these legal actions cannot be predicted with certainty, our reputation and the result of operations could be negatively impacted. The proceedings we may be involved in from time to time, could incur substantial judgments, fines, legal fees or other costs and have a material adverse effect on our business, financial condition, results of operations and cash flows. See "Item 8. Financial Information—A. Consolidated Statements and Other Financial Information—Legal Proceedings."

Our and the VIE's leased property interest may be defective and our right to lease the properties may be challenged, which could cause significant disruption to our business.

We and the VIE lease all the premises used in our operations from third parties. We and the VIE require the landlords' cooperation to effectively manage the condition of such premises, buildings and facilities. In the event that the condition of the office premises, buildings and facilities deteriorates, or if any or all of our and the VIE's landlords fail to properly maintain and renovate such premises, buildings or facilities in a timely manner or at all, the operation of our offices could be materially and adversely affected.

Moreover, certain lessors have not provided us and the VIE with valid ownership certificates or authorization of sublease for our and the VIE leased properties. Under the relevant PRC laws and regulations, if the lessors are unable to obtain certificate of title because such properties were built illegally or failed to pass the inspection or other reasons, such lease contracts may be recognized as void and as a result, we and the VIE may be required to vacate the relevant properties. In addition, if our and the VIE's lessors are not the owners of the properties and they have not obtained consents from the owners or their lessors or permits from the relevant government authorities, our and the VIE's leases could be invalidated. If this occurs, we and the VIE may have to renegotiate the leases with the owners or the parties who have the right to lease the properties, and the terms of the new leases may be less favorable to us and the VIE, or we and the VIE may be required to vacate the relevant properties if the terms of the new leases are not reached. Furthermore, one lease the VIE has been using for research and development and office purposes had expired, and the VIE is in the process of negotiating renewal with the lessor. We and the VIE may enter into new lease contracts with the lessors, and the terms of the new leases may be less favorable to us and the VIE, or we and the VIE may be required to vacate the relevant properties if the terms of the new leases are not reached.

Under PRC laws, all lease agreements are required to be registered with the local housing authorities. We and the VIE have not registered certain of our lease agreements with the relevant government authorities. Failure to complete these required registrations may expose our and the VIE's landlords, lessors, us and the VIE to potential monetary fines.

We have granted, and may continue to grant, restricted share units and other types of awards under our share incentive plan, which may result in increased share-based compensation expenses.

We adopted the 2015 Share Incentive Plan, or the 2015 Plan, and the 2019 Share Incentive Plan, or the 2019 Plan (collectively, the "Plans"), to incentivize our employees, directors and consultants and align their interests with ours. We recognize expenses in our consolidated statement of loss in accordance with U.S. GAAP. Under the Plans, we are authorized to grant restricted share units and other types of awards. As of the date of this annual report, the maximum number of ordinary shares that may be issued pursuant to all awards granted under the 2015 Plan and 2019 Plan is 8,867,053 and 8,266,949, respectively. As of March 31, 2023, 2,878,750 restricted share units and 53,737 share options had been granted and were outstanding under the Plans. As of December 31, 2022, our unrecognized share-based compensation expenses relating to unvested awards amounted to RMB158.9 million (US\$23.0 million).

We believe the granting of share-based awards is of significant importance to our ability to attract and retain key personnel and employees, and we will continue to grant share-based awards to employees in the future. However, the number of shares reserved for issuance under our share incentive plan may not be sufficient to recruit new employees and to compensate existing employees. Furthermore, prospective candidates and existing employees often consider the value of the equity awards they receive in connection with their employment. Thus, our ability to attract or retain highly skilled employees may be adversely affected by declines in the perceived value of our equity or equity awards. To attract and retain qualified employees, our expenses associated with share-based compensation may increase, which may have an adverse effect on our results of operations.

If we fail to implement and maintain an effective system of internal controls to remediate our material weaknesses over financial reporting, we may be unable to accurately report our results of operations, meet our reporting obligations or prevent fraud, and investor confidence in our company and the market price of the ADSs may be materially and adversely affected.

In preparing our consolidated financial statements as of and for the years ended December 31, 2021 included in this annual report, we and our independent registered public accounting firm, PricewaterhouseCoopers Zhong Tian LLP, identified three material weaknesses in our internal control over financial reporting as of December 31, 2021. As defined in the standards established by the U.S. Public Company Accounting Oversight Board, or PCAOB, a “material weakness” is a deficiency, or combination of deficiencies in internal control over financial reporting, such that there is a reasonable possibility that a material misstatement of the annual or interim financial statements will not be prevented or detected on a timely basis. The material weaknesses that have been identified relate to our (i) lack of financial reporting policies and procedures that are commensurate with U.S. GAAP and SEC reporting and compliance requirements, (ii) lack of sufficient controls for properly tracking the shipping records of the AAVs, and (iii) lack of monitoring of the collection of accounts receivable on a timely basis.

We implemented the following measures to improve our internal control over financial reporting to address the identified material weaknesses respectively:

- For our lack of financial reporting policies and procedures that are commensurate with U.S. GAAP and SEC reporting and compliance requirements, we (i) hired additional accounting and financial reporting personnel with U.S. GAAP and SEC reporting experience; (ii) provided continuous and appropriate training to the accounting and financial reporting personnel, especially the training related to US GAAP, and SEC rules and regulations; (iii) developed a set of accounting policies, which document the current US GAAP accounting standards and technical accounting guidance that are applicable to our business; and (iv) formalized a period-end closing process to prepare financial statements and related disclosures in compliance with US GAAP and SEC financial reporting requirements.
- For our lack of sufficient controls for properly tracking the shipping records of the AAVs, we (i) replaced the logistics service provider with a reputable and qualified vendor; (ii) optimized the approval process with detailed delivery information and with cross-departmental and multi-level personnel's approval and review before delivery; (iii) strengthened the delivery note with relevant parties' confirmation with signature, date and further evidenced by stamp from the logistics service provider; (iv) developed a detailed delivery ledger to control the delivery information; and (v) reconciled monthly with the logistics service provider on the delivery ledger. We have implemented and reinforced the above key controls for recording and tracking the shipping records of AAVs accurately and timely

- For our lack of monitoring of the collection of accounts receivable on a timely basis, we implemented controls on (i) issuance of debit note to our customers to notify and acknowledge the payment terms and schedule under the signed contracts; (ii) issuance of letter of collection for those customers with late payment to claim the outstanding and past-due payments on a quarterly basis ; (iii) negotiation with customers with seriously past-due payments over the outstanding balance and signed the letter of payment plan. We also strengthened finance department's monitoring control over the collection of accounts receivable through quarterly assessment with sales department.

The implementation of the foregoing measures has remediated our material weakness relating to our lack of sufficient controls for properly tracking the shipping records of the AAVs. However, these measures did not fully address all material weaknesses in internal control over financial reporting, and we concluded that the material weakness relating to our lack of financial reporting policies and procedures that are commensurate with U.S. GAAP and SEC reporting requirements and lack of monitoring of the collection of accounts receivable on a timely basis still existed as of December 31, 2022. Our failure to remediate the material weaknesses or our failure to discover and address any other control deficiencies could result in misstatements in our financial statements and impair our ability to comply with applicable financial reporting requirements and related regulatory filings on a timely basis. Moreover, ineffective internal control over financial reporting could significantly hinder our ability to prevent fraud.

We are subject to the Sarbanes-Oxley Act of 2002. Section 404 of the Sarbanes-Oxley Act, or Section 404, requires that we include a report from management on the effectiveness of our internal control over financial reporting in our annual report on Form 20-F beginning with our annual report for the fiscal year ended December 31, 2020. In addition, once we cease to be an "emerging growth company" as such term is defined in the JOBS Act, our independent registered public accounting firm must attest to and report on the effectiveness of our internal control over financial reporting. Moreover, 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 an adverse opinion on the effectiveness of internal control over financial reporting because of the existence of a material weakness 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. In addition, 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. We may be unable to timely complete our evaluation testing and any required remediation.

During the course of documenting and testing our internal control procedures, in order to satisfy the requirements of Section 404, we may identify other weaknesses and deficiencies in our internal control over financial reporting. If we fail to maintain the effectiveness of our internal control over financial reporting, 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. Generally speaking, if we fail to achieve and maintain an effective internal control environment, it could result in material misstatements in our financial statements and could also impair our ability to comply with applicable financial reporting requirements and related regulatory filings on a timely basis. As a result, our businesses, financial condition, results of operations and prospects, as well as the trading price of the ADSs, may be materially and adversely affected. 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. We may also be required to restate our financial statements from prior periods.

It may be difficult for overseas authorities to conduct investigations or collect evidence within China.

Shareholder claims or regulatory investigations that are common in the United States generally are difficult to pursue as a matter of law or practicality in China. For example, in China, there are significant legal and other obstacles to providing information needed for regulatory investigations or litigations initiated outside China. Although the authorities in China may establish a regulatory cooperation mechanism with the securities regulatory authorities of another country or region to implement cross-border supervision and administration, such cooperation with the securities regulatory authorities in the United States may not be efficient in the absence of mutual and practical cooperation mechanism. Furthermore, according to Article 177 of the PRC Securities Law, which became effective in March 2020, no overseas authorities, including the SEC, the PCAOB, and the U.S. Department of Justice, can directly conduct investigation or evidence collection activities within the PRC and no entity or individual in China may provide documents and information relating to securities business activities to overseas authorities without PRC government approval. On August 26, 2022, the PCAOB signed a Statement of Protocol with the China Securities Regulatory Commission and the Ministry of Finance of the People's Republic of China, taking the first step toward opening access for the PCAOB to inspect and investigate registered public accounting firms headquartered in mainland China and Hong Kong. The Statement of Protocol gives the PCAOB sole discretion to select the firms, audit engagements and potential violations it inspects and investigates and put in place procedures for PCAOB inspectors and investigators to view complete audit work papers with all information included and for the PCAOB to retain information as needed. In addition, the Statement of Protocol grants the PCAOB direct access to interview and take testimony from all personnel associated with the audits the PCAOB inspects or investigates. On December 15, 2022, the PCAOB issued a report that vacated its December 16, 2021 determination that the positions taken by authorities in mainland China and Hong Kong prevented it from inspecting and investigating completely registered public accounting firms headquartered in those jurisdictions. However, the PCAOB may still lose such access to inspect and investigate completely accounting firms in mainland China and Hong Kong in the future. As of now, the general inability for overseas authorities to directly conduct investigation or evidence collection activities within China may further increase difficulties faced by you in protecting your interests.

Risks Relating to Our Corporate Structure

If the PRC government finds that the contractual arrangements between the WFOE, the VIE and the VIE's shareholders do not comply with PRC regulations relating to the relevant industries, or if these regulations or the interpretation of existing regulations change in the future, we could be subject to severe penalties or be forced to relinquish our interests in those operations.

In January 2016, we obtained a controlling financial interest in the VIE because the WFOE entered into a series of contractual arrangements with the VIE and the VIE's shareholders, which enable us to (i) have the power to direct significant activities of the VIE, (ii) receive economic benefits from the VIE that potentially could be significant to the VIE, and (iii) have an exclusive option to purchase all or part of the equity interests and assets in the VIE, when and to the extent permitted by PRC laws. As a result of these contractual arrangements, we are considered the primary beneficiary of the VIE and the VIE's subsidiaries and thus consolidate their financial results under U.S. GAAP. See "Item 4. Information on the Company—C. Organizational Structure" for further details.

Our PRC legal counsel, AllBright Law Offices, based on its understanding of the relevant laws and regulations, is of the opinion that (i) the ownership structure of the WFOE, the VIE and the VIE's subsidiaries are in compliance with applicable PRC laws or regulations, and (ii) such contractual arrangements constitute valid, legal and binding obligations enforceable against each party of such agreements in accordance with the terms of each agreement from their respective effective dates to the date of this annual report, and will not result in any violation of PRC laws or regulations currently in effect. However, our PRC legal counsel has also advised us that there are substantial uncertainties regarding the interpretation and application of current and future PRC laws, regulations and rules. Accordingly, the PRC regulatory authorities may take a view that is contrary to the opinion of our PRC legal counsel.

If we or the VIE are found to be in violation of any existing or future PRC laws or regulations, or fail to obtain or maintain any of the required permits or approvals, the relevant PRC regulatory authorities would have broad discretion to take action in dealing with such violations or failures, including:

- revoking the business licenses and/or operating licenses of such entities;

- shutting down our servers or blocking our website, or discontinuing or placing restrictions or onerous conditions on our operation through any transactions between the WFOE and the VIE;
- imposing fines, confiscating the income from the WFOE or the VIE, or imposing other requirements with which we or the VIE may not be able to comply;
- requiring us to restructure our ownership structure or operations, including terminating the contractual arrangements with the VIE and deregistering the equity pledges of the VIE, which in turn would affect our ability to consolidate, derive economic interests from, or to direct the significant activities of the VIE;
- restricting or prohibiting our use of the proceeds of our securities offerings to finance our business and operations in China, and taking other regulatory or enforcement actions that could be harmful to our business;
- confiscating any of our income deemed to be obtained through illegal operations;
- discontinuing or placing restrictions or onerous conditions on our operations;
- imposing additional conditions or requirements with which we may not be able to comply; or
- taking other regulatory or enforcement actions against us that could be harmful to our business.

The imposition of any of these penalties would result in a material and adverse effect on our ability to conduct our business. In addition, it is unclear what impact the PRC government actions would have on us and on our ability to consolidate the financial results of the VIE in our consolidated financial statements, if the PRC government authorities were to find our legal structure and contractual arrangements to be in violation of PRC laws and regulations. If the imposition of any of these government actions causes us to lose our right to direct the activities of the VIE or our right to receive substantially all the economic benefits and residual returns from the VIE and we are not able to restructure our ownership structure and operations in a satisfactory manner, we would no longer be able to direct the significant activities of over or consolidate the financial results of the VIE in our consolidated financial statements. Either of these results, or any other significant penalties that might be imposed on us in this event, would have a material adverse effect on our financial condition and results of operations.

Our business may be significantly affected by the Foreign Investment Law.

On March 15, 2019, the National People's Congress promulgated the Foreign Investment Law, which took effect on January 1, 2020 and replaced the trio of existing laws regulating foreign investment in China, namely, the PRC Equity Joint Venture Law, the PRC Cooperative Joint Venture Law and the Wholly Foreign-owned Enterprise Law, together with their implementation rules and ancillary regulations. Uncertainties still exist in relation to the interpretation and implementation of the Foreign Investment Law. The Foreign Investment Law does not explicitly classify whether variable interest entities that are controlled via contractual arrangements would be deemed as foreign invested enterprises if they are ultimately "controlled" by foreign investors. However, it has a catch-all provision under definition of "foreign investment" to include investments made by foreign investors in China through means stipulated by laws or administrative regulations or other methods prescribed by the State Council. Therefore, it still leaves leeway for future laws, administrative regulations or provisions to provide for contractual arrangements as a form of foreign investment.

The Foreign Investment Law grants foreign invested entities the same treatment as PRC domestic entities, except for those foreign invested entities that operate in industries deemed to be either “restricted” or “prohibited” in the “negative list” to be published. The Foreign Investment Law provides that only foreign invested entities operating in foreign restricted or prohibited industries will require entry clearance and other approvals that are not required by PRC domestic entities or foreign invested entities operating in other industries. Pursuant to the latest version of the “negative list,” namely, the Special Management Measures (Negative List) for the Access of Foreign Investment (2021), which became effective on January 1, 2022, our principal business does not fall into the “restricted” or “prohibited” categories. However, we cannot assure you that the “negative list” will not be updated in the future in any way adverse to our business. In the event that the VIE’s and/or its subsidiaries’ operations in the PRC are not treated as domestic investment and the contractual arrangement between the WFOE, the VIE and the VIE’s shareholders are classified as foreign investment in the “restricted” or “prohibited” industry in the “negative list” under the Foreign Investment Law, such contractual arrangements may be deemed as invalid and illegal, and we may be required to unwind such contractual arrangements and/or deconsolidate the financial results of the VIE and the VIE’s subsidiaries under U.S. GAAP.

Furthermore, if future laws, administrative regulations or provisions mandate further actions to be taken by companies with respect to existing contractual arrangements, we may face substantial uncertainties as to whether we can complete such actions in a timely manner, or at all. In addition, the Foreign Investment Law provides that existing foreign invested enterprises established according to the existing laws regulating foreign investment may maintain their structure and corporate governance within five years after the implementation of the Foreign Investment Law, which means that we may be required to adjust the structure and corporate governance of certain of our PRC entities then. Failure to take timely and appropriate measures to cope with any of these or similar regulatory compliance challenges could materially and adversely affect our current corporate structure, corporate governance and business operations.

We rely on contractual arrangements with the VIE and the VIE’s shareholders for certain business operations in the PRC, which may not be as effective as direct ownership in providing operational control.

The VIE and its subsidiaries accounted for 19.6%, 0.4% and 0.01% of our consolidated revenues for the years ended December 31, 2020, 2021 and 2022, respectively. While we do not expect the VIE and the VIE’s subsidiaries to generate a significant portion of revenue on a consolidated basis, we have relied on and expect to continue to rely on contractual arrangements with the WFOE, the VIE and the VIE’s shareholders for certain business operations in the PRC. These contractual arrangements may not be as effective as direct ownership in providing us with over the power to direct the significant activities of the VIE. For example, the VIE and the VIE’s shareholders could breach their contractual arrangements with us by, among other things, failing to conduct the operations of the VIE in an acceptable manner or taking other actions that are detrimental to our interests.

If we had direct ownership in the VIE, we would be able to exercise our rights as shareholders to effect changes in the directors and senior management of the VIE, which in turn could implement changes, subject to any applicable fiduciary obligations, at the management and operational level. However, under the current contractual arrangements, we rely on the performance by the VIE and the VIE’s shareholders of their respective obligations under the contracts to direct the significant activities of the VIE. The VIE’s shareholders may act in a manner against the best interests of our company and may breach their obligations under these contracts. Such risks exist throughout the period in which we intend to operate certain portions of our business through the contractual arrangements with the VIE. If any dispute relating to these contracts remains unresolved, we will have to enforce our rights under these contracts through the operations of PRC laws and arbitrations, litigations and other legal proceedings and therefore will be subject to uncertainties in the PRC legal system. See “Item 3. Key Information—D. Risk Factors—Risks Relating to Our Corporate Structure—Any failure by the VIE or the VIE’s shareholders to perform their obligations under our contractual arrangements with them would have a material and adverse effect on our business.” Therefore, our contractual arrangements with the VIE may not be as effective in ensuring our power to direct the significant activities of the VIE as direct ownership in the VIE would be.

Any failure by the VIE or the VIE's shareholders to perform their obligations under our contractual arrangements with them would have a material and adverse effect on our business.

The WFOE has entered into a series of contractual arrangements with the VIE and the VIE's shareholders. For a description of these contractual arrangements, see "Item 4. Information on the Company—C. Organizational Structure." If the VIE or the VIE's shareholders fail to perform their respective obligations under the contractual arrangements, we may have to incur substantial costs and expend additional resources to enforce such arrangements. We may also have to rely on legal remedies under PRC laws, including seeking specific performance or injunctive relief, and claiming damages, which may be difficult to enforce under PRC laws. For example, if the shareholders of the VIE refuse to transfer their equity interest in the VIE to us or our designee if we exercise the purchase option pursuant to these contractual arrangements, or if they otherwise act in bad faith toward us, then we may have to take legal actions to compel them to perform their contractual obligations.

All of the agreements under our contractual arrangements are governed by PRC laws and provide for the resolution of disputes through arbitration in China. Accordingly, these contracts would be interpreted in accordance with PRC laws and any disputes would be resolved in accordance with PRC legal procedures. The legal system in the PRC is not as developed as in some 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. See "Item 3. Key Information—D. Risk Factors—Risks Relating to Doing Business in China—Uncertainties in the interpretation and enforcement of PRC laws and regulations could limit the legal protections available to you and us." Meanwhile, there are very few precedents and little formal guidance as to how contractual arrangements in the context of a VIE should be interpreted or enforced under PRC laws. There remain significant uncertainties regarding the ultimate outcome of such arbitration should legal action become necessary. In addition, under PRC laws, rulings by arbitrators are final, parties cannot appeal the arbitration results in courts, and if the losing parties fail to carry out the arbitration awards within a prescribed time limit, the prevailing parties may only enforce the arbitration awards in PRC courts through arbitration award recognition proceedings, which would require additional expenses and delays. In the event we are unable to enforce these contractual arrangements, or if we suffer significant delays or other obstacles in the process of enforcing these contractual arrangements, we may not be able to direct the significant activities of the VIE, and our ability to conduct certain business through the VIE may be materially and adversely affected.

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

The shareholders of the VIE are Mr. Weixian Xia and Mr. Shuai Feng, each a senior employee of our company. Conflicts of interest may arise from them in their roles as employees of our company and as shareholders of the VIE. The VIE's shareholders may breach, or cause the VIE to breach, or refuse to renew, the existing contractual arrangements we have with them and the VIE, which would have a material and adverse effect on our ability to direct the significant activities of the VIE and receive economic benefits from them. For example, the shareholders may be able to cause our agreements with the VIE to be performed in a manner adverse to us by, among other things, failing to remit payments due under the contractual arrangements to us on a timely basis. We cannot assure you that when conflicts of interest arise any or all of these shareholders will act in the best interests of our company or such conflicts will be resolved in our favor.

Currently, we do not have any arrangements to address potential conflicts of interest between these shareholders and our company, except that we could exercise our purchase option under the exclusive option agreements with these shareholders to request them to transfer all of their equity interests in the VIE to a PRC entity or individual designated by us, to the extent permitted by PRC laws. The shareholders of the VIE have executed powers of attorney to appoint the WFOE to vote on their behalf and exercise voting rights as shareholders of the VIE, and such rights were reassigned to us in February 2019. If we cannot resolve any conflicts of interest or disputes between us and the shareholders of the VIE, we would have to rely on legal proceedings, which may be expensive, time-consuming and disruptive to our operations. There is also substantial uncertainty as to the outcome of any such legal proceedings.

The shareholders of the VIE may be involved in personal disputes with third parties or other incidents that may have an adverse effect on their respective equity interests in the VIE and the validity or enforceability of our contractual arrangements with them. For example, in the event that any shareholder of the VIE divorces his or her spouse, the spouse may claim that the equity interest of the VIE held by such shareholder is part of their community property and should be divided between such shareholder and his or her spouse. If such claim is supported by the court, the relevant equity interest may be obtained by the shareholder's spouse or another third party who is not subject to obligations under our contractual arrangements, which could result in a loss of our power to direct the significant activities of the VIE. In addition, a judicial freeze was placed on the equity interests of the VIE in connection with an arbitration filed by a third party against Mr. Huazhi Hu, our founder, chairman of the board of directors and chief executive officer, who was also a former shareholder of the VIE. The arbitration arose from a financial dispute between the third party and Mr. Huazhi Hu, and was unrelated to our company. The third party did not have any claim against the VIE. The VIE was involved in the arbitration only because the third party regarded equity interests of the VIE as potential assets of shareholders of the VIE. The parties to the arbitration have reached a settlement. In March 2021, the third party filed a petition with the court and the judicial freeze on the VIE's equity interests had been released. In addition to the aforementioned arbitration, in October 2020, the VIE paid a guarantee deposit to a court in Guangzhou, China to lift the judicial freeze. For details, see "Item 7. Major Shareholders and Related Party Transactions—B. Related Party Transactions." If any of the equity interests of the VIE is similarly claimed by a third party with whom the current contractual arrangements are not binding, we could lose our power to direct the significant activities of the VIE or have to maintain such power by incurring unpredicted costs, which could cause significant disruption to our business and operations and harm our financial condition and results of operations.

Contractual arrangements in relation to the VIE may be subject to scrutiny by the PRC tax authorities and they may determine that we or the VIE and the VIE's subsidiaries, owe additional taxes, which could negatively affect our financial condition and the value of your investment.

Under applicable PRC laws and regulations, arrangements and transactions among related parties may be subject to audit or challenge by the PRC tax authorities. The Enterprise Income Tax Law requires every enterprise in China to submit its annual enterprise income tax return together with a report on transactions with its related parties to the relevant tax authorities. The tax authorities may impose reasonable adjustments on taxation if they have identified any related party transactions that are inconsistent with arm's length principles. We may face material and adverse tax consequences if the PRC tax authorities determine the contractual arrangements among the WFOE, the VIE and the VIE's shareholders were not entered into on an arm's length basis in such a way as to result in an impermissible reduction in taxes under applicable PRC laws, rules and regulations, and adjust the income of the VIE in the form of a transfer pricing adjustment. A transfer pricing adjustment could, among other things, result in a reduction of expense deductions recorded by the VIE for PRC tax purposes, which could increase our tax expenses. In addition, the PRC tax authorities may impose late payment fees and other penalties on the VIE for the adjusted but unpaid taxes according to the applicable regulations. Our financial position could be materially and adversely affected if the VIE's tax liabilities increase or if it is required to pay late payment fees and other penalties.

We may lose the ability to use and enjoy assets held by the VIE that are material to certain business operations in the PRC if the VIE goes bankrupt or becomes subject to a dissolution or liquidation proceeding.

As part of our contractual arrangements with the VIE, the VIE and the VIE's subsidiaries hold certain assets that are material to certain business operations in the PRC, including permits, domain names and IP rights, operating licenses, intangible assets and fixed assets. If the VIE goes bankrupt and all or part of its 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. Under the contractual arrangements, the VIE may not, in any manner, sell, transfer, mortgage or dispose of its assets or legal or beneficial interests in the business without our prior consent. If our consolidated affiliated entity undergoes a voluntary or involuntary liquidation proceeding, the independent third-party creditors may claim rights to some or all of these assets, thereby hindering our ability to operate our business, which could materially and adversely affect our business, financial condition and results of operations.

Our dual-class share structure with different voting rights will limit your ability to influence corporate matters and could discourage others from pursuing any change of control transactions that holders of our Class A ordinary shares and ADSs may view as beneficial.

Our authorized share capital is divided into Class A ordinary shares and Class B ordinary shares. In respect of matters requiring the votes of shareholders, holders of Class B ordinary shares are entitled to ten votes per share, while holders of Class A ordinary shares are entitled to one vote per share based on our dual-class share structure. Each Class B ordinary share is convertible into one Class A ordinary share at any time by its holder, while Class A ordinary shares are not convertible into Class B ordinary shares under any circumstances. Upon any sale, transfer, assignment or disposition of any Class B ordinary shares by their holder or a change of ultimate beneficial ownership of any Class B ordinary share to any person other than our founder, Mr. Huazhi Hu, or an affiliate controlled by our founder, such Class B ordinary shares shall be automatically and immediately converted into the same number of Class A ordinary shares.

As of March 31, 2023, Mr. Huazhi Hu, our founder, chairman of the board of directors and chief executive officer, beneficially owned all of our issued and outstanding Class B ordinary shares. These Class B ordinary shares constituted approximately 32.3% of our total issued and outstanding share capital and 82.7% of the aggregate voting power of our total issued and outstanding share capital as of March 31, 2023. See "Item 6. Directors, Senior Management and Employees—E. Share Ownership."

Although we have no current plan to issue additional Class B ordinary shares, our board of directors has the authority without further action by our shareholders to issue additional Class B ordinary shares, which will further dilute the voting power of our Class A ordinary shareholders. As a result of the dual-class share structure and the concentration of ownership, our founder has considerable influence over matters such as mergers, consolidations and the sale of all or substantially all of our assets, election of directors, amendments to organizational documents and other significant corporate actions. Our founder may take actions that are not in the best interest of our other shareholders. This concentration of ownership may discourage, delay or prevent a change in control of our company, which could have the effect of depriving our other shareholders of the opportunity to receive a premium for their shares as part of a sale of our company and may reduce the price of our ADSs. This concentrated control will limit your ability to influence corporate matters and could discourage others from pursuing any potential merger, takeover or other change of control transactions that holders of Class A ordinary shares and ADSs may view as beneficial.

In addition, our founder will continue to be able to control all matters submitted to our shareholders for approval even if his shareholdings represent substantially less than a majority of our outstanding common shares. This concentrated control will limit your ability to influence corporate matters for the foreseeable future, and, as a result, the market price of our Class A common shares could be adversely affected.

In July 2017, FTSE Russell and Standard & Poor's announced that they would cease to allow most newly public companies utilizing dual- or multi-class capital structures to be included in certain of their indices. Affected indices include the Russell 2000 and the S&P 500, S&P MidCap 400 and S&P SmallCap 600, which together comprise the S&P Composite 1500. Under the announced policies, our dual-class share structure would make us ineligible for inclusion in any of these indices, and as a result, mutual funds, exchange-traded funds and other investment vehicles that attempt to passively track these indices will not be investing in our shares, which may depress these valuations or depress our trading volume compared to those of other similar companies that are included in these indices.

Risks Relating to Doing Business in China

The PRC government's significant oversight over our and the VIE's business operation could result in a material adverse change in our operations and the value of the ADSs.

We conduct business operations in China primarily through our PRC subsidiaries. Our and the VIE's operations in China are governed by PRC laws and regulations. The PRC government's significant oversight over our and the VIE's business operation could result in a material adverse change in our and the VIE's operations and the value of the ADSs. The Chinese government may intervene or influence our operations at any time, or may exert more control over offerings conducted overseas and/or foreign investment in China-based issuers, which could result in a material change in our operations and/or the value of the ADSs. Any actions by the Chinese government to exert more oversight and control over offerings that are conducted overseas and/or foreign investment in China-based issuers could significantly limit or completely hinder our ability to offer or continue to offer securities to investors and cause the value of such securities to significantly decline or become worthless.

There are substantial uncertainties regarding the interpretation and application of PRC laws and regulations, including, but not limited to, the laws and regulations governing our and the VIE's business, or the enforcement and performance of our contractual arrangements with the VIE. These laws and regulations may be subject to change, the enforcement of laws and regulations in China could be uncertain and the rules and policies in China may change quickly with little advance notice, which could result in a material adverse change in our operations and the value of the ADSs. New laws and regulations that affect existing and proposed future businesses may also be applied retroactively. Due to the uncertainty and complexity of the regulatory environment, we cannot assure you that we and the VIE would always be in full compliance with applicable laws and regulations, the violation of which may have adverse effect on our and the VIE's business and our reputation.

Uncertainties in the interpretation and enforcement of PRC laws and regulations could limit the legal protections available to you and us.

The PRC legal system is a civil law system based on written statutes. Unlike the common law system, prior court decisions may be cited for reference but have limited precedential value in China. Our PRC legal system is evolving rapidly, but its current slate of laws may not be sufficient to cover all aspects of the economic activities in China, including such activities that relate to or have an impact on our business. Implementation and interpretations of laws, regulations and rules are not always undertaken in a uniform matter and enforcement of these laws, regulations and rules involves uncertainties.

From time to time, we, the VIE or the VIE's subsidiaries may have to resort to administrative and court proceedings to enforce our legal rights. However, since PRC administrative and court authorities have significant discretion in interpreting and implementing statutory and contractual terms, it may be more difficult to evaluate the outcome of administrative and court proceedings and the level of protection we, the VIE or the VIE's subsidiaries enjoy than in more developed legal systems. Furthermore, the PRC legal system is based in part on government policies and internal rules (some of which are not published in a timely manner or at all) that may have a retroactive effect. As a result, we, the VIE or the VIE's subsidiaries may not always be aware of any potential violation of these policies and rules until sometime after the violation. Such uncertainties, including unpredictability towards the scope and effect of our, the VIE or the VIE's subsidiaries' contractual, property (including intellectual property) and procedural rights, and any failure to respond to changes in the regulatory environment in China could materially and adversely affect our business and impede our ability to continue our operations.

We may be adversely affected by the complexities, uncertainties and changes in PRC regulations on technology companies.

The PRC government imposes licensing and permit requirements for companies in the technology industry. These laws, regulations and even such announcements 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.

In addition, our mobile application is regulated by the Administrative Provisions on Mobile Internet Applications Information Services, or the App Provisions, promulgated by the Cyberspace Administration of China, or the CAC, effective on August 1, 2016. According to the App Provisions, the providers of mobile applications shall not create, copy, publish or distribute information and content that is prohibited by laws and regulations. However, we cannot assure that all the information or content displayed on, retrieved from or linked to our mobile applications complies with the requirements of the App Provisions at all times. If our mobile applications were found to be violating the App Provisions, we may be subject to administrative penalties, including warnings, service suspensions or removal of our mobile applications from relevant mobile application stores, which may materially and adversely affect our business and operating results.

The interpretation and application of existing PRC laws, regulations and policies and possible new laws, regulations or policies relating to the technology industry, particularly the policies relating to new energy vehicles, 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 or renew our existing licenses or obtain new ones.

Uncertainties exist with respect to the interpretation and implementation of the PRC Foreign Investment Law and its Implementation Regulations and how they may impact the viability of our current corporate structure, corporate governance and business operations.

The National People's Congress approved the *PRC Foreign Investment Law*, or the Foreign Investment Law, on March 15, 2019 and the State Council approved the *Regulation on Implementing the Foreign Investment Law*, or the Implementation Regulations on December 12, 2019, effective from January 1, 2020, to replace prior 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 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. However, since the Foreign Investment Law and the Implementation Regulations are relatively new, uncertainties still exist in relation to its interpretation and implementation. For instance, under the Foreign Investment Law, "foreign investment" refers to the investment activities directly or indirectly conducted by foreign individuals, enterprises or other entities in China. Though it does not explicitly classify contractual arrangements as a form of foreign investment, there is no assurance that foreign investment via contractual arrangement would not be interpreted as a type of indirect foreign investment activities under the definition in the future. In addition, the definition contains a catch-all provision which includes investments made by foreign investors through means stipulated in laws or administrative regulations or other methods prescribed by the State Council. Therefore, it still leaves leeway for future laws, administrative regulations or provisions promulgated by the State Council to provide for contractual arrangements as a form of foreign investment. In any of these cases, it will be uncertain whether our contractual arrangements will be deemed to be in violation of the market access requirements for foreign investment under the PRC laws and regulations. Furthermore, if future laws, administrative regulations or provisions prescribed by the State Council mandate further actions to be taken by companies with respect to existing contractual arrangements, we may face substantial uncertainties as to whether we can complete such actions in a timely manner, or at all. Failure to take timely and appropriate measures to cope with any of these or similar regulatory compliance challenges could materially and adversely affect our current corporate structure, corporate governance and business operations.

The approval of and the filing with the CSRC or other PRC governmental authorities may be required in connection with our future offshore offerings under PRC law and if required, we cannot predict whether or how soon we will be able to obtain such approval or complete such filing.

On February 17, 2023, the CSRC issued rules and regulations concerning the filing management of overseas listing, which came into effect on March 31, 2023. The rules and regulations issued include the Provisional Measures for the Administration of Overseas Issuance and Listing of Securities by Domestic Enterprises, or the New Filing Rules, and five supporting guidelines. The New Filing Rules dictate that enterprises that have been listed overseas prior to March 31, 2023 constitute “Existing Issuers.” Existing Issuers are required to complete filing procedure with the CSRC if and when they pursue any refinancing activities, securities offerings and listings outside of Mainland China, including but not limited to follow-on offerings, secondary listings, and listing by introduction in a different market, unless such securities are issued as equity incentive awards or in connection with conversion of public reserve funds into increased company capital, share dividends or share split. Although we are an Existing Issuer and accordingly are not required to complete filing with the CSRC immediately, we may be subject to the CSRC filing procedures in the future in connection with our refinancing or other activities and, if required, we cannot predict whether we will be able to complete such filing procedures in time or at all. If we fail to complete such filing procedures, we may not conduct refinancing or other activities which are subject to the New Filing Rules, or we would be subject to sanctions by the CSRC or other PRC regulatory authorities. These regulatory authorities may impose fines and penalties on our operations in China, limit our ability to pay dividends outside of China, limit our operating activities in China, delay or restrict the repatriation of the proceeds from our offshore offerings into China or take other actions that could materially and adversely affect our business, financial condition, results of operations, and prospects, as well as the trading price of the ADSs. In addition, given that the New Filing Rules were recently promulgated, there remains substantial uncertainties as to their interpretation, application, and enforcement and how they will affect our operations and our future financing. We cannot guarantee that new rules or regulations promulgated in the future will not impose any additional requirements on us or otherwise tighten the regulations on companies with VIE structures.

The ADSs will be delisted and prohibited from trading in the U.S. under the Holding Foreign Companies Accountable Act, or the HFCAA, if the PCAOB is unable to inspect or fully investigate auditors located in China.

Pursuant to the HFCAA, if the SEC determines that we have filed audit reports issued by a registered public accounting firm that has not been subject to inspections by the PCAOB for two consecutive years, the SEC will prohibit our shares or ADSs from being traded on a national securities exchange or in the over-the-counter trading market in the United States.

On December 16, 2021, the PCAOB issued a report to notify the SEC of its determination that the PCAOB was unable to inspect or investigate completely registered public accounting firms headquartered in mainland China and Hong Kong and our auditor was subject to that determination. On May 26, 2022, the SEC conclusively listed us as a Commission-Identified Issuer under the HFCAA following the filing of our annual report on Form 20-F for the fiscal year ended December 31, 2021. On December 15, 2022, the PCAOB removed mainland China and Hong Kong from the list of jurisdictions where it is unable to inspect or investigate completely registered public accounting firms. For this reason, we do not expect to be identified as a Commission-Identified Issuer under the HFCAA after we file this annual report on Form 20-F for the fiscal year ended December 31, 2022.

Each year, the PCAOB will determine whether it can inspect and investigate completely audit firms in mainland China and Hong Kong, among other jurisdictions. If the PCAOB determines in the future that it no longer has full access to inspect and investigate completely accounting firms in mainland China and Hong Kong and we use an accounting firm headquartered in one of these jurisdictions to issue an audit report on our financial statements filed with the Securities and Exchange Commission, we would be identified as a Commission-Identified Issuer following the filing of the annual report on Form 20-F for the relevant fiscal year. In accordance with the HFCAA, our securities would be prohibited from being traded on a national securities exchange or in the over-the-counter trading market in the United States if we are identified as a Commission-Identified Issuer for two consecutive years in the future. If our shares and ADSs are prohibited from trading in the United States, there is no certainty that we will be able to list on a non-U.S. exchange or that a market for our shares will develop outside of the United States. A prohibition of being able to trade in the United States would substantially impair your ability to sell or purchase the ADSs when you wish to do so, and the risk and uncertainty associated with delisting would have a negative impact on the price of the ADSs. Also, such a prohibition would significantly affect our ability to raise capital on terms acceptable to us, or at all, which would have a material adverse impact on our business, financial condition, and prospects.

Increases in labor costs and enforcement of stricter labor laws and regulations in the PRC may adversely affect our business and our profitability.

China's overall economy and the average wage level in China have increased in recent years and are expected to continue to grow. The average wage level for our employees has also increased in recent years. We expect that our labor costs, including wages and employee benefits, will continue to increase. Unless we are able to pass on these increased labor costs to our customers, our profitability and results of operations may be materially and adversely affected.

In addition, we have been subject to stricter regulatory requirements in terms of entering into labor contracts with our employees and paying various statutory employee benefits, including pensions, housing funds, medical insurance, work-related injury insurance, unemployment insurance and maternity insurance to designated government agencies for the benefit of our employees. Pursuant to the PRC Labor Contract Law and its implementation rules, employers are subject to stricter requirements in terms of signing labor contracts, minimum wages, paying remuneration, determining the term of employee's probation and unilaterally terminating labor contracts. In the event that we decide to terminate some of our employees or otherwise change our employment or labor practices, the PRC Labor Contract Law and its implementation rules may limit our ability to effect those changes in a desirable or cost-effective manner, which could adversely affect our business and results of operations.

In October 2010, the Standing Committee of the National People's Congress promulgated the PRC Social Insurance Law, which came into effect on July 1, 2011. In April 1999, the State Council promulgated the Regulations on the Administration of Housing Funds, which was amended in March 2002. Companies registered and operating in China are required under the Social Insurance Law and the Regulations on the Administration of Housing Funds to, apply for social insurance registration and housing fund deposit registration within 30 days of their establishment and, to pay for their employees' different social insurance including pension insurance, medical insurance, work-related injury insurance, unemployment insurance and maternity insurance to the extent required by law. Recently, the PRC government enhanced its measures relating to social insurance collection, which lead to stricter enforcement. We could be subject to orders by the competent labor authorities for rectification and failure to comply with the orders which may further subject us to administrative fines.

As the interpretation and implementation of labor-related laws and regulations are still evolving, we cannot assure you that our employment practices do not and will not violate labor-related laws and regulations in China, which may subject us to labor disputes or government investigations. We cannot assure you that we have complied or will be able to comply with all labor-related laws and regulations including those relating to obligations to make social insurance payments and contribute to the housing provident funds. We have not fully paid the social insurance payment and housing provident funds for all of our employees as required by applicable PRC regulations. In addition, we have made social insurance payments and contribute to the housing provident funds for some of our employees through the third-party agents, which should be paid by us directly under the applicable PRC regulations. We may be required to make up the contributions for our employees, and may be further subjected to late fees payment and administrative fines, resulting in financial condition and results of operations to be adversely affected.

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

We are a holding company, and we rely on dividends and other distributions on equity paid by our PRC subsidiaries for our cash and financing requirements, including the funds necessary to pay dividends and other cash distributions to our shareholders and service any debt we may incur. If our PRC subsidiaries incur debt on their own behalf in the future, the instruments governing the debt may restrict its ability to pay dividends or make other distributions to us.

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

Our ability to pay dividends is primarily dependent on receiving distributions of funds from our PRC subsidiaries, the VIE and the VIE's subsidiaries. Relevant PRC statutory laws and regulations permit payments of dividends by our PRC subsidiaries, the VIE and the VIE's subsidiaries only out of their retained earnings, if any, as determined in accordance with PRC accounting standards and regulations. The results of operations reflected in the consolidated financial statements prepared in accordance with U.S. GAAP differ from those reflected in the statutory financial statements of our PRC subsidiaries, the VIE and the VIE's subsidiaries.

In response to the persistent capital outflow and the Renminbi's depreciation against the U.S. dollar, the People's Bank of China and the State Administration of Foreign Exchange, or SAFE, have implemented a series of capital control measures, including stricter vetting procedures for China-based companies to remit foreign currency for overseas acquisitions, dividend payments and shareholder loan repayments. The PRC government may continue to strengthen its capital controls, and the WFOE's dividends and other distributions may be subjected to tighter scrutiny in the future. Any limitation on the ability of our PRC subsidiaries to pay dividends or make other distributions to us could materially and adversely limit our ability to grow, make investments or acquisitions that could be beneficial to our business, pay dividends, or otherwise fund and conduct our business.

PRC regulation of loans to and direct investment in PRC entities by offshore holding companies and governmental control of currency conversion may delay or prevent us from using the proceeds of our offshore offerings to make loans to or make additional capital contributions to our PRC subsidiaries, the VIE and the VIE's subsidiaries, which could materially and adversely affect our liquidity and our ability to fund and expand our business.

We are an offshore holding company conducting our operations in China through our PRC subsidiaries, VIE and its subsidiaries. We may make loans to our PRC subsidiaries, VIE and its subsidiaries, or we may make additional capital contributions to our PRC subsidiaries, or we may establish new PRC subsidiaries and make capital contributions to these new PRC subsidiaries, or we may acquire offshore entities with business operations in China in an offshore transaction.

Most of these activities are subject to PRC regulations and approvals. For example, loans by us to our wholly owned PRC subsidiaries to finance their activities cannot exceed statutory limits and must be registered with the local counterpart of the State Administration of Foreign Exchange, or SAFE. If we decide to finance our wholly owned PRC subsidiaries by means of capital contributions, these capital contributions are subject to the requirement of making necessary filings in the Foreign Investment Comprehensive Management Information System and registration with other governmental authorities in China. Due to the restrictions imposed on loans in foreign currencies extended to any PRC domestic companies, we are not likely to make such loans to the VIE, which is a PRC domestic company. SAFE promulgated the *Circular on the Reforming of the Management Method of the Settlement of Foreign Currency Capital of Foreign-invested Enterprises*, or SAFE Circular 19, effective on June 1, 2015, in replacement of the Circular on the Relevant Issues Concerning the Launch of Reforming Trial of the Administration Model of the Settlement of Foreign Currency Capital of Foreign-Invested Enterprises, the Notice From the State Administration of Foreign Exchange on Relevant Issues Concerning Strengthening the Administration of Foreign Exchange Businesses, and the Circular on Further Clarification and Regulation of the Issues Concerning the Administration of Certain Capital Account Foreign Exchange Businesses. According to SAFE Circular 19, the flow and use of the RMB capital converted from foreign currency-denominated registered capital of a foreign-invested company is regulated such that RMB capital may not be used for the issuance of RMB entrusted loans, the repayment of inter-enterprise loans or the repayment of banks loans that have been transferred to a third party. Although SAFE Circular 19 allows RMB capital converted from foreign currency-denominated registered capital of a foreign-invested enterprise to be used for equity investments within China, it also reiterates the principle that RMB capital converted from the foreign currency-denominated capital of a foreign-invested company may not be directly or indirectly used for purposes beyond its business scope. Thus, it is unclear whether SAFE will permit such capital to be used for equity investments in China in actual practice. SAFE promulgated the *Notice of the State Administration of Foreign Exchange on Reforming and Standardizing the Foreign Exchange Settlement Management Policy of Capital Account*, or SAFE Circular 16, effective on June 9, 2016, which reiterates some of the rules set forth in SAFE Circular 19, but changes the prohibition against using RMB capital converted from foreign currency-denominated registered capital of a foreign-invested company to issue RMB entrusted loans to a prohibition against using such capital to issue loans to non-associated enterprises. Violations of SAFE Circular 19 and SAFE Circular 16 could result in administrative penalties. SAFE Circular 19 and SAFE Circular 16 may significantly limit our ability to transfer any foreign currency we hold, including the net proceeds from our securities offerings, to our PRC subsidiaries, which may adversely affect our liquidity and our ability to fund and expand our business in China.

In light of the various requirements imposed by PRC regulations on loans to and direct investment in PRC entities by offshore holding companies, we cannot assure you that we will be able to complete the necessary government registrations or obtain the necessary government approvals on a timely basis, if at all, with respect to future loans by us to our PRC subsidiaries or with respect to future capital contributions by us to our PRC subsidiary. If we fail to complete such registrations or obtain such approvals, our ability to use the proceeds we received from our securities offerings and to capitalize or otherwise fund our PRC operations may be negatively affected, which could materially and adversely affect our liquidity and our ability to fund and expand our business.

PRC regulations relating to the establishment of offshore special purpose vehicles by PRC residents may subject our PRC resident beneficial owners or our PRC subsidiaries to liabilities or penalties, limit our ability to inject capital into our PRC subsidiaries, limit the ability of our PRC liabilities to increase its registered capital or distribute profits to us, or may otherwise adversely affect us.

The SAFE promulgated the *Circular on Relevant Issues Relating to Domestic Resident's Investment and Financing and Round-Trip Investment through Special Purpose Vehicles*, or SAFE Circular 37, in July 2014 that requires PRC residents or entities to register with SAFE or its local branch in connection with their establishment or control of an offshore entity established for the purpose of overseas investment or financing with such PRC residents or entities' legally owned assets or equity interests in domestic enterprises or offshore assets or interests. On February 13, 2015, SAFE issued SAFE Circular No. 13, which took effect on June 1, 2015, pursuant to which, the power to accept SAFE registration was delegated from local SAFE to local qualified banks where the assets or interest in the domestic entity was located. SAFE Circular 37 is issued to replace the Notice on Relevant Issues Concerning Foreign Exchange Administration for PRC Residents Engaging in Financing and Roundtrip Investments via Overseas Special Purpose Vehicles, or SAFE Circular 75.

If our shareholders who are PRC residents or entities do not complete their registration pursuant to SAFE Circular 37 as required, our PRC subsidiaries may be prohibited from distributing their profits and proceeds from any reduction in capital, share transfer or liquidation to us, and we may be restricted in our ability to contribute additional capital to our PRC subsidiaries. Moreover, failure to comply with the SAFE registration described above could result in liability under PRC laws for evasion of applicable foreign exchange restrictions.

We have used our best efforts to notify PRC residents or entities who directly or indirectly hold shares in our Cayman Islands holding company and who are known to us as being PRC residents to complete the foreign exchange registrations. However, we may not be informed of the identities of all the PRC residents or entities holding direct or indirect interest in our company, nor can we compel our beneficial owners to comply with SAFE registration requirements. We cannot assure you that all other shareholders or beneficial owners of ours who are PRC residents or entities have complied with, and will in the future make, obtain or update any applicable registrations or approvals required by, SAFE regulations. Failure by such shareholders or beneficial owners to comply with SAFE regulations, or failure by us to amend the foreign exchange registrations of our PRC subsidiaries, could subject us to fines or legal sanctions, restrict our overseas or cross-border investment activities, limit the ability of our PRC subsidiaries to make distributions or pay dividends to us or affect our ownership structure, which could adversely affect our business and prospects.

The M&A Rules and certain other PRC regulations establish complex procedures for some acquisitions of Chinese companies by foreign investors, which could make it more difficult for us to pursue growth through acquisitions in China.

The *Regulations on Mergers and Acquisitions of Domestic Companies by Foreign Investors*, or the M&A Rules, adopted by six PRC regulatory agencies in August 2006 and amended in September 2009, and some other regulations and rules concerning mergers and acquisitions established additional procedures and requirements that could make merger and acquisition activities by foreign investors more time consuming and complex, including requirements in some instances that shall obtained an approval from the MOFCOM in advance of any change-of-control transaction in which a foreign investor takes control of a PRC domestic enterprise. Moreover, the Anti-Monopoly Law requires that the MOFCOM shall be notified in advance of any concentration of undertaking if certain thresholds are triggered. In addition, the security review rules issued by the MOFCOM that became effective in September 2011 specify that mergers and acquisitions by foreign investors that raise “national defense and security” concerns and mergers and acquisitions through which foreign investors may acquire de facto control over domestic enterprises that raise “national security” concerns are subject to strict review by the MOFCOM, and the rules prohibit any activities attempting to bypass a security review, including by structuring the transaction through a proxy or contractual control arrangement. In the future, we may grow our business by acquiring complementary businesses. Complying with the requirements of the above-mentioned regulations and other relevant rules to complete such transactions could be time consuming, and any required approval processes, including obtaining approval from the MOFCOM or its local counterparts may delay or inhibit our ability to complete such transactions, which could affect our ability to expand our business or maintain our market share.

Future movements in exchange rates between U.S. dollars and Renminbi may adversely affect the value of our ordinary shares or the ADSs.

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 in China and by China's foreign exchange policies. On July 21, 2005, the PRC government changed its decade-old policy of pegging the value of the Renminbi to the U.S. dollar, and the Renminbi appreciated more than 20% against the U.S. dollar over the following three years. Between July 2008 and June 2010, this appreciation halted and the exchange rate between the Renminbi and the U.S. dollar remained within a narrow band. Since June 2010, the Renminbi has fluctuated against the U.S. dollar, at times significantly and unpredictably. On November 30, 2015, the Executive Board of the International Monetary Fund (IMF) completed the regular five-year review of the basket of currencies that make up the Special Drawing Right, or the SDR, and decided that with effect from October 1, 2016, Renminbi is determined to be a freely usable currency and will be included in the SDR basket as a fifth currency, along with the U.S. dollar, the Euro, the Japanese yen and the British pound. With the development of the foreign exchange market and progress towards interest rate liberalization and Renminbi internationalization, the PRC government may in the future announce further changes to the exchange rate system and we cannot assure you that the Renminbi will not appreciate or depreciate significantly in value against the U.S. dollar in the future. 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.

Significant revaluation of the Renminbi may have a material and adverse effect on your investment. For example, if we decide to convert our Renminbi into U.S. dollars for the purpose of making payments for dividends on our ordinary shares or ADSs or for other business purposes, appreciation of the U.S. dollar against the Renminbi would have a negative effect on the U.S. dollar amount available to us.

Very limited hedging options are available in China to reduce our exposure to exchange rate fluctuations. To date, we have not entered into any material hedging transactions in an effort to reduce our exposure to foreign currency exchange risk. While we may decide to enter into hedging transactions in the future, the availability and effectiveness of these hedges may be limited, and we may not be able to adequately hedge our exposure or at all. In addition, our currency exchange losses may be magnified by PRC exchange control regulations that restrict our ability to convert Renminbi into foreign currency.

Governmental control of currency conversion may limit our ability to utilize our operating revenues effectively and affect the value of your investment.

The PRC government imposes controls on the convertibility of the Renminbi into foreign currencies and, in certain cases, the remittance of currency out of China. We receive substantially all of our revenues in Renminbi. Under our current corporate structure, our Cayman Islands holding company may rely on dividend payments from our PRC subsidiaries to fund any cash and financing requirements we may have. Under existing PRC foreign exchange regulations, payments of current account items, including profit distributions, interest payments and trade and service-related foreign exchange transactions, can be made in foreign currencies without prior approval of SAFE if certain procedural requirements are complied with. Specifically, under the existing exchange restrictions, without prior approval of SAFE, cash generated from the operations of our PRC subsidiaries in China may be used to pay dividends to our company. However, approval from or registration with appropriate government authorities is required where Renminbi is to be converted into foreign currency and remitted out of China to pay capital expenses, such as the repayment of loans denominated in foreign currencies. As a result, we need to obtain SAFE approval to use cash generated from the operations of our PRC subsidiaries and consolidated affiliated entities to pay off their respective debt in a currency other than Renminbi owed to entities outside China, or to make other capital expenditure payments outside China in a currency other than Renminbi.

The PRC government has imposed more restrictive foreign exchange policies and stepped-up scrutiny of major outbound capital movements including overseas direct investments. More restrictions and substantial vetting processes are put in place by SAFE to regulate cross-border transactions falling under the capital account. For example, if a person (i) uses Renminbi to pay amounts due that should be settled in a foreign currency or (ii) makes payments in Renminbi on behalf of a third party in exchange for repayments in a foreign currency, such person may be subject to a fine of not more than 30% of the illegal payment. In severe cases, the fine could be increased to 100% of the illegal payment. If any of our shareholders or affiliates to whom SAFE regulations are applicable violates any of the foreign exchange policies, it may be subject to penalties from the relevant PRC authorities. Historically, certain minority shareholders invested in our company through payments in Renminbi to the VIE in lieu of payments in U.S. dollars outside of the PRC. In an uncertain event that we are deemed to have participated in our shareholders' actions that are not in compliance with the relevant foreign exchange policies by the PRC regulatory authorities, we could be subject to restrictions on our ability to convert foreign currencies into Renminbi or vice versa, as well as monetary penalties. If the PRC foreign exchange control system prevents us from converting foreign currencies into Renminbi or vice versa, our ability to obtain sufficient foreign currencies to satisfy our foreign currency demands may be materially and adversely affected. For example, we may not be able to pay dividends in foreign currencies to our shareholders, including holders of the ADSs, and we may also encounter difficulties in remitting proceeds from our overseas financings and our revenue from the transactions with our overseas customers.

Failure to comply with PRC regulations regarding the registration requirements for employee stock ownership plans or share option plans may subject the PRC plan participants or us to fines and other legal or administrative sanctions.

Pursuant to SAFE Circular 37, PRC residents who participate in share incentive plans in overseas non-publicly-listed companies may submit applications to SAFE or its local branches for the foreign exchange registration with respect to offshore special purpose companies. In the meantime, our directors, executive officers and other employees who are PRC citizens or who are non-PRC residents residing in the PRC for a continuous period of not less than one year, and who have been granted incentive share awards by us, may follow the Notices on Issues Concerning the Foreign Exchange Administration for Domestic Individuals Participating in Stock Incentive Plan of Overseas Publicly-Listed Company, promulgated by the SAFE in 2012. Pursuant to the 2012 SAFE notices, PRC citizens and non-PRC citizens who reside in China for a continuous period of not less than one year who participate in any stock incentive plan of an overseas publicly listed company, are required to register with SAFE through a domestic qualified agent, which could be the PRC subsidiary of such overseas listed company, and complete certain other procedures. In addition, an overseas entrusted institution must be retained to handle matters in connection with the exercise or sale of stock options and the purchase or sale of shares and interests. We and our executive officers and other employees who are PRC citizens or who reside in the PRC for a continuous period of not less than one year and who have been granted restricted share units are subject to these regulations as our company has become an overseas listed company. Failure to complete the SAFE registrations may subject us to fines, and legal sanctions and may also limit our ability to contribute additional capital into our PRC subsidiaries and limit the ability of our PRC subsidiaries to distribute dividends to us. We also face regulatory uncertainties that could restrict our abilities to adopt additional incentive plans for our directors, executive officers and employees under PRC laws.

The State Administration of Taxation, or SAT, has issued certain circulars concerning employee share options and restricted shares. If our employees fail to pay or we fail to withhold their income taxes according to relevant laws and regulations, we may face sanctions imposed by the tax authorities or other PRC governmental authorities.

Discontinuation of any of the preferential tax treatments and government subsidies or imposition of any additional taxes and surcharges could adversely affect our financial condition and results of operations.

Each of the WFOE and the VIE is currently qualified as a high and new technology enterprise, or HNTE, and as such is eligible for a 15% preferential tax rate, which will expire in December 2022 and December 2024, respectively. The discontinuation of any of the preferential income tax treatment that we currently enjoy could have a material and adverse effect on our result of operations and financial condition. We cannot assure you that we will be able to maintain or lower our current effective tax rate in the future.

Our PRC subsidiaries have received various financial subsidies from PRC local government authorities. The financial subsidies result from discretionary incentives and policies adopted by PRC local government authorities. The discontinuation of such financial subsidies or imposition of any additional taxes could adversely affect our financial condition and results of operations.

If we are classified as a PRC resident enterprise for PRC income tax purposes, such classification could result in unfavorable tax consequences to us and our non-PRC shareholders or ADS holders.

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

We believe none of our entities outside of China is a PRC resident enterprise for PRC tax purposes. However, the tax resident status of an enterprise is subject to determination by the PRC tax authorities and uncertainties remain with respect to the interpretation of the term “de facto management body.” If the PRC tax authorities determine that we are a PRC resident enterprise for enterprise income tax purposes, we will be subject to the enterprise income tax on our global income at the rate of 25% and we will be required to comply with PRC enterprise income tax reporting obligations. In addition, gains realized sale or other disposition of the ADSs or ordinary shares may be subject to PRC tax at a rate of 10% (in the case of non-PRC enterprise) or 20% in the case of non-PRC individuals (in each case, subject to the provisions of any applicable tax treaty), if such gains are deemed to be from PRC sources. These rates may be reduced by an applicable tax treaty, but it is unclear whether non-PRC shareholders of the WFOE would be able to claim the benefits of any tax treaties between their country of tax residence and the PRC in the event that the WFOE is treated as a PRC resident enterprise. Any such PRC tax may reduce the returns on your investment in the ADSs.

We may not be able to obtain certain benefits under the relevant tax treaty on dividends paid by our PRC subsidiaries to us through our Hong Kong subsidiary.

We are a holding company incorporated under the laws of the Cayman Islands and as such rely on dividends and other distributions on equity from our PRC subsidiaries to satisfy part of our liquidity requirements. Pursuant to the PRC Enterprise Income Tax Law, a withholding tax rate of 10% currently applies to dividends paid by a PRC “resident enterprise” to a foreign enterprise investor, unless any such foreign investor’s jurisdiction of incorporation has a tax treaty with China that provides for preferential tax treatment. Pursuant to the *Arrangement between the Mainland China and the Hong Kong Special Administrative Region for the Avoidance of Double Taxation and Tax Evasion on Income*, such withholding tax rate may be lowered to 5% if a Hong Kong resident enterprise owns no less than 25% of a PRC enterprise. Furthermore, the *Administrative Measures for Non-Resident Enterprises to Enjoy Treatments under Tax Treaties*, which became effective in August 2015, require non-resident enterprises to determine whether they are qualified to enjoy the preferential tax treatment under the tax treaties and file relevant report and materials with the tax authorities. There are also other conditions for enjoying the reduced withholding tax rate according to other relevant tax rules and regulations. See “Item 10. Additional Information—E. Taxation—PRC Taxation.” As of December 31, 2022, our PRC subsidiaries and the VIE located in the PRC reported accumulated loss and therefore they had no retained earnings for offshore distribution. In the future, we intend to re-invest all earnings, if any, generated from our PRC subsidiaries for the operation and expansion of our business in China. Should our tax policy change to allow for offshore distribution of our earnings, we would be subject to a significant withholding tax. We cannot assure you that our determination regarding our qualification to enjoy the preferential tax treatment could be challenged by the relevant tax authority and we may be unable to complete the necessary filings with the relevant tax authority and enjoy the preferential withholding tax rate of 5% under the arrangement with respect to dividends to be paid by our PRC subsidiary to our Hong Kong subsidiary.

We face uncertainty with respect to indirect transfers of equity interests in PRC resident enterprises by their non-PRC holding companies.

In February 2015, the State Administration of Taxation issued the *Public Notice Regarding Certain Enterprise Income Tax Matters on Indirect Transfer of Properties by Non-Resident Enterprises*, or SAT Public Notice 7. SAT Public Notice 7 extends its tax jurisdiction to not only indirect transfers but also transactions involving transfer of other taxable assets, through the offshore transfer of a foreign intermediate holding company. In addition, SAT Public Notice 7 provides certain criteria on how to assess reasonable commercial purposes and has introduced safe harbors for internal group restructurings and the purchase and sale of equity through a public securities market. SAT Public Notice 7 also brings challenges to both the foreign transferor and transferee (or other person who is obligated to pay for the transfer) of the taxable assets. Where a non-resident enterprise conducts an “indirect transfer” by transferring the taxable assets indirectly by disposing of the equity interests of an overseas holding company, the non-resident enterprise being the transferor, or the transferee, or the PRC entity which directly owned the taxable assets must report to the relevant tax authority such indirect transfer. Using a “substance over form” principle, the PRC tax authority may disregard the existence of the overseas holding company if it lacks a reasonable commercial purpose and was established for the purpose of reducing, avoiding or deferring PRC tax. As a result, gains derived from such indirect transfer may be subject to PRC enterprise income tax, and the transferee or other person who is obligated to pay for the transfer is obligated to withhold the applicable taxes, currently at a rate of 10% (subject to available preferential tax treatment under applicable tax treaties or similar arrangements) for the transfer of equity interests in a PRC resident enterprise. On October 17, 2017, the SAT issued the Announcement of the State Administration of Taxation on Issues Concerning the Withholding of Non-resident Enterprise Income Tax at Source, or SAT Bulletin 37, which came into effect on December 1, 2017. The SAT Bulletin 37 further clarifies the practice and procedure of the withholding of nonresident enterprise income tax.

We face uncertainties on the reporting and consequences of future private equity financing transactions, share exchanges or other transactions involving the transfer of shares in our company by investors that are non-PRC resident enterprises. The PRC tax authorities may pursue such non-resident enterprises with respect to a filing or the transferees with respect to withholding obligation, and request our PRC subsidiaries to assist in the filing. As a result, we and non-resident enterprises in such transactions may risk being subject to filing obligations or being taxed under SAT Public Notice 7 and SAT Bulletin 37, and may be required to expend valuable resources to comply with them or to establish that we and our non-resident enterprises should not be taxed under these regulations, which may have a material adverse effect on our financial condition and results of operations.

If the custodians or authorized users of controlling non-tangible assets of our company, including our corporate chops and seals, fail to fulfill their responsibilities, or misappropriate or misuse these assets, our business and operations could be materially and adversely affected.

Under PRC law, legal documents for corporate transactions are executed using the chops or seal of the signing entity or with the signature of a legal representative whose designation is registered and filed with the relevant branch of the Administration of Market Regulation.

Although we usually utilize chops to enter into contracts, the designated legal representatives of each of our PRC subsidiaries, VIE and its subsidiaries have the apparent authority to enter into contracts on behalf of such entities without chops and bind such entities. All designated legal representatives of our PRC subsidiaries, variable interest entity and its subsidiaries are members of our senior management team who have signed employment agreements with us or our PRC subsidiaries, VIE and its subsidiaries under which they agree to abide by various duties they owe to us. In order to maintain the physical security of our chops and chops of our PRC entities, we generally store these items in secured locations accessible only by the authorized personnel in the legal or finance department of each of our subsidiaries, VIE and its subsidiaries. Although we monitor such authorized personnel, there is no assurance such procedures will prevent all instances of abuse or negligence.

Accordingly, if any of our authorized personnel misuse or misappropriate our corporate chops or seals, we could encounter difficulties in maintaining control over the relevant entities and experience significant disruption to our operations. If a designated legal representative obtains control of the chops in an effort to obtain control over any of our PRC subsidiaries, VIE or its subsidiaries, we or our PRC subsidiaries, VIE and its subsidiaries would need to pass a new shareholders or board resolution to designate a new legal representative and we would need to take legal action to seek the return of the chops, apply for new chops with the relevant authorities, or otherwise seek legal redress for the violation of the representative's fiduciary duties to us, which could involve significant time and resources and divert management attention away from our regular business. In addition, the affected entity may not be able to recover corporate assets that are sold or transferred out of our control in the event of such a misappropriation if a transferee relies on the apparent authority of the representative and acts in good faith.

The PCAOB had historically been unable to inspect our auditor in relation to their audit work performed for our financial statements and the inability of the PCAOB to conduct inspections of our auditor in the past has deprived our investors with the benefits of such inspections.

Our auditor, the independent registered public accounting firm that issues the audit report included elsewhere in this annual report, as an auditor of companies that are traded publicly in the United States and a firm registered with the PCAOB, is subject to laws in the United States pursuant to which the PCAOB conducts regular inspections to assess its compliance with the applicable professional standards. The auditor is located in mainland China, a jurisdiction where the PCAOB was historically unable to conduct inspections and investigations completely before 2022. As a result, we and investors in the ADSs were deprived of the benefits of such PCAOB inspections. The inability of the PCAOB to conduct inspections of auditors in China in the past has made it more difficult to evaluate the effectiveness of our independent registered public accounting firm's audit procedures or quality control procedures as compared to auditors outside of China that are subject to the PCAOB inspections. On December 15, 2022, the PCAOB issued a report that vacated its December 16, 2021 determination that the positions taken by authorities in mainland China and Hong Kong prevented it from inspecting and investigating completely registered public accounting firms headquartered in those jurisdictions. However, if the PCAOB determines in the future that it no longer has full access to inspect and investigate completely accounting firms in mainland China and Hong Kong, and we use an accounting firm headquartered in one of these jurisdictions to issue an audit report on our financial statements filed with the SEC, we and investors in the ADSs would be deprived of the benefits of such PCAOB inspections again, which could cause investors and potential investors in the ADSs to lose confidence in our audit procedures and reported financial information and the quality of our financial statements.

Risks Relating to the ADSs and Trading Market

The trading price of the ADSs is likely to be volatile, which could result in substantial losses to investors.

Since the ADSs became listed on the Nasdaq Global Market on December 12, 2019, the trading price of the ADSs has ranged from a low of US\$3.32 to a high of US\$129.80 per ADS. The trading price of the ADSs is likely to be volatile and could fluctuate widely due to multiple factors, some of which are beyond our control. This may happen because of broad market and industry factors, including the performance and fluctuation of the market prices of other companies with business operations located mainly in China that have listed their securities in the United States. In addition to market and industry factors, the price and trading volume for the ADSs may be highly volatile for factors specific to our own operations, including the following:

- variations in our revenues, earnings and cash flows;
- regulatory developments affecting us, our customers, or our industry;
- announcements of studies and reports relating to the quality of our products and service offerings or those of our competitors;
- announcements of new investments, acquisitions, strategic partnerships or joint ventures by us or our competitors;
- announcements of new products or service offerings and expansions by us or our competitors;
- changes in financial estimates by securities analysts;
- detrimental adverse publicity about us, our products or services or our industry;
- additions or departures of key personnel;

- detrimental negative publicity about us, our management or our industry;
- release of lock-up or other transfer restrictions on our outstanding equity securities or sales of additional equity securities; and
- actual or potential litigation or regulatory investigations.
- the ADS being delisted and prohibited from trading in the U.S. See “Item 3. Key Information—D. Risk Factors—Risks Relating to Doing Business in China—The ADSs will be delisted and prohibited from trading in the U.S. under the Holding Foreign Companies Accountable Act, or the HFCAA, if the PCAOB is unable to inspect or fully investigate auditors located in China.”

Any of these factors may result in large and sudden changes in the volume and price at which the ADSs will trade.

In the past, shareholders of public companies have often brought securities class action suits against companies following periods of instability in the market price of their securities. If we were involved in a class action suit, it could divert a significant amount of our management's attention and other resources from our business and operations and require us to incur significant expenses to defend the suit, which could harm our results of operations. Any such class action suit, whether or not successful, could harm our reputation and restrict our ability to raise capital in the future. In addition, if a claim is successfully made against us, we may be required to pay significant damages, which could have a material adverse effect on our financial condition and results of operations.

If securities or industry analysts do not publish research or reports about our business, or if they adversely change their recommendations regarding the ADSs, the market price for the ADSs and trading volume could decline.

The trading market for the ADSs will be influenced by research or reports that industry or securities analysts publish about our business. If one or more analysts who cover us downgrade the ADSs, the market price for the ADSs would likely decline. If one or more of these analysts cease to cover us or fail to regularly publish reports on us, we could lose visibility in the financial markets, which in turn could cause the market price or trading volume of the ADSs to decline.

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

Sales of substantial amounts of the ADSs in the public market, or the perception that these sales could occur, could adversely affect the market price of the ADSs and could materially impair our ability to raise capital through equity offerings in the future. We cannot predict what effect, if any, market sales of securities held by our significant shareholders or any other shareholder or the availability of these securities for future sale will have on the market price of the ADSs.

Because we do not expect to pay dividends in the foreseeable future, the holders of the ADSs must rely on price appreciation of the ADSs for a return on their investment.

We currently intend to retain most, if not all, of our available funds and any future earnings to fund the development and growth of our business. As a result, we do not expect to pay any cash dividends in the foreseeable future. Therefore, the ADS holders should not rely on an investment in the ADSs as a source for any future dividend income.

Our board of directors has discretion as to whether to distribute dividends, subject to certain restrictions under Cayman Islands law, namely that our company may only pay dividends out of profits or share premium, and provided always that in no circumstances may a dividend be paid if this would result in our company being unable to pay its debts as they fall due in the ordinary course of business. In addition, our shareholders may by ordinary resolution declare a dividend, but no dividend may exceed the amount recommended by our board of directors. Even if our board of directors decides to declare and pay dividends, the timing, amount and form of future dividends, if any, will depend on our future results of operations and cash flow, our capital requirements and surplus, the amount of distributions, if any, received by us from our subsidiaries, our financial condition, contractual restrictions and other factors deemed relevant by our board of directors. Accordingly, the return to ADS holders on the investment in the ADSs will likely depend entirely upon any future price appreciation of the ADSs. There is no guarantee that the ADSs will appreciate in value or even maintain the price at which the ADS holders purchased the ADSs. The ADS holders may not realize a return on their investment in the ADSs and they may even lose their entire investment in the ADSs.

Our 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 memorandum and articles of association contain provisions which could limit 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 and ADS holders of an opportunity to sell their shares or ADSs 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 transactions. 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.

You may face difficulties in protecting your interests, and your ability to protect your rights through U.S. courts may be limited, because we are incorporated under Cayman Islands law.

We are an exempted company incorporated under the laws of the Cayman Islands. Our corporate affairs are governed by our memorandum and articles of association, the Companies Act (As Revised) of the Cayman Islands and the common law of the Cayman Islands. The rights of shareholders to take action against our directors, actions by our 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 the common law of England, the decisions of whose courts are of persuasive authority, but are not binding, 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 precedent in some jurisdictions in the United States. In particular, the Cayman Islands has a less developed body of securities laws than the United States. Some U.S. states, such as Delaware, have more fully developed and judicially interpreted bodies of corporate law than the Cayman Islands. In addition, Cayman Islands companies may not have standing to initiate a shareholder derivative action in a federal court of the United States.

Shareholders of Cayman Islands exempted companies like us have no general rights under Cayman Islands law to inspect corporate records (other than the memorandum and articles of association, our register of mortgages and charges and special resolutions of our shareholders) or to obtain copies of lists of shareholders of these companies. Our directors have discretion under our articles of association to determine whether or not, and under what conditions, our corporate records may be inspected by our shareholders, but are not obliged to make them available to our shareholders. This may make it more difficult for you to obtain the information needed to establish any facts necessary for a shareholder motion or to solicit proxies from other shareholders in connection with a proxy contest.

In addition, we conduct substantially all of our business operations in China, and substantially all of our directors and senior management are based in China, which is an emerging market. The SEC, U.S. Department of Justice and other authorities often have substantial difficulties in bringing and enforcing actions against non-U.S. companies and non-U.S. persons, including company directors and officers, in certain emerging markets, including China. Additionally, our public shareholders may have limited rights and few practical remedies in emerging markets where we operate, as shareholder claims that are common in the United States, including class action securities law and fraud claims, generally are difficult to pursue as a matter of law or practicality in many emerging markets, including China. For example, in China, there are significant legal and other obstacles to obtaining information needed for shareholder investigations or litigation outside China or otherwise with respect to foreign entities. Although the local authorities in China may establish a regulatory cooperation mechanism with the securities regulatory authorities of another country or region to implement cross-border supervision and administration, the regulatory cooperation with the securities regulatory authorities in the United States has not been efficient in the absence of a mutual and practical cooperation mechanism. According to Article 177 of the PRC Securities Law which became effective in March 2020, no foreign securities regulator is allowed to directly conduct investigation or evidence collection activities within the territory of the PRC. Accordingly, without the consent of the competent PRC securities regulators and relevant authorities, no organization or individual may provide the documents and materials relating to securities business activities to foreign securities regulators.

As a result of all of the above, our public shareholders may have more difficulty in protecting their interests in the face of actions taken by our management, members of our board of directors or our controlling shareholders than they would as public shareholders of a company incorporated in the United States. For a discussion of significant differences between the provisions of the Companies Act of the Cayman Islands and the laws applicable to companies incorporated in the United States and their shareholders, see “Item 10. Additional Information—B. Memorandum and Articles of Association—Differences in Corporate Law.”

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

We are a Cayman Islands exempted company and substantially all of our assets are located outside of the United States. Most of our current operations are conducted in China. In addition, most of our current directors and officers are nationals and residents of countries other than the United States. As a result, it may be difficult or impossible for you to bring an action against us or against these individuals in the United States 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.

The voting rights of holders of ADSs are limited by the terms of the deposit agreement, and you may not be able to exercise your right to direct how the Class A ordinary shares which are represented by your ADSs are voted.

Holders of ADSs do not have the same rights as our registered shareholders. As a holder of the ADSs, you will not have any direct right to attend general meetings of our shareholders or to cast any votes at such meetings. You will only be able to exercise the voting rights which are carried by the underlying Class A ordinary shares represented by your ADSs indirectly by giving voting instructions to the depositary in accordance with the provisions of the deposit agreement. Under the deposit agreement, you may vote only by giving voting instructions to the depositary. If we instruct the depositary to ask for your instructions, then upon receipt of your voting instructions, the depositary will try, as far as is practicable, to vote the underlying Class A ordinary shares which are represented by your ADSs in accordance with your instructions. If we do not instruct the depositary to ask for your instructions, the depositary may still vote in accordance with instructions you give, but it is not required to do so. Under the deposit agreement for the ADSs, if you do not vote, the depositary may give us a discretionary proxy to vote the Class A ordinary shares underlying your ADSs at shareholders' meetings if:

- we have timely provided the depositary with notice of meeting and related voting materials;

- we have instructed the depositary that we wish a discretionary proxy to be given;
- we have informed the depositary that there is no substantial opposition as to a matter to be voted on at the meeting; and
- a matter to be voted on at the meeting would not have a material adverse impact on shareholders.

The effect of this discretionary proxy is that if you do not vote at shareholders' meetings, you cannot prevent the Class A ordinary shares underlying your ADSs from being voted, except under the circumstances described above. This may make it more difficult for shareholders to influence the management of our company. Holders of our ordinary shares are not subject to this discretionary proxy. You will not be able to directly exercise your right to vote with respect to the underlying Class A ordinary shares represented by your ADSs unless you cancel and withdraw such shares and become the registered holder of such shares prior to the record date for the general meeting.

Under our memorandum and articles of association, the minimum notice period required to be given by our company to our registered shareholders to convene a general meeting is ten calendar days. When a general meeting is convened, you may not receive sufficient advance notice of the meeting to withdraw the underlying Class A ordinary shares represented by your ADSs and become the registered holder of such shares to allow you to attend the general meeting and to vote directly with respect to any specific matter or resolution to be considered and voted upon at the general meeting. In addition, under our articles of association, for the purposes of determining those shareholders who are entitled to attend and vote at any general meeting, our directors may close our register of members and/or fix in advance a record date for such meeting, and such closure of our register of members or the setting of such a record date may prevent you from withdrawing the underlying Class A ordinary shares represented by your ADSs and becoming the registered holder of such shares prior to the record date, so that you would not be able to attend the general meeting or to vote directly. If we ask for your instructions, the depositary will notify you of the upcoming vote and will arrange to deliver our voting materials to you. We have agreed to give the depositary at least 45 days' prior notice of shareholder meetings. Nevertheless, we cannot assure you that you will receive the voting materials in time to ensure that you can instruct the depositary to vote the underlying Class A ordinary shares represented by your ADSs. In addition, the depositary and its agents are not responsible for failing to carry out voting instructions or for their manner of carrying out your voting instructions. This means that you may not be able to exercise your right to direct how the underlying Class A ordinary shares represented by your ADSs are voted and you may have no legal remedy if the underlying Class A ordinary shares represented by your ADSs are not voted as you requested.

You may not receive dividends or other distributions on our ordinary shares and you may not receive any value for them, if it is illegal or impractical to make them available to you.

The depositary of the ADSs has agreed to distribute, subject to the terms of the deposit agreement, the cash dividends or other distributions it or the custodian receives on our Class A ordinary shares or other deposited securities underlying the ADSs, after deducting its fees and expenses. You will receive these distributions in proportion to the number of Class A ordinary shares your ADSs represent. However, the depositary is not responsible if it decides that it is unlawful or impractical to make a distribution available to any holders of ADSs. For example, it would be unlawful to make a distribution to a holder of ADSs if it consists of securities that require registration under the Securities Act but that are not properly registered or distributed under an applicable exemption from registration. The depositary may also determine that it is not feasible to distribute certain property. Additionally, the value of certain distributions may be less than the cost of distribution. In these cases, the depositary may determine not to distribute such property. We have no obligation to register under U.S. securities laws any ADSs, ordinary shares, rights or other securities received through such distributions. We also have no obligation to take any other action to permit the distribution of ADSs, ordinary shares, rights or anything else to holders of ADSs. This means that you may not receive distributions we make on our ordinary shares or any value for them if it is illegal or impractical for us to make them available to you. These restrictions may cause a material decline in the value of the ADSs.

You may experience dilution of your holdings due to inability to participate in rights offerings.

We may, from time to time, distribute rights to our shareholders, including rights to acquire securities. Under the deposit agreement, the depositary will not distribute rights to holders of ADSs unless the distribution and sale of rights and the securities to which these rights relate are either exempt from registration under the Securities Act with respect to all holders of ADSs, or are registered under the provisions of the Securities Act. The depositary may, but is not required to, attempt to sell these undistributed rights to third parties, and may allow the rights to lapse. We may be unable to establish an exemption from registration under the Securities Act, and we are under no obligation to file a registration statement with respect to these rights or underlying securities or to endeavor to have a registration statement declared effective. Accordingly, holders of ADSs may be unable to participate in our rights offerings and may experience dilution of 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 books at any time or from time to time when it deems expedient in connection with the performance of its duties. The depositary may close its books from time to time for a number of reasons, including in connection with corporate events, such as a rights offering, or “for record date or processing purposes” in emergencies, and on weekends and public holidays. The depositary may refuse to deliver, transfer or register transfers of the ADSs generally when our share register or the books of the depositary are closed, or at any time if we or the depositary think it is 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.

ADSs holders may not be entitled to a jury trial with respect to claims arising under the deposit agreement, which could result in less favorable outcomes to the plaintiffs in any such action.

The deposit agreement governing the ADSs representing our Class A ordinary shares provides that, to the fullest extent permitted by law, ADS holders waive the right to a jury trial of any claim they may have against us or the depositary arising out of or relating to our shares, the ADSs or the deposit agreement, including any claim under the U.S. federal securities laws.

If we or the depositary opposed a jury trial demand based on the waiver, the court would determine whether the waiver was enforceable based on the facts and circumstances of that case in accordance with the applicable state and federal law. To our knowledge, the enforceability of a contractual pre-dispute jury trial waiver in connection with claims arising under the federal securities laws has not been finally adjudicated by the United States Supreme Court. However, we believe that a pre-dispute contractual waiver of jury trial is generally enforceable, including under the laws of the State of New York, which govern the deposit agreement, by a federal or state court in the City of New York, which has non-exclusive jurisdiction over matters arising under the deposit agreement. In determining whether to enforce a pre-dispute contractual waiver of jury trial, courts will generally consider whether a party knowingly, intelligently and voluntarily waived the right to a jury trial. We believe that this is the case with respect to the deposit agreement and the ADSs. It is advisable that you consult legal counsel regarding the jury waiver provision before entering into the deposit agreement.

If you or any other holders or beneficial owners of ADSs bring a claim against us or the depositary in connection with matters arising under the deposit agreement or the ADSs, including claims under federal securities laws, you or such other holder or beneficial owner may not be entitled to a jury trial with respect to such claims, which may have the effect of limiting and discouraging lawsuits against us and the depositary. If a lawsuit is brought against either or both of us and the depositary under the deposit agreement, it may be heard only by a judge or justice of the applicable trial court, which would be conducted according to different civil procedures and may result in different outcomes than a trial by jury would have, including results that could be less favorable to the plaintiffs in any such action.

Nevertheless, if this jury trial waiver provision is not permitted by applicable law, an action could proceed under the terms of the deposit agreement with a jury trial. No condition, stipulation or provision of the deposit agreement or ADSs serves as a waiver by any holder or beneficial owner of ADSs or by us or the depository of compliance with any substantive provision of the U.S. federal securities laws and the rules and regulations promulgated thereunder.

We are a foreign private issuer within the meaning of the rules under the Exchange Act, and as such we are exempt from certain provisions applicable to United States domestic public companies.

Because we are a foreign private issuer under the Exchange Act, we are exempt from certain provisions of the securities rules and regulations in the United States that are applicable to U.S. domestic issuers, including:

- the rules under the Exchange Act requiring the filing of quarterly reports on Form 10-Q or current reports on Form 8-K with the SEC;
- the sections of the Exchange Act regulating the solicitation of proxies, consents, or authorizations in respect of a security registered under the Exchange Act;
- the sections of the Exchange Act requiring insiders to file public reports of their stock ownership and trading activities and liability for insiders who profit from trades made in a short period of time; and
- the selective disclosure rules by issuers of material nonpublic information under Regulation FD.

We are required to file an annual report on Form 20-F within four months of the end of each fiscal year. In addition, we intend to publish our results on a quarterly basis through press releases, distributed pursuant to the rules and regulations of the Nasdaq Stock Market. Press releases relating to financial results and material events will also be furnished to the SEC on Form 6-K. However, the information we are required to file with or furnish to the SEC will be less extensive and less timely compared to that required to be filed with the SEC by U.S. domestic issuers. As a result, you may not be afforded the same protections or information which would be made available to you were you investing in a U.S. domestic issuer.

We are an emerging growth company within the meaning of the Securities Act and may take advantage of certain reduced reporting requirements.

We are an “emerging growth company,” as defined in the JOBS Act, and we may take advantage of certain exemptions from requirements 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 of 2002 for so long as we remain an emerging growth company. As a result, if we elect not to comply with such auditor attestation requirements, our investors may not have access to certain information they may deem important.

The JOBS Act also provides that an emerging growth company does not need to comply with any new or revised financial accounting standards until such date that a private company is otherwise required to comply with such new or revised accounting standards. We have elected to take advantage of the extended transition period. As a result of this election, our 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 incur increased costs as a result of being a public company, particularly after we cease to qualify as an “emerging growth company.”

We are a public company and expect to incur significant legal, accounting and other expenses that we did not incur as a private company, including additional costs associated with our public company reporting obligations. The Sarbanes-Oxley Act of 2002, as well as rules subsequently implemented by the SEC and the Nasdaq Stock Market, impose various requirements on the corporate governance practices of public companies. As a company with less than US\$1.235 billion in gross revenues for our last fiscal year, we qualify as an “emerging growth company” pursuant to the JOBS Act. An emerging growth company may take advantage of specified reduced reporting and other requirements that are otherwise applicable generally to public companies. These provisions include exemption from the auditor attestation requirement under Section 404 of the Sarbanes-Oxley Act of 2002 in the assessment of the emerging growth company’s internal control over financial reporting. The JOBS Act also permits an emerging growth company to delay adopting new or revised accounting standards until such time as those standards apply to private companies. We rely on such exemption provided by the JOBS Act. As a result, our financial statements may not be comparable to companies that comply with public company effective dates.

We expect these rules and regulations to increase our legal and financial compliance costs and to make some corporate activities more time-consuming and costly. After we are no longer an “emerging growth company,” we expect to incur significant expenses and devote substantial management effort toward ensuring compliance with the requirements of Section 404 of the Sarbanes-Oxley Act of 2002 and the other rules and regulations of the SEC. For example, as a result of being a public company, we need to increase the number of independent directors and adopt policies regarding internal controls and disclosure controls and procedures. In addition, operating as a public company makes it more difficult and more expensive for us to obtain director and officer liability insurance, and we may be required to accept reduced policy limits and coverage or incur substantially higher costs to obtain the same or similar coverage. In addition, we will incur additional costs associated with our public company reporting requirements. It may also be more difficult for us to find qualified persons to serve on our board of directors or as executive officers. We are currently evaluating and monitoring developments with respect to these rules and regulations, and we cannot predict or estimate with any degree of certainty the amount of additional costs we may incur or the timing of such costs.

As a company incorporated in the Cayman Islands, we are permitted to adopt certain home country practices in relation to corporate governance matters that differ significantly from the Nasdaq Stock Market corporate governance listing standards; these practices may afford less protection to shareholders than they would enjoy if we comply fully with the Nasdaq Stock Market corporate governance listing standards.

As a Cayman Islands exempted company listed on Nasdaq Global Market, we are subject to the Nasdaq Stock Market corporate governance listing standards. However, Nasdaq Stock Market rules permit a foreign private issuer like us to follow the corporate governance practices of its home country. Certain corporate governance practices in the Cayman Islands, which is our home country, may differ significantly from the Nasdaq Stock Market corporate governance listing standards. We have elected to follow our home country practice in lieu of certain corporate governance requirements of the Nasdaq Stock Market. See “Item 16G. Corporate Governance.” As a result, our shareholders may be afforded less protection than they would otherwise enjoy under the Nasdaq Stock Market corporate governance listing standards applicable to U.S. domestic issuers.

We are a “controlled company” within the meaning of the Nasdaq Stock Market Rules and, as a result, may rely on exemptions from certain corporate governance requirements that provide protection to shareholders of other companies.

We are a “controlled company” as defined under the Nasdaq Stock Market Rules because our founder, chairman of the board of directors and chief executive officer, Mr. Huazhi Hu, owns more than 50% of our total voting power. For so long as we remain a controlled company under that definition, we may rely on certain exemptions from corporate governance rules, including the rule that a majority of our board of directors must be independent directors and that we have to establish a nominating committee and a compensation committee composed entirely of independent directors. As a result, you will not have the same protection afforded to shareholders of companies that are subject to these corporate governance requirements should we choose to rely on such exemptions. We currently do not plan to rely on these exemptions.

If we are a passive foreign investment company, or PFIC, for any taxable year, our U.S. shareholders may be subject to adverse U.S. federal income tax consequences.

A non-U.S. corporation, such as our company, will be a PFIC for U.S. federal income tax purposes for any taxable year if either (i) at least 75% of its gross income for such year is passive income or (ii) at least 50% of the value of its assets (based on an average of the quarterly values of the assets) during such year is attributable to assets that produce or are held for the production of passive income. A separate determination must be made after the close of each taxable year as to whether a non-U.S. corporation is a PFIC for that year. Although the law in this regard is unclear, we intend to treat the VIE and the VIE's subsidiaries as being owned by us for U.S. federal income tax purposes, not only because we have the power to direct the significant activities of such entities but also because we are entitled to substantially all of their economic benefits and, as a result, we consolidate their results of operations in our consolidated financial statements.

Assuming that we are treated as the owner of the VIE (and its subsidiaries) for U.S. federal income tax purposes, and based upon our current and expected income and assets, including goodwill and other unbooked intangibles, and the market value of the ADSs, we do not believe we were a PFIC for U.S. federal income tax purposes for the taxable year ended December 31, 2022. While we do not expect to become a PFIC, because the value of our assets for purposes of the asset test may be determined by reference to the market price of the ADSs, fluctuations in the market price of the ADSs may cause us to become a PFIC for the current or subsequent taxable years. In addition, the composition of our income and assets will also be affected by our business plans including how quickly we use our cash and other liquid assets. If we determine not to deploy significant amounts of cash for active purposes or if it were determined that we do not own the stock of the VIE for U.S. federal income tax purposes, our risk of being a PFIC may substantially increase. In light of the foregoing, there can be no assurance that we were not, or will not be, a PFIC for any taxable year. Our U.S. counsel expresses no opinion with respect to our PFIC status for any taxable year.

If we are a PFIC for any taxable year during which a U.S. Holder (as defined in "Item 10. Additional Information—E. Taxation—U.S. Federal Income Taxation") holds the ADS or a Class A ordinary share, certain adverse U.S. federal income tax consequences could apply to the U.S. Holder. See "Item 10. Additional Information—E. Taxation—U.S. Federal Income Taxation—Passive Foreign Investment Company Rules."

Item 4. Information on the Company

A. History and Development of the Company

In December 2014, EHang Holdings Limited, or EHang Holdings, was incorporated in the Cayman Islands as our offshore holding company to facilitate offshore financing and listing. In the same month, Ehfly Technology Limited, or Ehfly Technology, was incorporated in Hong Kong as a direct, wholly-owned subsidiary of EHang Holdings. In addition, the following entities were incorporated to engage in the business of AAV manufacturing and sales and the provision of AAV commercial solutions and related services:

- In October 2015, Ehfly Technology established EHang Intelligent Equipment (Guangzhou) Co., Ltd., or the WFOE, as a wholly-owned subsidiary in China. The WFOE is engaged in the research, development, manufacture and sale of AAVs, and the research and development of software, communication technology and AAV technologies related to air mobility and intelligent aviation.
- In January 2016, we obtained a controlling financial interest in Guangzhou EHang Intelligent Technology Co., Ltd., or the VIE, because the WFOE entered into a series of contractual arrangements with the VIE and the VIE's shareholders. The VIE is primarily engaged in the research, development, manufacture and sale of AAVs, and the research and development of AAV operating systems and infrastructure.

- In June 2020, the WFOE, jointly with two other shareholders, established Yunfu EHang Intelligent Technology Limited to manufacture mainly passenger-grade AAVs.
- In March 2021, the VIE established Guangdong EHang General Aviation Co., Ltd., to provide operational flight services with AAVs.

Under PRC laws and regulations, our PRC subsidiaries may pay cash dividends to us out of their respective accumulated profits. However, the ability to our PRC subsidiaries to make such distribution to us is subject to various PRC laws and regulations, including the requirement to fund certain statutory funds, as well as potential restriction on currency exchange and capital controls imposed by the PRC government. For more details, see "Item 3. Key Information—D. Risk Factors—Risks Relating to Doing Business in China— We rely on dividends and other distributions on equity paid by our PRC subsidiaries to fund any cash and financing requirements we may have, and any limitation on the ability of our PRC subsidiaries to make payments to us could have a material adverse effect on our ability to conduct our business" and "Item 4. Information on the Company—B. Business Overview—PRC Regulation—Dividend Distribution." As a result of our contractual arrangements with the VIE and the VIE's shareholders, we are regarded as the primary beneficiary of the VIE, and we treat the VIE and the VIE's subsidiaries as our consolidated affiliated entities under U.S. GAAP. We have consolidated the financial results of the VIE and the VIE's subsidiaries in our consolidated financial statements in accordance with U.S. GAAP.

On December 12, 2019, the ADSs commenced trading on the Nasdaq Global Market under the symbol "EH." We raised approximately US\$33.9 million in net proceeds from the issuance of new shares in our initial public offering after deducting underwriting commissions and the offering expenses payable by us. In January 2020, the underwriters exercised their over-allotment option and we raised approximately US\$1.0 million in net proceeds from the issuance of new shares after deducting underwriting discounts and offering expenses payable by us.

Our principal executive offices are located at 11/F Building One, EHang Technology Park, No. 29 Bishan Blvd., Huangpu District, Guangzhou, Guangdong Province, 510700, People's Republic of China. Our telephone number at this address is +86 20 2902 8899. Our registered office is situated at the office of Maples Corporate Services Limited, PO Box 309, Ugland House, Grand Cayman, KY1-1104, Cayman Islands. Our agent for service of process in the United States is Cogency Global Inc., located at 122 East 42nd Street, 18th Floor, New York, NY 10168.

The SEC maintains an internet site that contains reports, proxy and information statements, and other information regarding issuers that file electronically with the SEC on www.sec.gov. You can also find information on our website www.ehang.com. The information on our website should not be deemed a part of this annual report.

B. Business Overview

We are a leading autonomous aerial vehicle ("AAV") technology platform company founded in 2014, with a mission to make safe, autonomous and eco-friendly air mobility accessible to everyone. We believe we were the first in the world to launch and deliver proprietary passenger-carrying AAVs, related command-and-control systems and commercial solutions, setting new milestones in AAV innovative technologies and the emerging urban air mobility ("UAM") market. In 2019, we became the world's first publicly traded technology company in the global UAM industry by listing on Nasdaq.

In today's increasingly populated and interconnected world, traditional modes of urban transportation continue to contribute to congestion and pollution, and they are largely confined to land-based infrastructure. Mobility for the future requires a revolutionary solution. While the sky above has always been a possibility, we brought a safe, autonomous, eco-friendly, cost-effective, easy-to-use and efficient air mobility solution one step closer to reality when we unveiled our first passenger-carrying AAV in 2016. Our AAVs require minimal space for vertical take-off and landing, enabling urban travel to expand to the three-dimensional space. Our AAV technologies have the potential to reduce road traffic and associated congestion by taking transportation to the skies while utilizing electric power to reduce pollution. We believe AAV technologies will transform the future of transportation, and benefit the society and communities by improving lives and creating new industries.

Unlike other manually controlled UAVs and piloted electric vertical takeoff and landing (“eVTOL”) aircraft, our intelligent AAVs can fly and operate autonomously from take-off to landing in pre-determined flight routes without any pilot onboard. Our in-flight operating systems and on-the-ground infrastructures enable reliable, real-time and cluster management of a fleet of AAVs and efficient operations at scale.

We strive to design safe, reliable and functional products. We adopt a full redundancy design approach for our AAVs to avoid single points of failure. At our R&D center, we have conducted a multitude of AAV flight tests, including climbing flight tests, high maneuverability tests, speed tests, night flying tests, as well as flight tests in harsh weather conditions. As of the date of this annual report, we have completed 75% of the compliance tests of the EH216-S on the world’s first type certification project with the Civil Aviation Administration of China (the “CAAC”) for a passenger-carrying AAV to demonstrate and verify our product safety, reliability and performance. As of March 31, 2023, the flight footprints of our EH184, EH116 and EH216 series AAVs have accumulated over 35,000 safe, autonomous trial or demo flights in 12 countries across Asia, Europe and Americas, predominantly in China. These trial or demo flights include a large number of passenger-carrying autonomous flights and flight tests in winds of up to 70 kilometers per hour, in fog with a visibility of approximately 50 meters, and at a flight altitude of 4,100 meters above sea level.

With our strategic positioning to be a UAM platform operator, we adopt an integrated business model by selling AAV solutions and providing operational services. We design, develop, manufacture, sell and operate AAVs and their supporting systems and infrastructure for a broad range of industries and applications, including air mobility (consisting of passenger transportation and logistics), smart city management and aerial media solutions.

Our major source of revenue comes from our core business, air mobility solutions, from our continued deliveries of the EH216 series AAVs since 2019. We delivered 21 units of the EH216 series in 2022.

As of December 31, 2022, we had delivered 185 units of the EH216 series AAVs, including 170 units of the EH216-S, seven units of the EH216-F and eight units of the EH216-L, mainly operated on a limited trial basis in tourism locations in China, for testing, training and demonstration purposes, and we had also delivered four command-and-control centers or systems for smart city management in China.

As of March 31, 2023, our order pipeline for the EH216-S had exceeded 100 units in China market, and the pre-orders we received for the EH216 series and the VT-30 had more than 1,200 units in overseas markets on a cumulative basis. Pre-orders do not obligate the customers to purchase our AAVs unless certain conditions are satisfied. Fulfilment is expected to take several years and is conditional upon, among other things, achievement of performance milestones and receipt of regulatory approvals.

Due to the shift of corporate priorities to type certification process, our revenues decreased by 68.5% from RMB180.1 million in 2020 to RMB56.8 million in 2021, and further decreased by 22.0% to RMB44.3 million (US\$6.4 million) in 2022. Our net loss increased by 241.0% from RMB92.0 million in 2020 to RMB 313.9 million in 2021, and further increased by 4.9% to RMB329.3 million (US\$47.7 million) in 2022. In 2022, revenues generated by air mobility solutions, smart city management solutions and aerial media solutions were RMB40.4 million (US\$5.9 million), RMB2.1 million (US\$0.3 million) and RMB1.3 million (US\$0.2 million), representing 91.2%, 4.8% and 3.0% of our total revenues, respectively. As of December 31, 2022, our accumulated deficit amounted to RMB1,450.4 million (US\$210.3 million).

The Emerging UAM Market

Urban Transportation Faces Increasing Challenges with Ground Mobility

Continued population growth and increased urbanization are adding pressure to urban transportation on the ground. Some 56% of the global population – 4.4 billion inhabitants – live in cities, according to the World Bank's data in 2022. The urban population is projected to more than double by 2050, when almost 7 of 10 people will live in cities.

Transportation is a nonnegligible part in this migration. The speed and scale of urbanization has led to unprecedented traffic congestion in megacities and could further exacerbate challenges faced by ground mobility, with growing demand for higher travel volume, frequency and efficiency across urban and suburban areas.

Expanding ground-based urban transportation infrastructure requires significant investment, including increasing costs of time and money in building traffic systems and parking lots. It's also becoming increasingly difficult given how the constraints in ground mobility capacity cause complications in scaling networks across locations. Ultimately, a new, innovative and environmentally-friendly transportation solution is needed in urban areas and in high demand.

eVTOL Technologies Make UAM Possible

The advancements in eVTOL technologies are enabling a new era of transportation with UAM, poised to revolutionize the way we move people and goods across urban and suburban areas.

One of the key drivers of eVTOL technology is the rapid development of battery technology driven by continued investment in ground-based electric vehicles. Lithium-ion batteries are becoming more efficient, with higher capacity and energy density, shorter charge times, and longer cycle life. These advancements are enabling eVTOL aircraft to fly longer distances and carry more passengers and cargo, while reducing the weight and cost of the overall system. Moreover, distributed electric propulsion ("DEP"), which uses multiple small electric motors instead of a single central engine, makes quiet and cost-effective eVTOL aircraft accessible. Other critical enablers include the development of advanced materials and manufacturing techniques, which are helping to reduce the weight and improve the performance of eVTOL aircraft, and the latest 5G telecommunications and sensor technologies that are essential for safe and efficient operation of these aircraft.

On the other hand, eVTOL technologies offer a range of advantages over traditional ground-based two-dimensional transportation options. It's a safe, efficient, simple and carbon-free mobility solution. With their ability to vertically take off and land, eVTOL aircraft require less infrastructure than traditional airports or helipads, and can utilize more of the three-dimensional urban airspace. Additionally, it also allows efficient direct point-to-point flights, reducing the time in travel and increasing productivity.

As a result, eVTOL technologies are making UAM possible, unlocking greater freedom of mobility. eVTOL aircraft could become an important part of a three-dimensional mobility solution that connects the ground, the sea and the sky for today's transportation issues.

AAVs Bring Revolutions to UAM

AAVs are transforming the UAM landscape, bringing a host of benefits that were previously unattainable. The integration of artificial intelligence and autonomous systems into AAVs enables them to reduce traffic congestion and accidents caused by human driver errors. With an on-demand ridesharing network, AAVs can increase the utilization of vehicles, improving travel efficiency and convenience for commuters. The resulting reduction in traffic congestion and commute times can significantly enhance the quality of life for urban residents.

Additionally, AAVs can save costs on professional pilots, who are often scarce and expensive to train. With autonomous systems, it is also convenient to effectively manage large-scale aircraft fleets and flight routes. The ability to remotely monitor and control AAVs in emergencies makes them a reliable transportation option for emergency services and critical medical supplies.

Furthermore, with their vertical take-off and landing capabilities, AAVs can utilize more urban airspace and reduce the strain on ground transportation infrastructure. The introduction of AAVs has the potential to change the way people live and travel, bringing social and economic revolutions in many conventional fields, including tourism and local transportation.

Significant UAM Market Opportunities

The potential of UAM market is immense and is expected to grow exponentially over the next few decades. China's UAM market has been promoted by increasingly favorable policies and regulations for the development of modern urban three-dimensional mobility, electric unmanned civil aviation, and low-altitude economy in recent years. Based on its large populations and massive market demand, the China UAM market has great potential for our AAVs with various use cases in aerial tourism, urban transportation, aerial logistics, emergency services, smart city management, etc. Besides, China's efficient and cost-effective UAV manufacturing and supply chain competence bolster up its UAM market growth potential.

The opportunities presented by the UAM market extend beyond just transportation. The emergence of eVTOL aircraft could be more efficient and sustainable than traditional modes of transportation such as helicopters, cars, and airlines. They have the potential to enable faster and more convenient travel, reduce traffic congestion and carbon emissions, and increase economic growth through job creation and new business opportunities.

We believe this innovative new type of UAM provided by eVTOL aircraft, particularly our AAVs, will create an incremental market with significant and long-term growth potential in addition to taking the existing market share from traditional transportation methods. To capture the significant growth potential in the AAV market, we strive to continue innovating and expanding the boundaries for air mobility.

Our Competitive Strengths

Pioneer and leader in the global UAM industry

As the world's leading AAV technology platform company, we are the pioneer and leader in the global UAM industry with prominent first-mover advantages.

We unveiled the world's first electric passenger-carrying AAV, the EH184, at CES in the U.S. in 2016, attracting worldwide interest and passion to this disruptive technological revolution and the emerging UAM industry.

We developed and established the first command-and-control system and center at our headquarters in Guangzhou, China, in 2017, enabling cluster management of our AAVs through an intelligent system platform.

In March 2018, we started our first delivery of a unit of the EH216-S, our dual-seat passenger-carrying AAV, to a customer for testing, training and demonstration purposes. This was believed to be the world's first commercial delivery of a passenger-carrying AAV in the UAM industry. Since then, as of December 31, 2022, we had delivered accumulated 185 units of the EH216 series AAVs to our customers worldwide, mainly operated on a limited trial basis in aerial tourism usage scenarios in China, for testing, training and demonstration purposes. With the delivery record unparalleled by others, we are a pioneer in the market and a leading player in the global UAM industry.

In December 2019, EHang was successfully listed on Nasdaq following an initial public offering, becoming the world's first publicly traded company in the UAM industry.

As a first mover, we not only design, develop, manufacture and sell our AAV products, but also actively collaborate with our customers and partners to explore various practical use cases through operating our AAVs globally. As of March 31, 2023, the flight footprints of our EH184, EH116 and EH216 series AAVs have accumulated over 35,000 safe, autonomous trial or demo flights in 12 countries across Asia, Europe and Americas, predominantly in China. The industry-leading flight record demonstrated our AAV product safety, reliability, adaptability and performance in different environments.

We are also a first mover in regulatory breakthrough and certification progress in this emerging industry. We expect to obtain the world's first airworthiness certificate of a passenger-carrying AAV or autonomous eVTOL aircraft as we are close to complete the type certification of the EH216-S with the CAAC in the near future. With that achieved, it is expected that we will be the first to start commercial operations of passenger-carrying AAVs in the UAM market.

Proprietary and revolutionary AAV technologies

With our mission to make safe, autonomous and eco-friendly air mobility accessible to everyone, we have proprietarily developed the revolutionary AAV technologies and products through deeply integrating our strong expertise in the fields of both aviation and software system. This makes our AAVs different from other piloted helicopters and eVTOL aircraft.

With safety as the orientation as well as our first priority above anything else, we innovate and stick to three fundamental technological principles, which are redundancy, autonomous flying, and cluster management that are reflected in all of our AAV products.

To ensure the safety, we adopt a full redundancy design and technologies in our AAVs from day one in order to avoid single points of failure, which often happen in conventional aircraft like helicopters. Through the configuration of distributed electric propulsion, our AAVs provide a safe and reliable propulsion system with backups for key components and sub-systems. If any would malfunction, the fail-safe system in our intelligent flight control systems can automatically monitor the situation in real time and quickly respond to restore the lost functionality through backups to ensure safety. For example, our EH216 series have 16 coaxial propellers driven by 16 independent motors mounted on 8 arms. According to our tests, the aircraft could still land safely even if any three propellers were intendedly stopped in flight, although the probability of which happens is extremely rare in normal situations. Additionally, our redundancy design is also reflected in our electric systems, sensors, flight control systems, communication systems, etc. to strengthen safety and reliability of our AAVs.

Autonomous flying is also embedded in our genes from day one. Unlike other manually controlled UAVs or piloted eVTOL aircraft, our intelligent AAVs can fly without any human pilot onboard and operate autonomously from take-off to landing along pre-determined flight routes under the safe protection by electric fence within the pre-approved airspace.

Cluster management is another key principle as well as our technological advantage to ensure flight safety and autonomy. Our proprietary airborne operating systems and on-the-ground command-and-control systems, or standalone smartphone-or-tablet-or-computer-based controller app, enable reliable and simultaneous management of AAV fleets at scale. Through 4G or 5G high-speed telecommunication networks, it allows real-time monitoring and warning of flight data and status of our AAVs, route planning and fleet management, remote control in emergencies to take contingency measures, etc. to ensure flight safety and enhance intelligence and efficiency.

With the three technological principles, we strive to make safe, reliable and functional AAV products through strict tests. At our R&D center and testing locations, we have conducted a multitude of AAV flight tests, including climbing flight tests, high maneuverability tests, speed tests, night flight tests, as well as flight tests in harsh weather conditions and environments, for example, in winds of up to 70 kilometers per hour, in fog with a visibility of approximately 50 meters, and at a flight altitude of 4,100 meters above sea level.

World's leading type certification progress for passenger-carrying AAV or eVTOL aircraft

The aviation industry has a nature of high and strict threshold of safety, regulations and certifications. New types of eVTOL aircraft, including our passenger-carrying AAVs, are also required to pass through the type certification to obtain the airworthiness certificate to be allowed for commercial operations by aviation regulators. The certification path usually takes several years case by case or even more efforts if there are no certification standards applicable to the specific type yet.

As the first mover of electric passenger-carrying AAVs, we were dedicated to not only designing, developing, and manufacturing our products that are able to be certified, but also collaborating with the CAAC and contribute our years of practice and experience to formulating the innovative type certification standards from a holistic view for our AAVs from zero to one.

The CAAC took the lead to officially start the first type certification process for a passenger-carrying AAV since it accepted our application for EH216-S in January 2021. In February 2022, the CAAC formally adopted and issued the *Special Conditions for Type Certification of EH216-S Unmanned Aircraft System*, according to the CAAC's *Regulations on Certification of Civil Aviation Products and Parts (CCAR-21)*. It lays down the certification basis and provides clear safety requirements for the type certification of EH216-S, including flight performance, aircraft structures, design and constructions, propulsion systems, systems and equipment, data link, ground control station, etc. This Special Conditions is regarded as a significant milestone of the world's first airworthiness standard specially for a passenger-carrying autonomous eVTOL aircraft, and was shared as an innovative case study by the CAAC for other countries' reference in formulating related regulations at the International Civil Aviation Organization ("ICAO") Assembly Conference in September 2022.

With specific requirements defined, we have worked out the Project Specific Certification Plan and the Certification Plan with solid means of compliance, all approved by the CAAC. Having successively passed through the type certification phases of Concept Design, Requirements Definition, and Compliance Planning, we progressed into the final phase of Demonstration and Verification of Compliance in the fourth quarter of 2022.

In the final phase, we have manufactured several EH216-S conforming aircraft in our Yunfu production facility, passed the manufacturing conformity inspection by the CAAC, and are conducting required compliance tests at flight bases in Guangzhou and Hezhou as well as laboratories in other locations. Based on the CAAC-agreed compliance test plans, 75% of the compliance tests have been completed as of the date of this annual report, including laboratory tests, ground tests and inspections, flight tests and data analysis, which means more than 90% of the entire type certification processes have been completed. We believe this represents the fastest progress among all the ongoing eVTOL aircraft type certification projects worldwide, as well as the first for a passenger-carrying autonomous eVTOL aircraft.

A rich set of AAV product portfolio for diversified commercial solutions

Based on our first priority of safety as well as our three fundamental technological principles, we have developed a scalable, integrated UAM technology platform. It carries a rich set of innovative AAV products with differentiated advantages for diversified and immense market demands.

Our proprietary AAV products have multiple configurations, including multi-rotors like the EH216 series, lift-and-cruise aircraft like the VT series, as well as fixed wings in our development pipeline. They are also designed in various sizes, from the large-sized passenger-carrying EH216-S and VT-30, the medium-sized industrial Falcon B, to the small-sized GD series for aerial media performance. We develop our AAVs for different uses aligned with their suitable performances, such as the EH216-S for short-to-medium-range low-altitude intra-city air mobility, while the VT-30 for long-range inter-city air mobility. Additionally, we provide flexible and customized solutions for different customer demands by further developing the EH216-F for high-rise firefighting, and the EH216-L for large-payload aerial logistics, on the basis of the passenger-carrying EH216-S.

The diversity of our product strategy brings various commercial solutions suitable for our diversified customers and market demand, and also generates extensive revenue streams for our multiple business lines of air mobility solutions, smart city management solutions and aerial media solutions.

Strong in-house research & development and production capabilities

Our cutting-edge AAV technologies and products rely on our strong in-house R&D capabilities. Motivated by Mr. Huazhi Hu, our founder, chairman and chief executive officer, who has a life-time passion and strong technical expertise in both aviation and command-and-control systems, we value the engineer culture and talents, and keep focusing and investing in technology innovation and product R&D since day one.

As of December 31, 2022, our R&D team accounted for 55.7% of our total employees. As of March 31, 2023, we had 331 issued patents, 302 pending patent applications, and 371 registered software copyrights in China, to protect our key technologies and intellectual property and maintain our core competitiveness in the long term.

We are the first eVTOL company in the world having established a production base with production capabilities of passenger-carrying AAVs. Our Yunfu Production Facility ran into operation in June 2021, with an initial annual capacity of 600 units of the EH216 series AAVs, which is also expandable as needed. It is close to plenty of top-tier suppliers located in the Pearl River Delta area in China, and has a planned total gross floor area of approximately 24,000 square meters and 115 manufacturing team members as of December 31, 2022. This lays a solid cornerstone of our high-quality, efficient and sufficient product manufacturing and delivery capabilities.

Strong customer base and wide partnership network across the value chain to enable UAM ecosystem and commercial operations

With the first type of passenger-carrying AAVs available in the market ahead of other eVTOL aircraft, we have accumulated a strong customer base and wide partnership network with key stakeholders worldwide including regulators, public sectors, aviation companies, tourism companies, real estate companies, vertiport designers and constructors, telecommunication providers, Maintenance, Repair and Overhaul ("MRO") service providers, industry associations, etc. We have also participated in a number of European Union's UAM demonstration projects. Our joint efforts and collaborations across the value chain will empower the UAM ecosystem for commercial operations and sustainable development.

Meanwhile, this has generated a growing product demand for our AAV products and solutions. As of March 31, 2023, our order pipeline for the EH216-S has exceeded 100 units in China market, while the pre-orders we had received for the EH216 series and the VT-30 were more than 1,200 units in overseas markets on a cumulative basis. It has formed a solid foundation for our future revenue growth after the completion of type certification.

Our Leading AAV Solutions

Adhering to the three fundamental technological principles to ensure safety, which are redundancy, autonomous flying, and cluster management, we have designed, developed and provided turnkey total solutions to our customers including our proprietary AAVs, related AAV operating systems and infrastructures.

AAV Models

Based on different designs, sizes and uses, our AAV product family consists of the EH216 series, the VT series, the Falcon B, the GD series, and more types in our development pipeline.

• EH216 Series

The EH216 series consists of the EH216-S (standard model), the EH216-F (firefighting model), and the EH216-L (logistics model). By a multirotor configuration with less complexity and strong reliability, the EH216 series adopt a distributed electric propulsion with 16 propellers driven by 16 independent motors mounted on 8 arms, which not only ensures redundancy and flight safety, but also enables stable and accurate navigating, vertically takeoff and landing in urban airspace. With the eight arms folded, the size of the EH216 series is similar to a private car, taking minor space for storage and vertiports than helicopters and most of other eVTOL aircraft, so as to provide higher flexibility and operation efficiency especially in urban areas.

Our flagship product the EH216-S is an electric dual-seat passenger-carrying AAV launched in 2018, the next generation upgraded from the EH184 and the EH116, the original single-seat prototypes of our electric passenger-carrying AAV. Designed for short-to-medium-range low-altitude intra-city air mobility, it has a suitable flight performance for urban environment, the maximum flight range of 30km, the maximum flight time of 25min, and the cruising speed of 100km/h. With 220kg payload, the EH216-S can carry two passengers and an 18-inch luggage per flight, with no pilot onboard, and fly autonomously from the origin to the destination. Through a large panoramic windshield for wide vision and an intuitive tablet interface in front of the seats, passengers can enjoy the bird's eye view, check the real-time flight status, and communicate with ground crew for support if needed. The modularized structure with an upper cabin for passengers and a lower compartment to house major components and sub-systems ensures structural safety to better protect passengers.

The EH216-F is an electric firefighting AAV launched in July 2020. It's developed from the EH216-S and customized for high-rise firefighting. It is equipped with customized firefighting devices, such as fire extinguishing projectiles and launchers, a firefighting foam tank and a high-pressure nozzle. It is capable of flying up to 600m height to distinguish high-rise fires accurately and efficiently, while traditional rescue ladders and fire nozzles cannot reach the height. In July 2021, the EH216-F has passed a comprehensive 10-month technical examination to prove its reliability and performance through 52 different types of tests by the China National Fire-Fighting Equipment Quality Supervision Testing Center, which is under the Ministry of Emergency Management of China.

The EH216-L is an electric logistics AAV launched in September 2020. It's developed from the EH216-S and customized for cargo transportation with 250kg payload.

• VT Series

The VT series refers to a series of electric lift-and-cruise AAVs we have designed and developed, consisting of the VT-30, the VT-20, and the VT-10. They combine the advantages of both multirotors and fixed wings, enabling vertically takeoff and landing and longer flight range than multirotor aircraft, while with no requirement for large infrastructures such as runways.

The VT-30 is an electric dual-seat passenger-carrying AAV. Complementary with the short-to-medium-range EH216-S designed for intra-city air mobility, the VT-30 is designed for long-range inter-city air transportation, driven by eight propellers and fixed wings on both sides, as well as a tail wing and a propeller at the rear, to achieve a maximum balance of lift and push. It's designed for a maximum flight range of 300km and a maximum flight time of 100min.

The VT-20 and the VT-10 are electric medium-sized AAVs with four propellers and fixed wings. They are designed for long-range surveillance, power line inspection, delivery, and others.

The VT series are currently under internal testing, and have not begun their deliveries.

- **Falcon B**

The Falcon B is an electric medium-sized industrial AAV. It is a multirotor with 8 propellers, able to carry 5kg payload to fly 19km in 17min at the maximum speed of 80km/h. As a highly adaptable and extensible flight platform, the Falcon B provides a compatible interface which can be connected and equipped with different custom modules for various industrial uses, such as cargo holds for food or emergency delivery, infrared cameras for forest fire inspection, high-resolution zoom cameras for traffic and facility monitoring, loudspeakers and headlamps for patrolling, etc. They were usually delivered to and adopted by our customers for smart city management.

- **GD Series**

The GD series refers to our small-sized quadrotor AAVs, consisting of the GD2.0X used for aerial surveillance, last-mile delivery, aerial media performances and others, and the GD3.0 specially for aerial media performances.

AAV Operating Systems

We have proprietarily designed and developed an integrated and digitalized AAV operating platform with airborne operating systems installed in our AAVs, the command-and-control system, the UAM flight operation and management platform, and related infrastructure to allow our AAVs to operate in various scenarios safely and efficiently. The AAV operating systems for different AAV commercial solutions share the same underlying technological architecture.

Our AAV airborne operating systems include an autopilot and flight control system, a communication system, a battery management system and a safety management system, among other things. They are installed on each of our AAVs to enable autopilot, navigation, real-time monitoring, control and performance adjustment. Human control can be exercised from the ground using smartphones, tablets or computers as well as through our command-and-control system, meeting the varied demands of our customers or passengers and contingencies.

- **Autopilot and Flight Control System**

The autopilot and flight control system enables the autonomous operation of our AAVs without any human pilot onboard and helps to ensure that our AAV flies in a pre-determined route from the origin to the destination with precise vertical take-off and landing.

- **Communication System**

We have developed proprietary network protocols based on advanced communication technologies to support high-speed wireless networks between our AAVs and ground command-and-control system. Our communication system is secured with data-encryption technologies for data security. We also use redundant data transmission links, which enable us to switch to a backup communication system if the primary system is breached.

- **Battery Management System**

Our intelligent battery management system, or BMS, is an industrial-grade solution that monitors all parameters of AAV batteries, including temperature, capacity and voltage. The core of our BMS is the self-adaptive smart battery management algorithm that optimizes the balance between performance and battery life and provides accurate predictions based on data and analysis of flight status. To ensure effective management of battery performance and battery life, an onboard battery management unit transmits real-time BMS data to the flight control system and command-and-control system.

- **Safety Management System**

Our AAVs use full-redundancy safety technologies in their flight control system, sensors, propulsion system and battery management system. Our proprietary redundancy control algorithms are based on a real-time voting mechanism. Our AAVs are designed with distributed electric propulsion, with an aim of achieving the highest level of safety through redundancy and efficiency. In the event of malfunction of certain parts of our AAVs, the operating systems automatically activate the backup components to ensure proper functioning and performance of our AAVs.

- **Command-and-Control System**

We have extensive expertise in command-and-control system. Our proprietary command-and-control system can accurately monitor in-flight status, dispatch aircraft, effect pre-warning and contingency measures, etc. The system ensures that our AAVs fly in pre-determined routes and maintain smooth and efficient operation. It also has the capability to monitor and detect irregularity in the status and operation of our AAVs and to activate contingency measures to restrict and limit actions or movements of our AAVs in emergency situations.

Powered by advanced AAV technologies, our command-and-control system allows for adaptability and scalability. Through continuous uplinks maintained between AAVs and the ground command-and-control system, we are able to simultaneously manage up to 3,500 units of AAVs with precision and accuracy to complete pre-defined actions and movements in the air for aerial media shows.

Beside the command-and-control system for large-scale operations and management, we have also developed an app to enable standalone operations through portable smartphones, tablets or computers to individually monitor and control our AAVs.

As of December 31, 2022, we had delivered four command-and-control centers or systems to our customers for smart city management in Shaoguan, Lianyungang, Hezhou and Shenzhen, in China.

- **UAM Operational Platform**

Digitization is essential for UAM flight operation and safety management. We have built a digital UAM operational platform architecture and established a visualized flight operation module for managing the EH216-S flight schedule, ground crew, availability of vertiports and landing pads, and other factors across the entire front-line UAM operational process. This platform, which has been put into trial running internally, is designed to connect and interact with the back-end command-and-control system, as well as the front-end flight booking and payment service windows through either our own app or third-party apps, in order to provide the operation team with a clear and efficient management platform, and offer passengers a smooth flight booking and riding experience.

Infrastructures

- **Vertiports**

Vertiports are also essential for eVTOL aircraft operations and mobility efficiency. We have developed a set of requirements and different concept of designs for our electric AAV vertiports, or we call it E-Ports.

Taking the EH216-S as an example, each E-Port is identified and registered in our UAM flight operation and management platform, therefore our AAVs can serve for on-demand flights only within E-Port network to ensure safety and autonomy.

E-Ports can locate at the rooftop, on mountains, near to parking lots, subway or railway stations, airports or harbors, so as to seamlessly connect with other transportation nodes to expand the three-dimensional travel networks.

The scale of each E-Port is determined by the customer demands, density of flight routes and traffic volumes. It could be either a simple landing pad, or a hub station with several landing pads, charging piles, passenger service areas, hangars for storage and maintenance, and more facilities.

Leveraging the advantages of EH216-S's smaller size, lighter weight, lower noise, higher flexibility compared with helicopters or large eVTOL aircraft, the E-Port network is easier to be deployed, established and expanded by operators in urban areas with lesser costs and time. Usually, our customers and partners take the role to build E-Ports for their own operations, while we provide designs and requirements.

- ***Charging Piles***

We have developed and upgraded several generations of efficient and intelligent charging piles for our electric AAVs, and have delivered to our customers along with our AAV products. Powered by fast charging technologies, our charging piles are able to fully charge the EH216 series in approximately 90 minutes. They can also monitor real-time charging status and battery health.

Our Business Lines

Based on our proprietary innovative AAV solutions, we have established three business lines, which are air mobility, smart city management, and aerial media solutions.

Air Mobility Solutions

Air mobility is our main business line. We provide customers with safe, autonomous, eco-friendly and efficient AAV products, solutions and operational services for air transportations of passengers, cargos, emergencies, etc.

- ***Passenger Transportation Solutions***

We provide safe and efficient options for low-altitude short-to-medium-range urban air transportation solutions and services to our customers currently with our EH216-S AAVs. In addition, we intend to extent to long-range inter-city air transportation by introducing the VT-30 into the market in the future.

Our main customers are public and private enterprises in the tourism and aviation industries. They can utilize our passenger-carrying AAVs in their UAM operations and businesses for autonomous flight experience, aerial sightseeing, island hopping, medical transport, emergency rescue, airport shuttle, urban commuting services, etc. Compared with the customers' conventional option of helicopters, our EH216-S AAV solutions have much lower lifetime cost than helicopters by greatly decreasing acquisition price, maintenance costs, and pilot expenses, while providing safer, autonomous, eco-friendly and quieter new way of air mobility.

China is our principal market. Driven by increasingly favorable policies and regulations for civil unmanned aviation and low-altitude economy in recent years, the massive local market demand for various commercial applications, and the advancement of our EH216-S type certification with the CAAC, we have received an increasing number of orders and purchase intentions from our customers in China since 2022. As of March 31, 2023, the order pipeline for the EH216-S has exceeded 100 units in the China market, and is continuously growing. These orders are expected to be fulfilled within one to three years after the EH216-S type certification is completed.

In June 2022, Tianxingjian Cultural Tourism Investment and Development LLC., an affiliated enterprise of the Jishou city government in China's Hunan province, placed an order for five units of the EH216-S, which have been delivered already, with the plan to develop a scenic flight project at the Aizhai Wonder Tourist Area in Jishou and to purchase an additional 25 units as the project progresses.

In December 2022, Qingdao West Coast New Area, one of China's national new areas in Shandong province, formed a strategic partnership with us with the goal to make Qingdao a world-class UAM application demonstration area and, as of the date of this annual report, has provided a US\$10 million investment to us by purchasing newly issued Class A ordinary shares from us.

In March 2023, Xiyu Tourism Development Co., Ltd. (300859.SZ), a leading tourism company in Xinjiang, signed a cooperation framework agreement with us with the purpose to develop low-altitude tourism and sightseeing projects with our AAVs in the Heavenly Lake of Tianshan, a national 5A-class tourist attraction, and other scenic areas in Xinjiang, China. Both parties plan to set up a joint venture to operate a minimum of 120 units of the EH216-S or our comparable passenger-carrying AAVs in the next five years.

In March 2023, Xi'an Aerospace Investment Co., Ltd., backed by the Xi'an municipal government, reached a strategic partnership with us and placed an indicative purchase order for 20 units of the EH216-S, the fulfillment of which is expected to be completed by 2025. They plan to develop a smart air city and a low-altitude flight demonstration area in Northwest China.

Meanwhile, we explored and expanded broader Asian markets, and received sizable pre-orders from our customers for a total of 200 units of the EH216 series and 11 units of the VT-30 in 2022. In Japan, we cooperated with AirX Inc., a leading air mobility digital platform company, and MASC, a Japanese aerospace research institution, to have demonstrated EH216-S autonomous flights for multiple applications across six cities in Japan, and also secured a pre-order for 50 units of the EH216 series from AirX Inc. and the first order for the VT-30 and from MASC. In Malaysia, we entered into a strategic partnership with AEROTREE, a Malaysian aviation company, for developing UAM businesses, including MRO and training, and obtained a pre-order for 50 units of the EH216 series and 10 units of the VT-30. In Indonesia, we partnered with Prestige Aviation, an Indonesian aviation company, and received a pre-order for 100 units of the EH216-S. In Thailand, we formed a strategic partnership with Charoen Pokphand Group Co., Ltd., one of the nation's largest conglomerates, with an intent to establish a joint venture there for our AAV sales and UAM operations.

In Europe, we continued active participation and contribution in several UAM projects in 2022. We completed EH216 flight demonstrations in Spain under the European Union's AMU-LED project, one of Europe's largest UAM demonstration projects, to verify and validate the UAM Concepts of Operations. We also participated in the SAMVA project, under an initiative of the European Union Agency for the Space Programme, for deploying European Geostationary Navigation Overlay Service on eVTOL aircraft operations, to enhance advanced air mobility services and U-Space airspace integration across the continent. In addition, we assisted the Spanish National Police to complete the EH216 maiden flight and initiate its trial operations for emergency and public safety missions in Spain.

- **Logistics Solutions**

Our AAVs are capable of providing autonomous aerial logistics solutions and services, covering from last-mile deliveries to inter-city logistics transportation. Our AAVs are designed to carry and transport goods, cargo, emergency and medical supplies. In addition to offering logistics AAVs, we also design and develop customized aerial logistics solutions and relevant command-and-control systems on the back-end. The target customers of our logistics solutions are logistics or delivery service providers.

We entered into a 15-year development and conditional purchase agreement in 2016 with Lung Biotechnology PBC, a wholly-owned subsidiary of a U.S. biotechnology company United Therapeutics Corporation (Nasdaq: UTHR), with the aim to enable routine fully-autonomous organ delivery missions from its facilities to hospitals for transplant. The customer intended to purchase 1,000 units of customized AAVs upon achievement of specified performance milestones and that the customer obtains required approvals from the FAA and the FDA for their commercial operation of our AAVs. As of December 31, 2022, we had delivered five units of passenger-carrying AAVs to this customer for their trial operations conducted in Canada.

During the COVID-19 outbreak, we assisted local governments and medical institutions to transport emergency and medical supplies by utilizing the EH216-L and the Falcon B (logistics model) AAVs to complete autonomous, contactless, efficient air delivery missions in Guangzhou and Hezhou, China.

Smart City Management Solutions

We believe we are the first company having developed and delivered the smart city management solutions with integrated and intelligent command-and-control systems or centers that can centralize and coordinate a wide range of AAV applications simultaneously. We customize and adapt our AAVs to capture live videos, images and data generated by attached modules such as cameras, electro-optical, infrared or other sensors, and loudspeakers as our customers' requirements. The signals and instructions are wirelessly transmitted through high-speed telecommunication network between AAVs and the command-and-control systems we develop for our customers, enabling our customers to receive and send crucial information in real time remotely and safely.

The main customers of our smart city management solutions are public sectors. We provide an integrated and efficient digital platform with customized AAV models as turn-key solutions for monitoring and management across many ordinary municipal functions and public utilities, such as traffic management, powerline inspection, environmental monitoring, firefighting, emergency rescue, aerial mapping, etc. Compared with the traditional manpower-and-time-consuming working mode, the cost-effectiveness and efficiency are greatly improved.

As of December 31, 2022, except for the first AAV command-and-control center established in Guangzhou for our own use, we had delivered four command-and-control centers or systems along with suitable AAV models as integrated packages for smart city management solutions to our customers in Shaoguan, Lianyungang, Hezhou and Shenzhen, China. These delivered command-and-control centers or systems are currently operated by our customers, while we provide related required trainings and technical supports. We will offer customers operational services for subscription fees if customers choose to outsource the operations of the command-and-control centers or systems. Besides, we sell AAVs to some smart city management customers on a standalone basis, which can be controlled by our app.

Aerial Media Solutions

We were the first company to launch the aerial media solutions in 2016 and are a leading player in China and Europe in providing aerial media performances, also known as drone light shows. Our services involve managing and choreographing a fleet of AAVs that are equipped with LED lights into a series of moving images. We utilize a range of proprietary navigation technologies, operating systems, and infrastructure to deliver smooth and mesmerizing AAV formations, synchronized movement and accurate display of two-dimensional and three-dimensional patterns, brand logos, or messages. Our remote command-and-control capacity and auto formation flight system enable us to support diverse flight missions and light effects with varying degrees of difficulties. We also use real-time kinematic satellite-based navigation technology (RTK-GPS) to achieve centimeter-level positioning precision for our AAVs.

We not only provide large-scale aerial media performance services for outdoor events such as celebrations, festivals, and brand campaigns, but also offer aerial media packages that includes our proprietary GD series AAVs and relevant software to our customers who are able to design and carry out performances themselves with our products.

As of December 31, 2022, we, together with our customers and partners, had completed approximately 200 aerial media performances by our AAVs in China and Europe. Moreover, we broke two Guinness World Records for our aerial media performances in China in 2018. We set the record for "The Most UAVs Airborne Simultaneously" by deploying 1,374 units of the GD2.0X, and we also set the record for "The Most Consecutive Formations Formed by UAVs Same Set".

Our Business Strategies

Extend our technological leadership

We plan to continue to invest in technological innovation to cement our leadership in AAV technologies and establish ourselves as the industry benchmark for AAV commercial solutions. We will continue to expand our talent pool and intellectual property, and drive innovation.

Expand our AAV portfolio and strengthen our platform

We plan to continue to optimize our existing AAV models, expand our AAV portfolio, and obtain required certificates for commercial applications. We will develop future AAV models for different uses. We will continue to develop our technology platform and ancillary products and services to strengthen our ability to provide end-to-end AAV commercial solutions that address the growing needs of our customers.

Take advantage of the first AAV type certificate to be obtained for entry into market

We aim to be the first mover enabling passenger-carrying AAVs entry into market for commercial operations in China by taking advantage of the EH216-S type certificate we are expected to obtain from the CAAC. Then we plan to extend to more countries in Asia and other regions worldwide by potential bilateral agreements between aviation regulators and required local certifications.

Capitalize our first mover advantages to continue commercialization and promote adoption

We will capitalize our first mover advantages and capture the window period with no direct competitions before any other eVTOL products entering the market, and we will deliver our accumulated backlog orders, develop our AAV business, and expand our market share. We will continue to commercialize our AAV technology and solutions and promote their adoption worldwide, not only through the sale of our AAVs, but also through offering flight operational services. As we continue promoting the regulatory and social acceptance, infrastructure network establishment, and industrial deployment, we will collaborate with our customers and partners to pilot air mobility services with predetermined routes as a precursor for more flexible, on-demand services networks starting from scenic areas gradually to urban areas.

Keep enhancing commercial operation capabilities

We will keep developing and improving our UAM digital operational platform for an effective and efficient management of aircraft, flight schedule and routes, ground crew, vertiports, air traffic, and approved airspace. In addition, we will continue to enhance commercial operation capabilities by expanding air mobility operation team, improving operational standards and rules, and exploring feasible and replicable commercial operational mode together with our business partners. With that, we will continue to expand efforts under our 100 Air Mobility Routes Initiative.

Explore new monetization opportunities and develop diversified revenue streams

We plan to explore new monetization opportunities and develop diversified revenue streams by leveraging our fundamental AAV technology platform to pursuit operating synergies across our business lines and better economic efficiency. For example, we may charge recurring fees for our software system licenses, operational and maintenance services for our AAVs. We may also enter into revenue sharing, financial leasing, strategic investment arrangements with customers to capture flexible and greater business opportunities.

Expand strategic partnerships across the value chain to develop a sustainable UAM ecosystem

We plan to continue to expand our partnership network across the value chain in the global UAM industry with business partners and regulatory agencies to foster and grow the commercial AAV market and develop a sustainable UAM ecosystem.

Research and Development Capabilities

Our in-house design, development and engineering capabilities underpin our leadership and support the advancement of our platform. Our design is characterized by unabated efforts to improve safety, reliability and functionality. We have a dedicated research, design and development team in Guangzhou. The team consists of members with strong backgrounds in the fields of electrical engineering, aerospace engineering, mechanical engineering, automation, material engineering and software development. The key R&D team members are mainly graduates of top universities. Our research and development team focuses on core research development, engineering technology, hardware development, and command-and-control systems of AAVs. We have a dedicated software technology group to lead the research and development of AAV software and algorithms.

Our success has been driven by a passionate, visionary, tech-savvy and entrepreneurial management team with a unique combination of aviation, internet and software expertise. Our founder, chairman and chief executive officer, Mr. Huazhi Hu is one of the pioneers and leaders in the global AAV industry, who was awarded the Technology Innovation Award by the Living Legends of Aviation Europe in 2019 and ranked the Top one inventor at air taxi firms, who personally took 10% share of all patents filed globally as of August 11, 2022 according to a Roland Berger analyst's research. As a Tsinghua University-trained software engineer, Mr. Hu has amassed substantial experience in the development of command-and-control systems. He was one of the key architects and lead developers behind certain large-scale command-and-control systems, such as that for the 2008 Beijing Olympics.

At our R&D center, we have pioneered a multitude of AAV flight tests for airworthiness, including climbing flight tests, high-maneuver flight tests, speed flight tests, night flight tests, as well as flight tests in harsh weather conditions, including low visibility, high and low temperatures, typhoon and fog. Our EH184, EH116 and EH216 series AAVs have completed more than 35,000 safe trial flights in 12 countries across Asia, Europe and North America, predominantly in China as of March 31, 2023. These trial flights include passenger-carrying flights and flight tests in winds of up to 70 kilometers per hour, in fogs with a visibility of approximately 50 meters, at an air temperature of 52 degrees Celsius and minus 14 degrees Celsius, and at a flight altitude of 4,100 meters above sea level. These tests will help us validate airworthiness of our AAV products from the design phase to full-scale production while delivering highly reliable and quality AAVs.

Manufacturing, Quality Control and Supply Chain

As an original equipment manufacturer of AAVs, we adopt a safe, compliant, lean and efficient production strategy across our business, focusing on effective prototyping, manufacturing, supply chain management, final assembly, integration, quality control and final acceptance testing.

Manufacturing

We currently have an AAV production facility in Yunfu city, Guangdong province, China, which commenced operation in June 2021. It has a planned total gross floor area of approximately 24,000 square meters, equipped with a series of function areas across the production processes for different types of our AAV models from manufacturing of key components and carbon fiber composite airframes to aircraft assembling and flight testing. The Yunfu facility has a planned initial annual capacity of 600 units of the EH216 series AAVs, which can be further expanded as the sales volume increases in the future.

To ensure high levels of quality and reliability, our dedicated manufacturing team, in close collaboration with our design and engineering arm, manages and conducts the design, engineering and production of key proprietary AAV components, such as flight control system units, communication system units, battery management system units and motor drivers, and performs in-house final assembly of our AAV products.

Our production partners are subject to rigorous selection and review procedures. All of our production system operations incorporate internal and external quality programs and processes to ensure our required standards for acceptance rates, reduce lead times and lower cost.

Quality Control

Our quality control efforts focus on designing and producing products and implementing processes that will ensure high levels of safety and reliability. We have a dedicated quality control team that works with our engineering arm and our suppliers to ensure that the product designs meet safety requirements and functional specifications. Together with our supplier review committee, our quality control team also collaborates with our suppliers to ensure that their processes and systems are capable of delivering the parts and components we need at the required quality levels, on time and within budgets.

Our AAVs are produced with strict product quality control. Our quality control team undertakes robust inspections of our production lines in accordance with internal guidelines and assessment criteria. We also conduct licensed flight tests for our AAVs under a variety of conditions, which have proven to be an efficient and effective means for us to assess the quality and airworthiness of our products. Data and results generated from flight tests are carefully studied and analyzed to inform any process of alteration or improvement that may follow. In conjunction with our provision of a broad range of after-sales services and assistance to our customers, our AAV quality control management extends beyond the point of sale as we continue tracking the performance and quality of our AAVs.

We are committed to a high level of quality assurance. Since 2017, we have been certified to AS9100, a globally recognized aerospace and aviation quality management system standard.

Supply Chain

We adopt a strict reviewing mechanism to ensure quality and stability of our supply chain. We also aim to fully engage with our suppliers to foster long-standing and strong partnership with qualified suppliers. Our production facility is located in the Pearl River Delta area, a world-leading manufacturing hub, giving us easy access to a large number of high-quality suppliers in an efficient manner. Our AAVs are generally manufactured on specific orders and we have been able to effectively manage our inventory level. Historically, we have not experienced significant delays in the supply or availability of our key raw materials or components provided by our suppliers, nor have we experienced a significant price increase for raw materials or components.

We require our suppliers to maintain high-quality deliverables and to comply with specified industry standards. Parts and components sourced from our suppliers must be certified by the China Compulsory Certification or the Underwriters Laboratory, and/or certified with the ISO 9001. Our suppliers of key parts and components are additionally required to be certified with AS9100 or alternative equivalent certificates. We regularly monitor the performance of our suppliers using parameters such as supplier defect rates, production and delivery performance, as well as inventory management.

Marketing, Sales and After-Sales Services

Marketing

As the first mover in the emerging UAM industry, we have spent years dedicated to educate the stakeholders of regulators, partners, customers and end users with our innovative and cutting-edge AAV technologies and knowledges, to increase social acceptance of this new way of air mobility, and to promote the visibility of our EHang brand and products globally. We believe these are necessary and significant efforts to accumulate our customer base and partner network, to cultivate the new market from the infancy stage evolving to the mature period, and to catalyze the establishment of UAM ecosystem for the commercial operations.

We kept communicating with our customers, investors and followers through multiple domestic and international online and offline channels and activities, including but not limited to our website, various social media and video platforms, hotlines and emails, mainstream media coverages, brand and product launch events, high-profile exhibitions and industry conferences, worldwide trial and demonstration autonomous flights, etc. The consistent exposures and marketing efforts contributed to our brand awareness, reputation and sales leads.

We issued a white paper entitled The Future of Transportation: White Paper on UAM System in January 2020, which explored in depth UAM's potential to transform transportation globally with insights into vehicle design, an overview of potential applications and regulatory landscape, and our recommendations as to the optimization of UAM's path towards commercialization. We believe this white paper has facilitated the education of the emerging market at the early stage and consolidated our thought leadership as the first mover in the innovative industry.

Sales

We adopted the direct sales model to sell our AAV products and solutions to our customers, which are mainly public and private enterprises. We have established an in-house direct sales team based in the PRC and Europe to serve our customers from around the world. We are also in discussion with existing and potential business partners in the PRC and abroad to complement our direct sales efforts with sales to distributors and franchise arrangements.

On top of our sales in the PRC, we have exported our AAVs to Asia, Europe, North America and Latin America. We strive to ensure that our exported products comply with the regulatory and safety standards of the local markets.

Our customers place purchase orders taking into account the terms of the relevant framework agreement, if applicable, and the customer's procurement requirements. We start production after the purchase order from customers is made, and production generally takes three to six months to deliver. Customers are contractually required to make upfront payment to us.

Except for purchase orders, we have also entered into a number of long-term framework and conditional agreements time to time with our customers and business partners relating to preorder or distribution of our AAV solutions. These non-binding agreements do not obligate the customers to purchase the products unless certain conditions are satisfied. Fulfillment is expected to take several years and is conditional upon, among other things, achievement of performance milestones and receipt of regulatory approvals. See "Item 3. Key Information—D. Risk Factors—Risks Relating to Our Business and Industry—Our framework and conditional agreements may not result in material sales of our products."

After-Sales Services and Warranty

We provide after-sales services for customers of our AAVs. We currently offer free installation and training programs thereafter to prepare our customers for its safe operation. The term of our warranty for the EH216 series AAVs is six months to three years depending on the specific parts and components, and the term of our warranty for our small-and-medium-sized AAVs is from six to twelve months depending on the product line and the specific parts and components. Within the warranty period, customers are entitled to free repair and maintenance services, while costs for accessories and maintenance fees beyond the warranty will be charged separately. The warranty on certain components of our AAVs, such as batteries, is covered by our suppliers' back-to-back warranty and we are entitled to have the suppliers replace or repair these defective components at their costs. We also provide our customers with lifetime consulting services on maintenance and operation through our website, over the telephone and via email.

For our AAV commercial solutions, we provide a full spectrum of services. To facilitate the efficient operation of our AAV command-and-control systems, we provide, among others, system operation and maintenance training, service support, engineering support, inspection and repair, technical consulting support, and data and documentation assistance. Our customers enjoy services throughout the operational life of our command-and-control systems. Most of these services are performed on-site.

We continue to maintain and upgrade our AAV software infrastructure to enhance the functionality, reliability and safety of our AAVs. We regularly inspect, maintain and upgrade the fundamental communication network and transmission system to ensure the smooth communication between our AAVs and the command-and-control systems.

In addition, we will leverage our partners' strength and network to enhance our service and maintenance capabilities. For example, we have established a partnership with Hong Kong Aircraft Engineering Company Limited ("HAECO"), a subsidiary of Swire Group and a world leading aircraft engineering and maintenance company, to cooperate in multiple areas such as continued airworthiness, digital platforms, after-sales maintenance service system, aircraft maintenance, and talent training for the commercial operation of our AAVs.

Operational Services

With our strategic positioning to be a UAM platform operator, we adopt an integrated business model by selling AAV solutions and providing operational services. We plan to initiate commercial operational services to our customers and end users after obtaining required certificates and approvals. Therefore, we expect to be the world's first company to start commercial operations of passenger-carrying AAVs or pilotless eVTOL aircraft initially in PRC once the EH216-S is certified by the CAAC.

In preparation for commercial operations, we have established a well-trained in-house air mobility operation team specifically for flight operations of our AAVs, including the staff for route planning, flight operations, safety management, regulatory compliance, digital operational platform, sales and marketing. Our key team members have previous operational experience at leading aviation, airline and mobility companies, such as Airbus, Hainan Airlines, Hong Kong Airlines, Hong Kong Express, BMW, CITIC COHC, etc.

As the pioneer passenger-carrying AAV enterprise for airworthiness certification appointed by the CAAC, we have been allowed and encouraged to carry out trial operations with our AAVs in China to accumulate trial data and experience. We launched the "100 Air Mobility Routes Initiative" in April 2021 with a goal to open up 100 AAV flight routes for air mobility and an initial focus on the Guangdong-Hong Kong-Macao Greater Bay Area of China. As of March 31, 2023, we and our customers have set up 18 operation spots in 16 Chinese cities, and carried out more than 8,200 operational trial flights with the EH216-S AAVs in the practical environment mainly for aerial sightseeing and tourism applications. In this process, we have been exploring and improving operational procedures and safety rules, running our digital UAM operational platform on a trial basis, and developing feasible, replicable operational expertise and mode. We and our customers plan to switch trial operations into commercial operations after required certifications are completed.

Competition

We operate in the emerging UAM industry, and provide various commercial solutions, including air mobility (consisting of passenger transportation and logistics), smart city management and aerial media solutions. Our air mobility solutions may be alternatives with better efficiency and economics to those offered by traditional industry players, such as helicopters and ground transportation service providers. We believe the primary competitive factors in our markets include technological innovation, safety, certification, quality, user experience, and operational and manufacturing efficiency.

We believe we are the first mover and a leader in air mobility solutions. A number of other companies are also developing passenger-carrying eVTOL aircraft, but to our knowledge, none of these companies have delivered passenger-carrying AAVs to customers as of the date of this annual report. In other areas of our business, including logistics, smart city management and aerial media solutions, we also face several major competitors in separate field. We believe that we are strategically positioned in the commercial UAM market with exceptional AAV technologies, innovation capabilities, faster airworthiness certification progress, broad use cases and leading positions in providing integrated smart city management solutions and aerial media solutions.

Intellectual Property

We have significant capabilities in the areas of AAVs engineering, development and design and have developed a number of proprietary systems and technologies. Our success depends in part on our ability to protect our core technologies and intellectual property. We rely on a combination of patents, patent applications, trade secrets, know-how, copyrights, trademarks, intellectual property licenses and other contractual rights to establish and protect our proprietary rights in our technologies. In addition, we have entered into confidentiality and non-disclosure agreements with our employees and business partners. The agreements we entered into with employees provide that all software, inventions, developments, works of authorship and trade secrets created by them during the course of their employment are our property.

As of March 31, 2023, we had 331 issued patents, 302 pending patent applications, 371 registered trademarks, and 24 registered copyrights in China. We will continue to expand our intellectual property portfolio.

Seasonality

Because of our rapid growth, our overall business has not experienced a significant pattern of seasonality. However, some of our specific businesses such as aerial media solutions have showed seasonality in which we may receive more revenues from such business in major holidays. We may also have a lower number of deliveries of our AAVs in the first quarter of each fiscal year due to holiday seasons. We may experience more pronounced seasonality as our business continues to expand.

Insurance

We maintain various types of insurance, employer's liability insurance, to protect assets in the event of any accident that might cause significant losses. We also purchase insurance policies that are either legally compulsory or required by our customers. For example, we maintain third-party liability insurance for UAVs, which is required for our UAV commercial operation license. We have liability insurances with coverage and conditions that we consider appropriate. For example, we maintain aviation product liability insurance, which covers bodily injury or property damage caused by defects in our products. In relation to our passenger-carrying AAVs in operation, we have maintained airplane body and flight insurance to cover damages to passengers and third-party liabilities. We believe that our insurance coverage is adequate to cover our key assets, facilities and liabilities.

PRC Regulation

This section sets forth a summary of the most significant rules and regulations that affect our business activities in China.

General Administration of Civil Aviation and Airspace Control

On October 30, 1995, the Standing Committee of the National People's Congress of the PRC, or the SCNPC, adopted the *Civil Aviation Law of the PRC*, or the Civil Aviation Law, which was subsequently amended on April 24, 2015, November 7, 2016, November 4, 2017, December 29, 2018, and April 29, 2021, respectively. The Civil Aviation Law sets forth the general principle and rules for administration of civil aviation as well as for domestic airspace control. Pursuant to this law, the CAAC, which is a State Council department, is currently in charge of civil aviation and has the general authority to supervise and administer civil aviation activities nationwide. The CAAC may promulgate regulations concerning civil aviation activities in accordance with laws enacted and decisions issued by the State Council and within the limits of the CAAC's authority. According to the Civil Aviation Law, the state has complete and exclusive sovereignty over the airspace above its territory. The division of airspace must take account of the needs of civil aviation, national defense and security, as well as the interests of the public, so as to ensure the reasonable, sufficient and efficient use of airspace. Detailed measures for airspace control will be formulated by the State Council and the Central Military Commission, or the CMC. In addition, pursuant to the Civil Aviation Law, the detailed rules of UAVs promulgated by the State Council and the CMC shall be followed.

Design, Manufacturing and Airworthiness Standard for UAVs

The Civil Aviation Law contains rules and regulations on airworthiness for all civil aircrafts other than those used for flight missions by the military force, customs offices and police departments. The law mandates that the design of engines, screw propellers and apparatuses used in civil aircrafts must be approved with a Type Certificate, whereas the production and maintenance of engines, screw propellers and apparatuses used in civil aircrafts require a Production Certificate and a Maintenance Certificate, respectively. In addition, after the completion of nationality registration with CAAC, the civil aviation will possess the nationality of PRC. An aircraft possessing the nationality of PRC may take flight if it holds an Airworthiness Certificate.

Designing our AAVs: Type Certification issued by CAAC shows that the design of the aviation products or its component parts meet the requirements under applicable airworthiness regulations. Our AAVs, as a special category aircraft under Section 21.17 of Certification Procedures for Civil Aviation Products and Parts, or CCAR-21, is required to meet the criteria set forth in the *Special Conditions for Type Certification of EH216-S Unmanned Aircraft System*, or the Special Conditions, promulgated by the CAAC on February 9, 2022. The Special Conditions provided clear safety requirements for the type certification of EH216-S, including flight performance, aircraft structures, design and manufacture, propulsion systems, data link, ground control station, etc. Following the Project Specific Certification Plan and the Certification Plan with solid means of compliance that the CAAC has approved, as of the date of this annual report, we have completed 75% of the compliance tests to demonstrate and verify the airworthiness of the EH216-S.

Manufacturing our AAVs: Production Certification issued by CAAC shows we are able to manufacture our aircraft or components with approved quality system under an CAAC-approved type design. To obtain Production Certification from the CAAC, we must demonstrate that our organization and our personnel, quality manual, facilities, and quality system can produce our aircraft such that they conform to its approved design. We are working to develop the systems and processes we will need to obtain CAAC production certification with the goal of obtaining such certification shortly following receipt of our type certificate.

Airworthiness Standard of our AAVs: Airworthiness Certification from the CAAC signifies that an aircraft possessing the nationality of PRC may take flight. On December 19, 2022, the CAAC published *Administration Procedure for Certification of the Airworthiness of Civil Unmanned Aerial Vehicle System Guidance*, or UAV Airworthiness Procedure, which is guide and regulate the type certificate, production certificate and airworthiness of Unmanned Aerial Vehicle System in medium and large size. According to UAV Airworthiness Procedure, airworthiness certificates for UAVs are divided into three categories, that is standard airworthiness certificate, special airworthiness certificate and special flight permit. We expect that the airworthiness certificates issued to our aircraft after the procurement of Type Certificate and Production Certification.

On January 25, 2019, the CAAC published the *UAV Airworthiness Guidance based on Operational Risks*, or UAV Airworthiness Guidance, pursuant to which we are one of the airworthiness assessment pilot programs and would help the CAAC in developing UAV airworthiness standards and assessment rules. According to the UAV Airworthiness Guidance, the UAV airworthiness framework will be based on the assessment, classification and management of operational risks.

On January 20, 2020, the Department of Aircraft Airworthiness Certification of the CAAC issued the *Airworthiness Standards for Fixed-wing Unmanned Aerial Vehicle Systems Used for High-risk Cargo Transportation (Interim)*, which are mainly applicable to fixed-wing unmanned aerial vehicle systems used for feeder cargo transportation under high-risk operating conditions. In July 2020, CAAC published *Data Specifications of Unmanned Aircraft Cloud System* for standard for cloud system of UAV. Some of our UAVs model may be required to meet specific industry requirements. In addition, on December 21, 2022, CAAC promulgated *Analysis Guideline for Determination of the Classification and System Safety of Civil Unmanned Aerial Vehicle Airworthiness*, pursuant to which, the operation risks of UAVs shall be determined by severity and possibility of integrated adverse effects, based on the potential adverse effects during the operation of the civil unmanned aerial vehicle system.

Pending the enactment of the foregoing bills and the necessary judiciary and administrative interpretations and clarifications on some of the existing guidelines, the CAAC has put in place interim measures to allow for and regulate the testing of various forms of UAVs. To speed up the building of legal and criterion system for civil unmanned aerial vehicle, CAAC also published *Guideline for the Construction of Regulation and Standard of Civil Unmanned Aerial Vehicles V1.0*, which will provide further details on airworthiness, flight operation and business operation.

Furthermore, in March 2020, the MIIT published the latest discussion draft of the *Administrative Measures on the Production and Manufacturing of Civil Use Unmanned Aerial Vehicles* or the Draft Production and Manufacturing Standards of UAVs, for public review and comments. The Draft Production and Manufacturing Standards of UAVs classifies UAVs into five types, namely, micro, light, small, medium, and large. Each UAV should have a unique product identification number. The MIIT is responsible for formulating relevant standards and regulations on the unique product identification codes of UAVs. UAV manufacturers shall enter the product identification code on the chip of a UAV in an inerasible storage area and also mark it on the body and outer package of the UAV.

Real-Name Registration of UAVs

As a manufacturer and seller of UAVs, we are required to collect certain information relating to our products and our customers and to submit such information to the relevant regional authorities pursuant to the *Circular of the General Office of the Ministry of Industry and Information Technology on Information Filing for Civil Unmanned Aerial Vehicle Production Enterprise and Products*, which took effect on May 22, 2017. We are also obligated to provide information relating to our AAV products and purchasers starting from June 2017 and pursuant to the *Administrative Provisions on the Real-name Registration of Private Unmanned Aerial Vehicles* issued by the CAAC. Information to be reported includes (i) the name, registered address and contact information of us as the manufacturer; (ii) the name and model detail of our AAV products; (iii) the empty weight and maximum take-off weight of our AAV products; (iv) the categorization of our AAV products in accordance with the CAAC guidelines, and (v) the name and contact information of purchasers of our AAVs. These administrative provisions regulate the use of private UAVs with a maximum take-off weight of 0.25 kilograms and above within the territory of the PRC, and direct owners of such private UAVs to register their UAVs on a real-name basis. Non-compliance will result in restrictions on the use of the relevant UAVs and penalties. We have historically complied with these requirements for our AAVs. The *Administrative Procedures for the Real-name Registration of Civil UAVs (Draft)* issued by the CAAC on March 30, 2020 make changes to the real-name registration process mainly for the purpose of making it more convenient for owners who purchase private UAVs. Specifically, it is stipulated that a manufacturer of UAVs shall register in advance the product information of its UAV products in the *UAV real-name registration system* in batches first, and then the owner of the UAV products can then search by the UAV serial number in the UAV real-name registration system for the pre-registered UAV system and submit additional personal information. On October 29, 2021, CAAC promulgated *Civil Unmanned Aircraft Registration Management Procedures (Draft for Comment)* which requires real-name registration and nationality registration.

Operations of AAVs

Airspace Control

According to the *General Flight Rules* issued by the State Council and the CMC on October 18, 2007 and took effect on November 22, 2007, the overall flight control within the territory of the PRC is under the unified organization of and enforcement by the People's Liberation Army Air Force, and the various flight control departments shall exercise air traffic control in accordance with their respective responsibilities. Prior application must be filed and approval be obtained before any flight can be conducted within the PRC territory, including test flights for our AAVs, and take-offs relating to our aerial media solutions and logistics services.

Our PRC related PRC operating entities are required to obtain clearance from the local counterpart of the People's Liberation Army Air Force for the flight routes for our AAVs. Subject to any difference in policies adopted by the local authorities, approval for airspace and flight plan is normally granted by the local flight control department of the military. The flight plan shall also be filed with the local public security department and the CAAC. As an example of the general observations above, on November 19, 2018, the CAAC issued the *Flight Management Implementing Rule for UAVs in the Shenzhen Area (Interim)*, under which the South Military Zone Air Force is responsible for the piloting of UAVs within the municipal area of Shenzhen. An enterprise or individual who seeks a flight task approval shall file the application with the flight control department of the South Military Zone Air Force five days prior to such flight. The flight control department of the South Military Zone Air Force, after consulting the CAAC and the public security department, may grant its approval two days prior to the flight. After such approval and except for certain flights of mini-UAV with an empty weight of less than 0.25 kilogram, subject to certain other conditions, or small-UAV with an empty weight of less than 4 kilograms, subject to certain other conditions, a flight plan must be submitted via a designated reporting platform no later than 3:00 pm on the day prior to the flight and the flight control department of the South Military Zone Air Force will respond no later than 9:00 pm on the same day of filing and will distribute the relevant information to the public security department and the CAAC. In addition, with the approval of Hainan Provincial Government, *Hainan Administrative Rule for Civil UAVs (Interim)* was promulgated in April 2020. Generally, for the flights of our AAVs, we, the VIE and the VIE's subsidiaries have established prior communications with the local flight control department, the public security authority and the local counterpart of the CAAC in seeking the necessary approvals and have ensured compliance with their respective instructions in all material respects.

Geo-fencing

The geo-fencing of UAVs is of great significance for the development of the industry. Currently, there is no effective unified standard for geo-fencing of UAVs in the world and various countries are in the exploration stage. In China, the CAAC issued the Standard of Fence of Unmanned Aircraft System (*Draft for Comment*) in 2017.

Both our EH216-S and Falcon B have passed the tests of geo-fencing by the Civil UAS Inspection Center of China Academy of Civil Aviation Science and Technology (CAST), and obtained the certificate from the China National Accreditation Service for Conformity Assessment (CNAS) and ILAC-MRA in July 2019, which is internationally recognized.

Pilot Operations

The Department of Flight Standard, the Department of Aircraft Airworthiness Certification and the Office of Air Traffic Regulation of the CAAC, jointly issued the *Pilot Operation Rules (Interim) for Specific Unmanned Aircraft*, or the Interim Rules, on February 1, 2019, pursuant to which, unmanned aircrafts are classified into nine categories based on their empty weight and takeoff gross weight. In particular, Class I captures unmanned aircrafts with empty weight and takeoff gross weight between 0 to 1.5 kg (including 1.5 kg); Class II captures unmanned aircrafts with empty weight between 1.5 kg and 4 kg (including 4 kg) and takeoff gross weight between 1.5 kg and 7 kg (including 7 kg); Class III captures unmanned aircrafts with empty weight between 4 kg and 15 kg (including 15 kg) and takeoff gross weight between 7 kg and 25 kg (including 25 kg); Class IV captures unmanned aircrafts with empty weight between 15 kg and 116 kg (including 116 kg) and takeoff gross weight between 25 kg and 150 kg (including 150 kg); Class XI captures unmanned aircrafts with empty weight between 116 kg and 5,700 kg (including 5,700 kg) and takeoff gross weight between 150 kg and 5,700 kg (including 5,700 kg); Class XII captures unmanned aircrafts with empty weight and takeoff gross weight in excess of 5,700 kg. The Interim Rules are applicable to Class IV unmanned aircrafts, Class III unmanned aircrafts with high risks and the pilot operation of which would need a pre-assessment in the belief of the authority, Class XI and Class XII unmanned aircrafts with low risks and in relation to which the authority believes a pilot operation assessment is sufficient. According to the classification above, our EH216 series AAVs belong to Class XI and Falcon B belongs to Class III. According to the Interim Rules, the applicant for the pilot operation of any UAV that falls within any of the foregoing applicable classes shall first submit a proposal for initial discussion and application with the CAAC and shall then conduct a pre-pilot operation safety evaluation based on specific operation risk assessment, or SORA. The applicant shall subsequently verify the operation risks based on its initial operation, following which the CAAC shall issue the relevant approval if its assessment team confirms that the risks of pilot operation can be appropriately controlled and are acceptable. Upon its receipt, the applicant shall maintain the approval, together with the operation rules and a complete manual for the CAAC's inspection and supervision. The pilot operation will be suspended or terminated under certain circumstances, such as any non-compliance with the approved letter, the presence of uncontrollable operation risks and the voluntary surrender by the applicant. Operation records relating to pilot operations shall be maintained, including operation manual, list of unmanned aircraft, maintenance record of aircraft, and qualification of personnel. The applicant shall also purchase insurance policy for third party liabilities. In addition, "risks" is defined under the Interim Rules to take into account both the frequencies (or probabilities) of the events and the level of severity. It also includes both ground risks and risks in air.

MIIT also published Interim Rules on Flight Management of Unmanned Aircraft (Draft for Comment), or the MIIT UAV Interim Rules, on January 26, 2018, which provides that civil use unmanned aircrafts are classified into (a) micro unmanned aircraft which has empty weight no more than 0.25 kg, height capital less than 50 meters, max speed less than 40 km per hour and radio transmitting equipment meeting the technical requirements for micropower short-range radio transmitting; (b) light unmanned aircraft which has empty weight no more than 4kg, max takeoff gross weight no more than 7kg, max speed no more than 100km per hour and remote control with airspace maintenance capability and reliable surveillance capability that meeting airspace management requirement s; (c) small unmanned aircraft which has empty weight no more than 15 kg or max takeoff gross weight no more than 25 kg; (d) medium unmanned aircraft which has takeoff gross weight between 25 kg and 150 kg and empty wight more than 15 kg; and (e) large unmanned aircraft which has takeoff gross weight more than 150 kg.

UAV Commercial Operation License

The *Administrative Measures for Commercial Flight Activities of Unmanned Aerial Vehicle for Civil Use (Interim)* promulgated by CAAC on March 21, 2018 and taking effect on June 1, 2018, asserts jurisdiction over the commercial operation of any UAV with empty weight of more than 0.25 kilograms and regulates a broad range of UAV activities including aerial spraying, photography, aerial performance flight and UAV operator training. On August 4, 2020, the Ministry of Transport of the PRC promulgated Provisions on the Administration of Operation License for General Aviation, effective on January 1, 2021, pursuant to which, an enterprise engaging in general aviation operations shall obtain a general aviation enterprise operation license. Civil aircraft includes manned aircraft and unmanned aircraft. The company operating the regulated activities must first obtain a General Aviation Enterprise Operation License from CAAC for using UAVs in such activities, and the applicant shall meet certain criteria including, among others, (a) the applicant shall be a corporation having a PRC national as its legal representative; (b) the applicant shall possess proper civil aircraft meeting certain requirements, such as the completion of registration in PRC and the compliance with the related airworthiness requirements, standard airworthiness certificate for civil aircraft used for passenger carrying and human carrying business activities (unless otherwise stipulated by CAAC), the compatibility with the commercial general aviation activities to be engaged in, at least two civil aircrafts for engaging in passenger carrying business or one civil aircraft for human-carrying and other business; (c) there are pilots who are suitable for civil aircraft, having professional training and obtaining related license; and (d) the applicant shall have purchased third party liability insurance policy on the ground. The VIE and its subsidiaries have obtained the necessary operation licenses for aerial spraying, aerial photography, operator training, flight show, aerial media solutions and other purposes. The regulations on operations for UAVs are still evolving and may be subject to differing interpretations or significant changes. However, in the northwest region of China, the *Administrative Measures for Logistics Services of Civil Unmanned Aerial Vehicle in Northwest Region (Interim)* promulgated by CAAC Northwest Regional Administration on April 3, 2019, stipulates that the company operates logistic services in Shaanxi Province, Gansu Province, Ningxia Province and Qinghai Province by UAVs shall obtain an operating license for logistic service from CAAC Northwest Regional Administration. We are not operating logistic services in northwest region of China at the current stage. We may be required to obtain the Operation License for logistic service if we operate logistic services in Northwest region in the future.

Pilot and Operator License

On August 31, 2018, the Flight Standard Department of the CAAC issued the *Regulations on the Administration of Civil Unmanned Aerial Vehicles Pilots*, according to which a UAV pilot must obtain the relevant UAV pilot license depending on the type and specifications of the UAV operated. On December 23, 2021, CAAC promulgated *Consultation Circular Soliciting Comments on Regulations on the Administration of Civil Unmanned Aerial Vehicles Pilots*, or Draft New Regulation on UAV Pilots, which provides that in relation to the operation of UAV systems and that of UAVs in clusters, at scale or otherwise in a distributed manner, the pilots responsible for safe operation shall hold a license, and other person involving in control tasks do not need to hold a license, but should complete the relevant training carried out by the operator. The regulations on operations for UAVs are still evolving and can be subject to differing interpretations or significant changes. Distributed operation refers to the mode of operating UAV systems through a collection of multiple sub-units and communication nodes and their deployment to multiple sites or terminals for collaborative operation. As of the date of this annual report, 40 of our employees have obtained UAV class III pilot licenses and class IV pilot licenses, which satisfied the requirement to operate these categories of our AAVs. To the extent our AAVs are operated and controlled through distributed operation (such as during the delivery of our aerial media and smart management solutions), we may be required to obtain any official pilot license for certain pilot issued by the CAAC according to the Draft New Regulation on UAV Pilots. Since the revised draft has not been formally adopted as of the date of the document, the revised draft and its anticipated adoption or effective date are subject to further changes with substantial uncertainty. The pilots who operate our AAV flights also completed the AAV training provided by our company on the basis of the CAAC UAV Pilot Licenses.

In addition, the draft bill of the *Interim Measures for Flight Administration of Unmanned Aerial Vehicle* published by the CAAC on January 26, 2018 stipulates that any unit or individual that organizes UAV flight activities in a distributed manner shall be subject to safety review and obtain a safe operation license. The individual operator of UAV systems or clusters or distributed operations are however exempted for such licensing requirement. We may be required to obtain the safe operation license for certain component of our business once the above draft bill comes into effect. This draft bill was further reviewed by standing meeting of State Council on April 7, 2023.

Operators of our AAVs may be subject to additional licensing requirements. On December 29, 2015, the CAAC issued the *Rules on Operation of Light and Small Unmanned Aircraft (Trial)*, pursuant to which, pilots of specified UAVs shall meet certain qualification, and are prohibited from consumption of alcohol and drugs as well as careless piloting. Our AAV operators have complied with all the above requirements in material respects.

Import and Export

On December 31, 2005, the Ministry of Commerce and the General Administration for Customs jointly issued the *Measures for the Administration on Import and Export License for Dual-use Items and Technologies*, pursuant to which a license is required for the exportation of any dual-use goods, products and technologies of the PRC included in a control list issued by the Ministry of Commerce on December 30, 2022, effective on January 1, 2023. Notably, certain types of UAVs are *subject* to the foregoing export license requirements, such as UAVs with (a) a maximum endurance time greater than or equal to 1 hour, (b) maximum endurance time greater than or equal to half an hour but less than 1 hour and the ability to take-off and conduct stable flight against a wind speed of no less than 46.3 kilometer/hour; (c) aircraft range equal to or higher than 300 kilometers with payload of more than 500 kg; (d) automatic controlling system and navigation capability containing aerosol preparation for planting with volume of 20 liters or being capable of installing aerosol preparation system for planting with volumes of 20 liters after designing and modification. We may be required to obtain the necessary license for the exportation of certain of our AAVs.

Wireless Communication

Our AAVs and command-and-control centers have installed certain radio transmission equipment and telecommunication equipment. For radio transmission equipment, pursuant to the Regulations on the Administration of Radio in the PRC promulgated by the State Council and CMC, with effect from December 1, 2016, radio transmission equipment produced or imported for the purpose of sale and use in the PRC shall comply with laws and regulations in respect of product quality and administration of state radio, as well as other applicable national standards. Except for micro power short-distance radio transmission equipment, for any production or import of other radio transmission equipment for domestic sale and use, an application for model confirmation shall be filed with the radio regulatory authority of the state. According to Telecommunications Regulation of PRC promulgated by State Counsel on September 25, 2000, amended in July 2014 and February 2016, the government stipulates a network connection licensing system for telecommunications equipment. The telecommunications equipment accessing a public telecommunications network shall comply with the national standards, and obtain a network access certificate. We purchase certain equipment and models with Transmission Equipment Type Approval Certificate and Network Access Certificate from our supplier.

Bidding and Construction

Our undertaking of the development of command-and-control centers is subject to bidding laws and constructions laws.

On December 27, 2017, the SCNPC promulgated the *Bidding Law of the PRC*. The Bidding Law provides that two or more legal persons or other organizations may form a consortium to bid jointly as one bidder. Each member of a consortium shall have the relevant capability to undertake the bidding project; where the qualification criteria for bidders are imposed either by State regulations or terms of the bidding documents, each member of a consortium shall satisfy the corresponding qualification criteria. The consortium members shall each sign a joint bidding agreement to clearly specify the work and responsibilities to be undertaken by each party, and submit the joint bidding agreement to the bid inviter together with the bid.

On November 1, 1997, the SCNPC promulgated the *Construction Law of PRC*, which was amended on April 22, 2011 and April 23, 2019. The Construction Law provides that construction enterprises, survey units, design units and project supervision units engaging in construction activities shall be classified under different qualification grades based on certain criteria such as their registered capital, technical professionals team, technical equipment owned and track records of completed construction projects, etc., and may engage in construction activities within the scope permitted for their qualification grade upon passing examination of qualifications and obtaining the qualification certificate for the corresponding grade. Contractor of construction projects shall also possess a qualification certificate. Construction enterprises are prohibited from contracting projects beyond the scope of business permitted for their qualification grade or in any form in the name of another construction enterprise. A construction enterprise must not allow another organization or individual to use their qualification certificate or business license to contract any form of construction projects. According to the Construction Law, Contractors contracting projects without obtaining a qualification certificate shall be clamped down and be subject to a fine; illegal income, if any, shall be confiscated.

We entered into certain construction agreements in relation to our smart city management projects with the necessary construction qualifications held by our third-party partners on these projects. These projects are bidden jointly with qualified entity and sub-contracted to qualified entity. If we are found to have violated the applicable bidding laws and construction laws, we may be subject to fine. We will continue to cooperate with other partners with qualification for current smart city management projects.

Product Liability and Tort Liability

Pursuant to the *Product Quality Law of the PRC*, which was promulgated on February 22, 1993 and subsequently amended on July 8, 2000, August 27, 2009 and December 29, 2018, the production or sale of products that do not meet applicable health and safety standards and requirements is prohibited. Products must not pose unreasonable dangers to human or property. Where a defective product causes physical injury to a person or damage to property, the aggrieved party may make a claim for compensation from the producer or the seller of the product. Producers and sellers of non-compliant products may be ordered to cease production and sale of such products, subject to fines and/or revocation of business license. Non-compliant products, as well as earnings attributable to the sales of such products may also be confiscated.

In addition, pursuant to the *Tort Law of the PRC*, promulgated by the SCNPC on December 26, 2009 and taking effect since July 1, 2010, the manufacturer of defective products that cause damage shall bear tort liability. On May 28, 2020, the Third Session of the 13th National People's Congress passed the Civil Code of the People's Republic of China, which took effect on January 1, 2021 and replaced the *Tort Law of the PRC*. Where defects are discovered after the relevant products are put in circulation, the manufacturer and the seller shall promptly adopt remedial measures such as warnings and product recalls, failing which, the manufacturer and the seller will be liable for tort claims.

Consumer Rights Protection

Our business is subject to a variety of consumer protection laws, including the *PRC Consumer Rights and Interests Protection Law*, as amended on October 25, 2013, which imposes stringent obligations on business operators. Failure to comply with these consumer protection laws could subject us to administrative sanctions, such as the issuance of warning, confiscation of income, imposition of fines, order to cease business operations, revocation of business licenses, as well as potential civil and criminal liabilities.

Internet Information Security and Privacy Protection

In November 2016, the SCNPC promulgated the *Cyber Security Law of the PRC*, or the Cyber Security Law, which became effective on June 1, 2017. The Cyber Security Law requires that a network operator, which includes, among others, internet information services providers, to take technical measures and/or other necessary measures in accordance with applicable laws, regulations and national and industrial standards, to ensure the safe and stable operation of its networks. We are considered an "internet information service provider" as we operate website and mobile application and providing certain internet services mainly through our mobile application. The Cyber Security Law further requires internet information service providers to formulate contingency plans for network security incidents, report to competent departments immediately upon the occurrence of any incident endangering cyber security and take corresponding remedial measures. Internet information service providers are also required to maintain the integrity, confidentiality and availability of network data. The Cyber Security Law reaffirms the basic principles and requirements specified in other existing laws and regulations on personal data protection, such as the requirements on the collection, use, processing, storage and disclosure of personal data, and internet information service providers being required to take technical and other necessary measures to ensure the security of the personal information they have collected and prevent the personal information from being divulged, damaged or lost. Any violation of the Cyber Security Law may subject the internet information service provider like us to warnings, fines, confiscation of illegal gains, revocation of licenses, cancellation of filings, shutdown of websites or criminal liabilities.

The recommended national standard, *Information Security Technology Personal Information Security Specification*, which became effective in October 2020, puts forward specific refinement requirements on the collection, preservation, use, sharing, transfer, and public disclosure of personal information. Although it is not mandatory, in the absence of clear implementation rules and standards for the law on cyber security and other personal information protection, it will be used as the basis for judging and making determinations. On November 28, 2019, The *Notice of Identification Method of Application Illegal Collection and Use of Personal Information* was issued, which provides a reference for the identification of illegal collection and use of personal information by mobile apps, and provides guidance for app operators' self-inspection and self-correction and netizens' social supervision.

On June 10, 2021, the Standing Committee of the National People's Congress of China promulgated the *Data Security Law of PRC*, or Data Security Law, which took effect in September 2021. The Data Security Law sets forth data security and privacy related compliance obligations on entities and individuals carrying out data related activities. The Data Security Law also introduces a data classification and layered protection system based on the importance of data and the degree of impact on national security, public interests or legitimate rights and interests of individuals or organizations when such data is tampered with, destroyed, leaked or illegally acquired or used. In addition, the Data Security Law provides a national security review procedure for those data activities that may affect national security, and imposes export restrictions on certain data and information. According to the PRC National Security Law, the State shall establish institutions and mechanisms for national security review and regulation, and conduct national security review on certain matters that affect or may affect PRC national security, such as key technologies and IT products and services. In early July 2021, regulatory authorities in China launched cybersecurity investigations with regard to several China-based companies that are listed in the United States.

On July 10, 2021, the CAC released the revised draft of *Cybersecurity Review Measures (for public comments)*. On December 28, 2021, the CAC, NDRC, MIIT, the MPS, the Ministry of National Security, the MOF, the MOFCOM, the People's Bank of China, the SAMR, the National Radio and Television Administration, the CSRC, the National Administration of State Secrets Protection and the State Cryptography Administration jointly released the *Cybersecurity Review Measures*, which took effect on February 15, 2022. Pursuant to the Cybersecurity Review Measures, network platform operators with information of over one million users shall be subject to cybersecurity review before listing abroad. The cybersecurity review will evaluate, among others, the risk of critical information infrastructure, core data, important data, or the risk of a large amount of personal information being influenced, controlled or maliciously used by foreign governments after going public, and Cyber information security risk.

On August 17, 2021, the State Council promulgated the *Regulations on the Protection of the Security of Critical Information Infrastructure*, or the CIIO Regulations, which took effect in September 2021. The CIIO Regulations supplement and specify the provisions on the security of critical information infrastructure as stated in the Cyber Security Law. The CIIO Regulations provide, among others, that protection department of certain industry or sector shall notify the operator of the critical information infrastructure in time after the identification of certain critical information infrastructure. According to the CIIO Regulations, operators of certain industries or sectors that may endanger national security, people's livelihood and public interest in case of damage, function loss or data leakage may be identified as critical information infrastructure operators by the CAC or the respective industrial regulatory authorities once they meet the identification standards promulgated by the governmental authorities.

On August 20, 2021, the Standing Committee of the National People's Congress of China promulgated the *Personal Information Protection Law of the PRC*, or the Personal Information Protection Law, which took effect in November 2021. As the first systematic and comprehensive law specifically for the protection of personal information in the PRC, the Personal Information Protection Law provides, among others, that (i) an individual's separate consent shall be obtained before operation of such individual's sensitive personal information, e.g., biometric characteristics and individual location tracking, (ii) personal information operators operating sensitive personal information shall notify individuals of the necessity of such operations and the influence on the individuals' rights, (iii) if personal information operators reject individuals' requests to exercise their rights, individuals may file a lawsuit with a People's Court.

Furthermore, on May 28, 2020, the National People's Congress of the PRC approved the PRC Civil Code, which came into effect on January 1, 2021. Pursuant to the PRC Civil Code, the collection, storage, use, process, transmission, provision and disclosure of personal information should follow the principles of legitimacy, properness and necessity.

On July 7, 2022, the CAC issued the *Measures for the Security Assessment of Outbound Data Transfer*, pursuant to which, the data processor shall apply to the CAC for the security assessment via the local provincial-level cyberspace administration authority for an outbound data transfer under following circumstances: (i) outbound transfer of important data by a data processor; (ii) outbound transfer of personal information by a critical information infrastructure operator or a personal information processor who has processed the personal information of more than 1,000,000 people; (iii) outbound transfer of personal information by a personal information processor who has made outbound transfers of the personal information of 100,000 people cumulatively or the sensitive personal information of 10,000 people cumulatively since 1 January of the previous year; and (v) other circumstances as specified by the CAC. The assessment results of the data exit are valid for two years.

In addition, on November 14, 2021, *the Administration Regulations on Cyber Data Security (Draft for Comments)* was proposed by the CAC for public comments until December 13, 2021. It sets out general guidelines, protection of personal information, security of important data, security management of cross-border data transfer, obligations of internet platform operators, supervision and management, and legal liabilities. Key requirements include: data processors should be in compliance with the requirements of multi-level cybersecurity protection, strengthen the data processing system, data transmission network, data storage environment and other security protection, processing of important data systems in principle should meet the third level or above of multi-level cybersecurity protection and critical information infrastructure security protection requirements; data processors should establish a data security emergency response mechanism, and promptly start the emergency response mechanism in the event of a data security incident; the detailed rules for data processors to apply when providing personal information to third parties, or sharing, trading or entrusting important data to third parties; the scenarios of cybersecurity review which shall be subject to Cybersecurity Review Measures; the definitions of important data and operators' security protection obligations; the detailed rules on cross-border data transfer which added missing details to the Personal Information Protection Law; data processors processing personal information of more than one million people shall also comply with the regulations for processing of important data; data processors dealing with important data or listing overseas (including Hong Kong) should carry out an annual data security assessment by themselves or by entrusting data security service agencies, and each year before January 31, data security assessment report for the previous year shall be submitted to the districted city level cyberspace administration department. The draft measures reiterate that data processors which process the personal information of at least one million users must apply for a cybersecurity review if they plan listing of companies in foreign countries, and the draft measures further require the data processors that carry out the following activities to apply for cybersecurity review in accordance with the relevant laws and regulations: (i) the merger, reorganization or division of internet platform operators that have gathered a large number of data resources related to national security, economic development and public interests affects or may affect national security; (ii) the listing of the data processor in Hong Kong affects or may affect the national security; and (iii) other data processing activities that affect or may affect national security. In addition, in one of the following situations, data processors shall delete or anonymize personal information within 15 business days: (i) the purpose of processing personal information has been achieved or the purpose of processing is no longer needed; (ii) the storage term agreed with the users or specified in the personal information processing rules has expired; (iii) the service has been terminated or the account has been canceled by the individual; or (iv) unnecessary personal information or personal information unavoidably collected due to the use of automatic data collection technology but without the consent of the individual. Any failure to comply with such requirements may subject us to, among others, suspension of services, fines, revoking relevant business permits or business licenses and penalties. Since the revised draft has not been formally adopted as of the date of the document, the revised draft (especially its operative provisions) and its anticipated adoption or effective date are subject to further changes with substantial uncertainty.

However, the relationship between the *Data Security Law of the PRC* and the implemented *National Security Law of the PRC*, the *Cyber Security Law of the PRC*, the *Confidentiality Law of the PRC* and the *Personal Information Protection Law of the PRC* needs to be carefully clarified.

Intellectual Property Rights

Patent Law

According to the *Patent Law of the PRC* (as amended in 1992, 2000, 2008 and 2020), or the Patent Law, the State Intellectual Property Office is responsible for administering patent laws in the PRC. The provincial, autonomous region and municipal level patent administration departments are responsible for the administration of patent laws within their respective jurisdictions. The Chinese patent system adopts a first-to-file principle, which means that when more than one person files patent applications with respect to the same invention, the person who files the application first will obtain the patent of the invention. To be patentable, an invention or a utility model must meet three criteria: novelty, inventiveness and practicability. A patent is valid for twenty years in the case of an invention, ten years in the case of utility models and fifteen years in the case of designs.

Regulations on Copyright

The *Copyright Law of the PRC*, or the Copyright Law, which took effect on June 1, 1991 and was amended in 2001, 2010 and 2020, provides that Chinese citizens, legal persons, or other organizations shall, whether published or not, own copyright in their copyrightable works, which include, among others, works of literature, art, natural science, social science, engineering technology and computer software. Copyright owners enjoy certain legal rights, including right of publication, right of authorship and right of reproduction. The Copyright Law also extends copyright protection to internet activities, products disseminated over the internet and software products. In addition, the Copyright Law provides for a voluntary registration system administered by the China Copyright Protection Center, or the CPCC. According to the Copyright Law, an infringer of the copyrights shall be subject to various civil liabilities, which include ceasing infringement activities, making apology to the copyright owners and compensating the copyright owners for his/her loss. Infringers of copyright may also be subject to fines and/or administrative or criminal liabilities in severe situations. In order to further implement the Regulations on Computer Software Protection, the National Copyright Administration issued the *Measures for the Registration of Computer Software Copyright* on February 20, 2002, which specify detailed procedures and requirements with respect to the registration of software copyrights.

Pursuant to the *Computer Software Copyright Protection Regulations* promulgated by the State Council on December 20, 2001 and amended on January 30, 2013, software copyright owner may complete registration formalities with a software registration authority recognized by the State Council's copyright administrative department. The software copyright owner may authorize others to exercise that copyright, and is entitled to receive remuneration.

Trademark Law

Trademarks are protected by the *Trademark Law of the PRC* which was adopted on August 23, 1982 and subsequently amended in 1993, 2001, 2013 and 2019 (to take effect on November 1, 2019) as well as by the *Implementation Regulations of the PRC Trademark Law* adopted by the State Council in 2002 and as most recently amended on April 29, 2014. The Trademark Office under the State Administration for Industry and Commerce takes charge of trademark registrations. The Trademark Office grants a ten-year term to registered trademarks which term may be renewed for another ten-year period upon request by the trademark owner. A trademark registrant may license its registered trademarks to another party by entering into trademark license agreements, which must be filed with the Trademark Office for its record. As with trademark registrations, the Trademark Law has adopted a first-to-file principle. If a trademark applied for is identical or similar to another trademark which has already been registered or subject to a preliminary examination and approval for use on the same or similar kinds of products or services, such trademark application may be rejected. Any person applying for the registration of a trademark may not injure existing trademark rights 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.

Regulations on Domain Names

The MIIT promulgated the *Measures on Administration of Internet Domain Names*, or the Domain Name Measures, on August 24, 2017, which took effect on November 1, 2017 and replaced the *Administrative Measures on China Internet Domain Names* promulgated by the MIIT on November 5, 2004. According to the Domain Name Measures, the MIIT is in charge of the administration of PRC internet domain names. The domain name registrations follow a first-to-file principle. Applicants for registration of domain names must provide the true, accurate and complete information of their identities to domain name registration service institutions. The applicants will become the holders of such domain names upon the completion of the registration procedures.

Foreign Investment

The Foreign Investment Law

On March 15, 2019, the SCNPC approved the *Foreign Investment Law of the PRC*, which took effect on January 1, 2020 and replace three existing laws on foreign investments in China, namely, the *PRC Equity Joint Venture Law*, the *PRC Cooperative Joint Venture Law* and the *Wholly Foreign-owned Enterprise Law*, together with their implementation rules and ancillary regulations. The *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 invested enterprises in China. The *Foreign Investment Law* establishes the basic framework for the access to, and the promotion, protection and administration of foreign investments in view of investment protection and fair competition.

According to the *Foreign Investment Law*, “foreign investment” refers to investment activities directly or indirectly conducted by one or more natural persons, business entities, or otherwise organizations of a foreign country (collectively referred to as “foreign investor”) within China, and the investment activities include the following situations: (i) a foreign investor, individually or collectively with other investors, establishes a foreign-invested enterprise within China; (ii) a foreign investor acquires stock shares, equity shares, shares in assets, or other like rights and interests of an enterprise within China; (iii) a foreign investor, individually or collectively with other investors, invests in a new project within China; and (iv) investments in other means as provided by laws, administrative regulations, or the State Council.

According to the *Foreign Investment Law*, the State Council will publish or approve to publish a catalogue for special administrative measures, or the “negative list.” The *Foreign Investment Law* grants national treatment to foreign invested entities, except for those foreign invested entities that operate in industries deemed to be either “restricted” or “prohibited” in the “negative list”. The *Foreign Investment Law* provides that foreign invested entities operating in foreign restricted or prohibited industries will require market entry clearance and other approvals from relevant PRC governmental authorities.

Furthermore, the *Foreign Investment Law* provides that foreign invested enterprises established according to the existing laws regulating foreign investment may maintain their structure and corporate governance within five years after the implementing of the *Foreign Investment Law*.

In addition, the *Foreign Investment Law* also provides several protective rules and principles for foreign investors and their investments in the PRC, including, among others, that local governments shall abide by their commitments to the foreign investors; foreign-invested enterprises are allowed to issue stocks and corporate bonds; except for special circumstances, in which case statutory procedures shall be followed and fair and reasonable compensation shall be made in a timely manner, expropriation or requisition of the investment of foreign investors is prohibited; mandatory technology transfer is prohibited; and the capital contributions, profits, capital gains, proceeds out of asset disposal, licensing fees of intellectual property rights, indemnity or compensation legally obtained, or proceeds received upon settlement by foreign investors within China, may be freely remitted inward and outward in RMB or a foreign currency. Also, foreign investors or the foreign investment enterprise should be imposed legal liabilities for failing to report investment information in accordance with the requirements.

On December 26, 2019, the State Council promulgated the *Implementation Regulations on the Foreign Investment Law*, which came into effect on January 1, 2020. It further requires that foreign-invested enterprises and domestic enterprises shall be treated equally with respect to policy making and implementation. Pursuant to the Implementation Regulations on the Foreign Investment Law, if the existing foreign-invested enterprises fail to change their original forms as of January 1, 2025, the relevant market regulation departments will not process other registration matters for these enterprises, and may disclose their relevant information to the public.

On December 30, 2019, the MOFCOM and the State Administration for Market Regulation jointly issued the *Measures for Reporting of Foreign Investment Information, or the Foreign Investment Information Measures*, which came into effect on January 1, 2020 and replaced the Interim Administrative Measures for the Record-filing of the Establishment and Modification of Foreign-invested Enterprises. Since January 1, 2020, for foreign investors carrying out investment activities directly or indirectly in the PRC, foreign investors or foreign-invested enterprises shall submit investment information through the Enterprise Registration System and the National Enterprise Credit Information Publicity System operated by the State Administration for Market Regulation. Foreign investors or foreign-invested enterprises shall disclose their investment information by submitting reports for their establishments, modifications and cancellations and their annual reports in accordance with the Foreign Investment Information Measures. If a foreign-invested enterprise investing in the PRC has finished submitting its reports for its establishment, modifications and cancellation and its annual reports, the relevant information will be shared by the competent market regulation department to the competent commercial department, and does not require such foreign-invested enterprise to submit the reports separately.

The establishment, operation and management of corporate entities in the PRC are governed by the PRC Company Law, which was initially promulgated by the SCNPC on December 29, 1993 and was most recently amended on October 26, 2018. The current PRC Company Law came into effect on October 26, 2018. The PRC Company Law generally governs two types of companies, limited liability companies and joint stock limited companies. The PRC Company Law also applies to foreign-invested companies that are also subject to the operation of other laws and regulations applicable to foreign investment.

Foreign Investment Industries Guidance Catalogue

On June 28, 2017, the Ministry of Commerce of the People's Republic of China, or the MOFCOM, and the National Development and Reform Commission, or the NDRC, jointly promulgated the *Guidance Catalogue of Industries for Foreign Investment (Revised in 2017)*, or the Catalogue, which came into effect on July 28, 2017. The Catalogue includes the Catalogue of Industries for Encouraging Foreign Investment, or the Encouraged Catalogue, and the Special Administrative Measures for Access of Foreign Investment (Negative List), or the Negative List. The Encourage Catalogue sets forth the industries and economic activities that foreign investment in China is encouraged to be engaged in. The Negative List sets forth the prohibited or restricted industries or economic activities for foreign investment in China. The Encouraged Catalogue was amended and promulgated on October 26, 2022, and the Negative List was amended on June 28, 2018, June 30, 2019, June 23, 2020 and December 27, 2021. Any industry not listed in the Encouraged Catalogue and the Negative List is a permitted industry. Pursuant to the Negative List, a company that designs and manufactures UAVs can be wholly owned by foreign investors.

Foreign Exchange

General Administration of Foreign Exchange

Under the *Regulation of the People's Republic of China on Foreign Exchange Administration* promulgated on January 29, 1996 and most recently amended on August 5, 2008 and various regulations issued by the State Administration of Foreign Exchange, or the SAFE, and other relevant PRC government authorities, Renminbi is convertible into other currencies for current account items, such as trade-related receipts and payments and payment of interest and dividends. The conversion of Renminbi into other currencies and remittance of the converted foreign currency outside the PRC for capital account items, such as direct equity investments, loans and repatriation of investment, require the prior approval from the SAFE or its local office.

Payments for transactions that take place within the PRC must be made in Renminbi. Unless otherwise approved, PRC companies may not repatriate foreign currency payments received from abroad or retain the same abroad. Foreign-invested enterprises may retain foreign exchange in accounts with designated foreign exchange banks under the current account items subject to a cap set by the SAFE or its local office. Foreign exchange proceeds under the current accounts may be either retained or sold to a financial institution engaged in settlement and sale of foreign exchange pursuant to relevant SAFE rules and regulations. For foreign exchange proceeds under the capital accounts, approval from the SAFE is generally required for the retention or sale of such proceeds to a financial institution engaged in settlement and sale of foreign exchange.

Pursuant to the Circular of the SAFE on Further Improving and Adjusting Foreign Exchange Administration *Policies for Direct Investments*, or the SAFE Circular No. 59 promulgated by the SAFE on November 19, 2012, which became effective on December 17, 2012 and was further amended on May 4, 2015, and again October 10, 2018, and December 30, 2019, approval of the SAFE is not required for opening a foreign exchange account and depositing foreign exchange into the accounts relating to the direct investments. The SAFE Circular No. 59 also simplified foreign exchange-related registration required for foreign investors to acquire equity interests in PRC companies and further improved the administration on foreign exchange settlement for foreign-invested enterprises.

The *Circular on Further Simplifying and Improving the Foreign Currency Management Policy on Direct Investments*, or the SAFE Circular No. 13, effective from June 1, 2015, and was amended on December 30, 2019, removes the requirement of administrative approvals for foreign exchange registration of direct domestic investments and direct overseas investments and simplifies the procedure of foreign exchange-related registration. Pursuant to the SAFE Circular No. 13, the investors shall register with banks for direct domestic investment and direct overseas investments.

The *Circular on Reforming the Management Approach regarding the Settlement of Foreign Exchange of Foreign-invested Enterprises*, or the SAFE Circular No. 19, which was promulgated by the SAFE on March 30, 2015 and became effective on June 1, 2015, provides that a foreign-invested enterprise may, according to its actual business needs, settle with a bank the portion of the foreign exchange capital in its capital account for which the relevant foreign exchange administration has confirmed monetary capital contribution rights and interests (or for which the bank has registered the injection of the monetary capital contribution into the account). Pursuant to the SAFE Circular No. 19, for the time being, foreign-invested enterprises are allowed to settle 100% of their foreign exchange capital on a discretionary basis; a foreign-invested enterprise shall truthfully use its capital for its own operational purposes within the scope of business; where an ordinary foreign-invested enterprise makes domestic equity investment with the amount of foreign exchanges settled, the invested enterprise must first go through domestic re-investment registration and open a corresponding account for foreign exchange settlement pending payment with the foreign exchange administration or the bank at the place where it is registered. According to the *Circular of the State Administration of Foreign Exchange on Abolishing and Nullifying Five Regulatory Documents on Foreign Exchange Administration and Seven Regulatory Documents on Foreign Exchange Administration* promulgated on December 30, 2019, there are no longer restrictions on the use of foreign exchange settlement in the special overseas inflow deposit account and the special domestic inflow deposit account.

The *Circular on Reforming and Regulating Policies on the Control over Foreign Exchange Settlement of Capital Accounts*, or the SAFE Circular No. 16, which was promulgated by the SAFE and became effective on June 9, 2016, provides that enterprises registered in the PRC may also convert their foreign debts from foreign currency into Renminbi on a self-discretionary basis. The SAFE Circular No. 16 also provides an integrated standard for conversion of foreign exchange under capital account items (including but not limited to foreign currency capital and foreign debts) on a self-discretionary basis, which applies to all enterprises registered in the PRC.

According to the SAFE Circular No. 13, the *Administrative Rules on the Company Registration* that was promulgated by the State Council on June 24, 1994 and most recently amended on February 6, 2016, and other laws and regulations governing foreign invested enterprises and company registrations, the establishment of a foreign invested enterprise and any capital increases and other major changes in a foreign invested enterprise shall be registered with a designated bank at the place of its registration and the State Administration for Market Regulation, or the SAMR, or its local counterparts, and be filed via the foreign investment comprehensive administrative system, or the FICMIS, if such foreign invested enterprise does not involve special access administrative measures prescribed by the PRC government.

On October 23, 2019, the SAFE promulgated the *Notice of the State Administration of Foreign Exchange on Further Promoting the Convenience of Cross-border Trade and Investment*, or the SAFE Circular 28. The SAFE Circular 28 stipulates that non-investment FIEs may use capital to carry out domestic equity investment in accordance with the law provided that such investment does not violate the Negative List and the projects invested are genuine and in compliance with laws and regulations.

Loans by the Foreign Companies to their PRC Subsidiaries

A loan made by foreign investors to a foreign invested enterprise in which it has an equity interest is considered to be foreign debt in China and is regulated by various laws and regulations, including the *Regulation of the People's Republic of China on Foreign Exchange Administration*, the *Interim Provisions on the Management of Foreign Debts*, the *Statistical Monitoring of Foreign Debts Tentative Provisions*, the *Detailed Rules for the Implementation of Provisional Regulations on Statistics and Supervision of External Debt*, and the *Administrative Measures for Registration of Foreign Debts*. Under these rules and regulations, a shareholder loan in the form of foreign debt made to a PRC entity does not require the prior approval of the SAFE. However, such foreign debt must be registered with and recorded by the SAFE or its local branches within fifteen business days after execution of the relevant agreement. Pursuant to these rules and regulations, the balance of the foreign debts of a foreign invested enterprise shall not exceed the difference between the total investment and the registered capital of the foreign invested enterprise, or Total Investment and Registered Capital Balance.

Pursuant to the Interim Provisions of the State Administration for Industry and Commerce on the Ratio of the Registered Capital to the Total Investment of a Sino-Foreign Equity Joint Venture Enterprise, promulgated by SAMR on February 17, 1987 and taking effect on March 1, 1987, with respect to a sino-foreign equity joint venture, the registered capital shall be (i) no less than 7/10 of its total investment, if the total investment is US\$3 million or under US\$3 million; (ii) no less than 1/2 of its total investment, if the total investment is ranging from US\$3 million to US\$10 million (including US\$10 million), provided that the registered capital shall not be less than US\$2.1 million if the total investment is less than US\$4.2 million; (iii) no less than 2/5 of its total investment, if the total investment is ranging from US\$10 million to US\$30 million (including US\$30 million), provided that the registered capital shall not be less than US\$5 million if the total investment is less than US\$12.5 million; and (iv) no less than 1/3 of its total investment, if the total investment exceeds US\$30 million, provided that the registered capital shall not be less than US\$12 million if the total investment is less than US\$36 million.

On January 11, 2017, the People's Bank of China, or the PBOC promulgated the Notice of the People's Bank of China on Matters concerning the Macro-Prudential Management of Full-Covered Cross-Border Financing, or the PBOC Notice No. 9. Pursuant to the PBOC Notice No. 9, within a transition period of one year from January 11, 2017, the foreign invested enterprises may adopt the currently valid foreign debt management mechanism, or Current Foreign Debt Mechanism, or the mechanism as provided in the PBOC Notice No. 9, or Notice No. 9 Foreign Debt Mechanism, at their own discretions. The PBOC Notice No. 9 provides that enterprises may conduct independent cross-border financing in Renminbi or foreign currencies as required. Pursuant to the PBOC Notice No. 9, the outstanding cross-border financing of an enterprise (the outstanding balance drawn, here and below) shall be calculated using a risk-weighted approach, or Risk-Weighted Approach, and shall not exceed the specified upper limit, namely: risk-weighted outstanding cross-border financing \leq the upper limit of risk-weighted outstanding cross-border financing. Risk-weighted outstanding cross-border financing = \sum outstanding amount of Renminbi and foreign currency denominated cross-border financing * maturity risk conversion factor * type risk conversion factor + \sum outstanding foreign currency denominated cross-border financing * exchange rate risk conversion factor. Maturity risk conversion factor shall be one (1) for medium and long-term cross-border financing with a term of more than one year and 1.5 for short-term cross-border financing with a term of no less than one (1) year. Type risk conversion factor shall be one (1) for on-balance-sheet financing and one (1) for off-balance-sheet financing (contingent liabilities) for the time being. Exchange rate risk conversion factor shall be 0.5. The PBOC Notice No. 9 further provides that the upper limit of risk-weighted outstanding cross-border financing for enterprises shall be calculated and adjustable based on the equation of upper limit of risk-weighted outstanding cross-border financing = the capital or the net assets \times the leverage rate of cross-border financing \times the macro-prudential adjustment parameter. For enterprises, the leverage rate of cross-border financing shall be 2 and the macro-prudential adjustment parameter shall be 1, which means that the upper limit of risk-weighted outstanding cross-border financing for an enterprise shall be 200% of its net assets. Enterprises shall file with the SAFE in its capital item information system after entering into the relevant cross-border financing contracts and prior to three (3) business days before drawing any money from the foreign debts. On March 11, 2020, the PBOC and the SAFE issued PBOC and SAFE Notice Concerning Adjustment to the Full Caliber Cross-border Finance Adjustment Parameter, pursuant to which the macro-prudential adjustment parameter has been increased from 1 to 1.25, which means that the upper limit of risk-weighted outstanding cross-border financing for an enterprise is increased to 250% of its net assets.

Based on the foregoing, if we provide funding to our wholly foreign owned subsidiaries through shareholder loans, the balance of such loans shall not exceed the Total Investment and Registered Capital Balance and we will need to register such loans with the SAFE or its local branches in the event that the Current Foreign Debt Mechanism applies, or the balance of such loans shall be subject to the Risk-Weighted Approach and the net asset limits and we will need to file the loans with the SAFE in its information system in the event that the Notice No. 9 Foreign Debt Mechanism applies. According to the PBOC Notice No. 9, after a transition period of one year from January 11, 2017, the PBOC and the SAFE will determine the cross-border financing administration mechanism for the foreign-invested enterprises after evaluating the overall implementation of the PBOC Notice No. 9. It is uncertain which mechanism will be adopted by the PBOC and the SAFE in the future and what statutory limits will be imposed on us when providing loans to our PRC subsidiaries.

Offshore Investment by PRC Residents

Pursuant to the SAFE's Notice on Relevant Issues Concerning Foreign Exchange Administration for PRC Residents to Engage in Financing and Round-Trip Investment via Overseas Special Purpose Vehicles and its subsequent amendments, supplements or implementation rules, or SAFE Circular 75, issued on October 21, 2005, a PRC resident (whether a natural person or a legal person) shall register with the local branch of the SAFE before it establishes or controls an overseas special purpose vehicle, or an SPV, with assets or equity interests in a PRC company, for the purpose of overseas equity financing. On July 4, 2014, SAFE issued the SAFE's Notice on Relevant Issues Concerning Foreign Exchange Administration for PRC Residents to Engage in Outbound Investment and Financing and Round-trip Investments via Special Purpose Vehicles, or the SAFE Circular 37, which superseded SAFE Circular 75. According to SAFE Circular 37, the PRC domestic resident shall apply for SAFE registration for overseas investment before paying capital to SPV by using his, her or its legal assets whether overseas or domestic. The SPV is defined as "offshore enterprise directly established or indirectly controlled by the domestic residents (including domestic institutions and individuals) with their legally owned assets and equity of the domestic enterprise, or legally owned offshore assets or equity, for the purpose of offshore investment and financing". In addition, in the event that the SPV undergoes changes of its basic information such as the individual shareholder, name, operation term, etc., or material events including increase or decrease in investment amount by domestic individual shareholder, equity transfer or swap, mergers, spin-off, etc., the domestic resident shall timely complete the change of foreign exchange registration formality for offshore investment.

According to the SAFE Circular 37, failure to make such registration or truthfully disclose actual controllers of the round-trip enterprises may subject PRC residents to fines of up to RMB300,000 in case of domestic institutions or RMB50,000 in case of domestic individuals. If the registered or beneficial shareholders of the offshore holding company who are PRC residents do not complete their registration with the local SAFE branches, the relevant PRC subsidiary may be prohibited from distributing their profits and proceeds from any reduction in capital, share transfer or liquidation to the offshore company, and the offshore company may be restricted in its ability to contribute additional capital to its PRC subsidiary. Moreover, failure to comply with the SAFE registration and amendment requirements described above could result in liability under PRC laws for violating applicable foreign exchange restrictions.

Mr. Huazhi Hu, our founder, has completed initial registration under the SAFE Circular 37 with respect to his shareholding in our company through his wholly-owned company incorporated in the British Virgin Islands. An amendment to the registration is required if there are material changes to the registrant, such as any changes to the identity of the registrant, increases or decreases in investment amount, transfers or exchanges of shares and mergers. We cannot provide any assurance that all of our shareholders who are PRC residents will file all applicable registrations or amend previously filed registrations as required by these SAFE regulations. The failure or inability of our PRC resident shareholders to comply with the registration procedures may subject the PRC resident shareholders to fines and legal sanctions, restrict our cross-border investment activities, or limit our PRC subsidiaries' ability to distribute dividends to or obtain foreign exchange-dominated loans from our company.

Dividend Distribution

The principal laws and regulations regulating the distribution of dividends by foreign-invested enterprises in the PRC include the *PRC Company Law*, as amended in 2004, 2005, 2013 and 2018, the *Foreign Investment Law of PRC* promulgated in 2020 and the *Implementation Rules to the Foreign Investment Law* promulgated in 2020. Under the current regulatory regime in the PRC, foreign-invested enterprises may pay dividends only out of their retained earnings, if any, as determined in accordance with PRC accounting standards and regulations. A PRC company is required to set aside as statutory reserve funds of at least 10% of its after-tax profit, until the cumulative amount of such reserve funds reaches 50% of its registered capital unless laws regarding foreign investment provide otherwise. A PRC company shall not distribute any profits until any losses from prior fiscal years have been offset. Profits retained from prior fiscal years may be distributed together with distributable profits from the current fiscal year.

Taxation

Enterprise Income Tax

On March 16, 2007, the SCNPC promulgated the Enterprise Income Tax Law of the PRC which was amended on February 24, 2017 and December 29, 2018. On December 6, 2007, the State Council enacted the *Regulations for the Implementation of the Enterprise Income Tax Law*, or collectively, the EIT Law. The EIT Law came into effect on January 1, 2008 and was amended on April 23, 2019. Under the EIT Law, both resident enterprises and non-resident enterprises are subject to tax in the PRC. Resident enterprises are defined as enterprises that are established in China in accordance with PRC laws, or that are established in accordance with the laws of foreign countries but are actually or in effect controlled from within the PRC. Non-resident enterprises are defined as enterprises that are organized under the laws of foreign countries and whose actual management is conducted outside the PRC, but have established institutions or premises in the PRC, or have no such established institutions or premises but have income generated from inside the PRC. Under the EIT Law and relevant implementing regulations, a uniform corporate income tax rate of 25% is applied. However, if non-resident enterprises have not formed permanent establishments or premises in the PRC, or if they have formed permanent establishment or premises in the PRC but there is no actual relationship between the relevant income derived in the PRC and the established institutions or premises set up by them, enterprise income tax is set at the rate of 10% with respect to their income sourced from inside the PRC. According to the EIT Law and relevant regulations, subject to the approval of competent tax authorities, the income tax of an enterprise that has been determined to be a high and new technology enterprise shall be reduced to a preferential rate of 15%.

Value-added Tax

The *Provisional Regulations of the PRC on Value-added Tax* was promulgated by the State Council on December 13, 1993 and came into effect on January 1, 1994 and was subsequently amended from time to time, and the *Detailed Rules for the Implementation of the Provisional Regulations of the PRC on Value-added Tax* (Revised in 2011) was promulgated by the Ministry of Finance, or the MOF, on December 25, 1993 and subsequently amended on December 15, 2008 and October 28, 2011, or collectively, VAT Law. According to the VAT Law and the Order 691, all enterprises and individuals engaged in the sale of goods, the provision of processing, repair and replacement services, sale of services, intangible assets, real property and the importation of goods within the territory of the PRC are taxpayers of VAT.

On November 19, 2017, the State Council promulgated the *Decisions on Abolishing the Provisional Regulations of the PRC on Business Tax and Amending the Provisional Regulations of the PRC on Value-added Tax*, or the Order 691. The VAT tax rates generally applicable are simplified as 17%, 11%, 6% and 0%, and the VAT tax rate applicable to the small-scale taxpayers is 3%. Pursuant to the *Circular of the Ministry of Finance and the State Administration of Taxation on Adjusting Value-added Tax Rates* promulgated on April 4, 2018 by the Ministry of Finance and the State Administration of Taxation, which became effective on May 1, 2018, where a taxpayer engages in a taxable sales activity for the value-added tax purpose or imports goods, the previous applicable 17% and 11% tax rates are adjusted to be 16% and 10%, respectively. Pursuant to *Announcement on Policies for Deepening the VAT Reform* issued by the PRC Ministry of Finance, the PRC State Taxation Administration and the General Administration of Customs ("Announcement No. 39") on March 20, 2019 and effective on April 1, 2019, the previous rate of 16% or 10% are adjusted to be 13% or 9%, respective, for taxpayer's general sale activities or imports.

Tax on Indirect Transfer

On February 3, 2015, the SAT issued the *Circular on Issues of Enterprise Income Tax on Indirect Transfers of Assets by Non-PRC Resident Enterprises*, or the SAT Circular 7. Pursuant to the SAT Circular 7, an "indirect transfer" of assets, including equity interests in a PRC resident enterprise, by non-PRC resident enterprises, may be recharacterized and treated as a direct transfer of PRC taxable assets, if such arrangement does not have a reasonable commercial purpose and was established for the purpose of avoiding payment of PRC enterprise income tax. As a result, gains derived from such indirect transfer may be subject to PRC enterprise income tax. When determining whether there is a "reasonable commercial purpose" of the transaction arrangement, features to be taken into consideration include, *inter alia*, whether the main value of the equity interest of the relevant offshore enterprise derives directly or indirectly from PRC taxable assets; whether the assets of the relevant offshore enterprise mainly consists of direct or indirect investment in China or if its income is mainly derived from China; and whether the offshore enterprise and its subsidiaries directly or indirectly holding PRC taxable assets have real commercial nature which is evidenced by their actual function and risk exposure. The SAT Circular 7 does not apply to transactions of sale of shares by investors through a public stock exchange where such shares were acquired on a public stock exchange. On October 17, 2017, the SAT issued the *Circular on Issues of Tax Withholding regarding Source of Non-PRC Resident Enterprise Income Tax*, or the SAT Circular 37, which further elaborates on the relevant implemental rules regarding the calculation, reporting and payment obligations of the withholding tax by the non-resident enterprises.

Employment and Social Welfare

Labor Contract Law

The *Labor Contract Law of the PRC*, or the Labor Contract Law, which was promulgated on January 1, 2008 and amended on December 28, 2012, is primarily aimed at regulating rights and obligations of employer and employee relationships, including the establishment, performance and termination of labor contracts. Pursuant to the Labor Contract Law, labor contracts shall be concluded in writing if labor relationships are to be or have been established between employers and employees. Employers are prohibited from forcing employees to work in excess of certain time limit and employers shall pay employees for overtime work in accordance with national regulations. In addition, employee wages shall be no lower than the local minimum wages and must be paid to employees in a timely manner.

Interim Provisions on Labor Dispatch

Pursuant to the *Interim Provisions on Labor Dispatch* promulgated by the Ministry of Human Resources and Social Security on January 24, 2014, which became effective on March 1, 2014, dispatched workers are entitled to the same pay as the fulltime employees for the same nature of work. Employers are allowed to use dispatched workers for temporary, auxiliary or substitutive positions, and the number of dispatched workers must not exceed 10% of the total number of employees.

Social Insurance and Housing Fund

As required under the Regulation of Insurance for Labor Injury implemented on January 1, 2004 and amended in 2010, the Provisional Measures for Maternity Insurance of Employees of Corporations implemented on January 1, 1995, the *Decisions on the Establishment of a Unified Pension Insurance Program for Enterprise Employees of the State Council* issued on July 16, 1997, the Decisions on the *Establishment of the Medical Insurance Program for Urban Workers of the State* Council promulgated on December 14, 1998, the *Unemployment Insurance Measures* promulgated on January 22, 1999 and the *Social Insurance Law of the PRC* implemented on July 1, 2011 and amended on December 29, 2018, employers are required to provide their employees in the PRC with welfare benefits covering pension insurance, unemployment insurance, maternity insurance, labor injury insurance and medical insurance. These payments are made to local administrative authorities. Any employer that fails to make social insurance contributions may be ordered to rectify the non-compliance and pay the required contributions within a prescribed time limit and be subject to a late fee. If the employer still fails to rectify the failure to make the relevant contributions within the grace period, it may be subject to a fine ranging from one (1) to three (3) times the amount overdue.

In accordance with the *Regulations on the Management of Housing Fund* which was promulgated by the State Council in 1999 and amended in 2002 and 2019, employers must register at the designated administrative centers and open bank accounts for depositing employees' housing funds. An employee and his/her employer are also required to pay and deposit certain percentage of the monthly average salary of such employee as housing funds in the preceding year in full and on time.

Employee Stock Incentive Plan

Pursuant to the Notice of Issues Related to the Foreign Exchange Administration for Domestic Individuals Participating in Stock Incentive Plan of Overseas Listed Company, or the SAFE Circular 7, which was issued by the SAFE on February 15, 2012, if PRC "domestic individuals" (both PRC residents and non-PRC residents who reside in China for a continuous period of not less than one year, excluding foreign diplomatic personnel and representatives of international organizations) participate in any stock incentive plan of an overseas listed company, a PRC domestic qualified agent, which could be the PRC subsidiary of such overseas listed company, shall, among others things, file, on behalf of such individual, an application with the SAFE to conduct the SAFE registration with respect to such stock incentive plan, and obtain approval for an annual allowance with respect to the purchase of foreign exchange in connection with stock holding or stock option exercises. In addition, the SAFE Circular 37 also provides certain requirements and procedures of foreign exchange registration in relation to equity incentive plan of SPV before listing. In this regard, if a non-listed SPV grants equity incentives to its directors, supervisors, senior officers or other employees in its domestic subsidiaries, the relevant domestic individual residents may register with the SAFE before exercising their rights.

In addition, the SAT has issued certain circulars concerning employee stock options and restricted shares. Under these circulars, employees working in the PRC who exercise stock options or are granted restricted shares will be subject to PRC individual income tax. The PRC subsidiaries of an overseas listed company are required to file documents related to employee stock options and restricted shares with relevant tax authorities and to withhold individual income taxes of employees who exercise their stock option or purchase restricted shares. If the employees fail to pay or the PRC subsidiaries fail to withhold income tax in accordance with relevant laws and regulations, the PRC subsidiaries may face sanctions imposed by the tax authorities or other PRC governmental authorities.

M&A Rules and Overseas Listing

On August 8, 2006, six (6) PRC governmental and regulatory agencies, including the MOFCOM and the China Securities Regulatory Commission, or the CSRC, promulgated the *Rules on Acquisition of Domestic Enterprises by Foreign Investors*, or the M&A Rules that became effective on September 8, 2006 and was revised on June 22, 2009, governing the mergers and acquisitions of domestic enterprises by foreign investors. The M&A Rules, among other things, require that if an overseas company established or controlled by PRC companies or individuals, or PRC Citizens, intends to acquire equity interests or assets of any other PRC domestic company affiliated with the PRC Citizens, such acquisition must be submitted to the MOFCOM for approval. The M&A Rules also require that an offshore SPV, or an SPV formed for overseas listing purposes and controlled directly or indirectly by PRC companies or individuals, shall obtain the approval of the CSRC prior to overseas listing and trading of such SPV's securities on an overseas stock exchange.

On February 17, 2023, the CSRC issued rules and regulations concerning the filing management of overseas listing, which came into effect on March 31, 2023. The rules and regulations issued include the Provisional Measures for the Administration of Overseas Issuance and Listing of Securities by Domestic Enterprises, or the New Filing Rules, and five supporting guidelines. The New Filing Rules dictate that enterprises that have been listed overseas prior to March 31, 2023 constitute "Existing Issuers." Existing Issuers are required to complete filing procedure with the CSRC before they conduct refinancing activities or issue securities such as convertible bonds, exchangeable bonds and preference shares, unless such securities are issued as equity incentive awards or in connection with conversion of public reserve funds into increased company capital, share dividends or share split. Given that the New Filing Rules were recently promulgated, there remains substantial uncertainties as to their interpretation, application, and enforcement and how they will affect an Existing Issuer's operations and future financing.

Environmental Protection and Work Safety

Environmental Protection

Pursuant to the *Environmental Protection Law of the PRC* promulgated by the SCNPC, on December 26, 1989, amended on April 24, 2014 and effective on January 1, 2015, any entity which discharges or will discharge pollutants during course of operations or other activities must implement effective environmental protection safeguards and procedures to control and properly treat waste gas, waste water, waste residue, dust, malodorous gases, radioactive substances, noise vibrations, electromagnetic radiation and other hazards produced during such activities.

Environmental protection authorities impose various administrative penalties on persons or enterprises in violation of the *Environmental Protection Law*. Such penalties include warnings, fines, orders to rectify within the prescribed period, orders to cease construction, orders to restrict or suspend production, orders to make recovery, orders to disclose relevant information or make an announcement, imposition of administrative action against relevant responsible persons, and orders to shut down enterprises. Any person or entity that pollutes the environment resulting in damage could also be held liable under the Civil Code of the PRC. In addition, environmental organizations may also bring lawsuits against any entity that discharges pollutants detrimental to the public welfare.

Work Safety

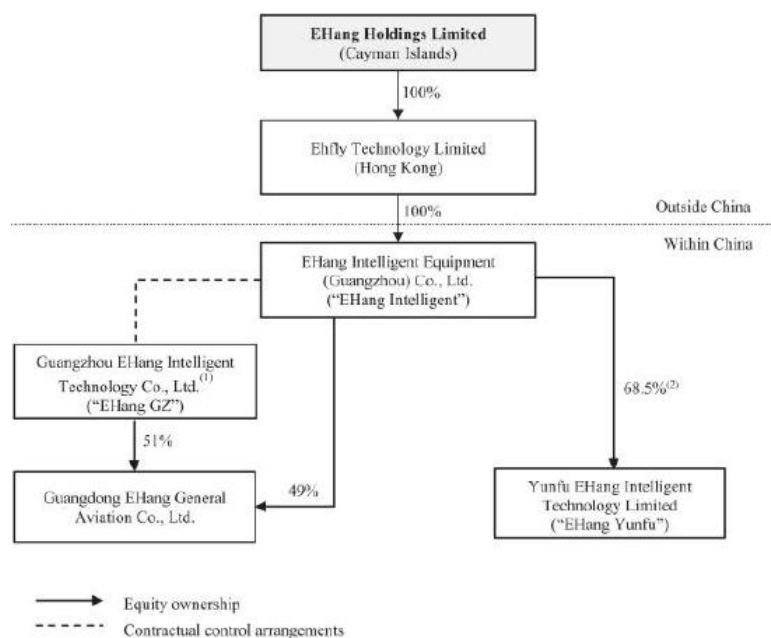
Under relevant construction safety laws and regulations, including the *Work Safety Law of the PRC* which was promulgated by the SCNPC on June 29, 2002, amended on August 27, 2009, August 31, 2014, and effective as of December 1, 2014, production and operating business entities must establish objectives and measures for work safety and improve the working environment and conditions for workers in a planned and systematic way. A work safety protection scheme must also be set up to implement the work safety job responsibility system. In addition, production and operating business entities must arrange work safety training and provide the employees with protective equipment that meets the national standards or industrial standards. Automobile and components manufacturers are subject to the aforementioned environment protection and work safety requirements.

Fire Control

Pursuant to the *Fire Safety Law of the PRC* promulgated by the SCNPC on April 29, 1998, amended on October 28, 2008 and April 23, 2019 and which became effective on April 23, 2019 and the *Interim Provisions for Management of Examination and Acceptance of Fire Protection Design of Construction Projects* promulgated by the Ministry of Housing and Urban-Rural Development of the PRC on April 1, 2020 and became effective on June 1, 2020, the construction entity of a large-scale crowded venue (including the construction of a manufacturing factory that is over 2,500 square meters) and other special construction projects must apply for fire prevention design review with fire control authorities, and complete fire assessment inspection and acceptance procedures after the construction project is completed. The construction entity of other construction projects must provide fire protection design and technical materials meeting the construction needs when it applies for construction work permits, and complete the filing for fire safety completion inspection and acceptance procedures within five business days after passing the construction completion inspection and acceptance. If the construction entity fails to pass the fire safety inspection before such venue is put into use, or fails to conform to the fire safety requirements after such inspection, it shall be subject to (i) orders to suspend the construction of projects, use of such projects or operation of relevant business; and (ii) a fine ranging between RMB30,000 and RMB300,000.

C. Organizational Structure.

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



Notes:

- (1) Messrs. Shuai Feng and Weixian Xia are senior employees of our company and they hold 95.0% and 5.0% equity interests in the VIE, respectively.
- (2) The remaining 31.5% equity interests in Yunfu EHang Intelligent Technology Limited are held by our joint venture partners.

Contractual Arrangements with the VIE and its Shareholders

The following is a summary of the currently effective contractual arrangements by and among the WFOE, the VIE and the VIE's shareholders.

Contractual Agreements that Provide Us with Power to Direct the Activities of the VIE

Shareholders Voting Proxy Agreement. Pursuant to the shareholders voting proxy agreement dated October 21, 2020 and the power of attorney granted thereunder, each of the VIE's shareholders irrevocably authorizes the WFOE to act as his attorney-in-fact to exercise all of his rights as a shareholder of the VIE, including, but not limited to, the right to (i) attend shareholders' meetings; (ii) vote on any resolution that requires a shareholder vote pursuant to applicable laws and the articles of association of the VIE, such as the sale and transfer of all or part of the equity interests owned by such shareholder; and (iii) designate and appoint legal representative, directors, supervisors, general manager and other senior management. The shareholders voting proxy agreement will remain effective for 20 years and can be extended at the WFOE's sole discretion. The power of attorney granted under the shareholders voting proxy agreement will remain effective continuously from the date of execution, and the WFOE is entitled to assign its rights relating to the equity interests to any other person or entity at its own discretion.

Loan Agreement. Pursuant to the special agreement on the capital increase of the VIE dated February 22, 2019, or the loan agreement, among the WFOE, and the shareholders of the VIE, which was amended on September 7, 2020 and October 21, 2020, respectively, the WFOE has granted interest-free loans with an aggregate amount of RMB60 million to the shareholders of the VIE for the sole purpose of providing funds necessary for the capital increase to the VIE. The loans shall be repaid by the shareholders of the VIE through a transfer of their equity interests in the VIE to the WFOE, in proportion to the amount of the loans to be repaid. As of the date of this annual report, the full amount of these loans remains outstanding.

Share Pledge Agreements. Pursuant to the share pledge agreements, dated October 21, 2020, between the WFOE and each of the shareholders of the VIE, the shareholders of the VIE have pledged their entire equity interests in the VIE to the WFOE, to guarantee the performance of their obligations under the exclusive consulting and services agreement, the share pledge agreement and the exclusive option agreement described elsewhere in this annual report. In the event of a breach by any of the VIE's shareholders of his contractual obligations under the relevant agreements, the WFOE, as pledgee, will have the right to acquire all or part of the pledged equity interests in the VIE. The shareholders of the VIE also undertake that, without the prior written consent of the WFOE, they will not create any encumbrance on or otherwise transfer or dispose of their respective equity interests in the VIE. The share pledge agreements will remain effective until all the contractual obligations under the relevant agreement have been satisfied in full. As of the date of this annual report, we have registered the share pledges with the relevant authorities in accordance with PRC regulations.

Agreement that Allows Us to Receive Economic Benefits from the VIE

Exclusive Consulting and Services Agreements. Pursuant to the exclusive technical consulting and service agreement and the exclusive services agreement, each dated January 29, 2016, and subsequently amended on November 30, 2018, or the exclusive consulting and services agreements, between the WFOE and the VIE, the WFOE has the exclusive right to provide the VIE and the VIE's subsidiaries with consulting and services, including but not limited to those relating to the development, manufacturing and sales of intelligent aerial vehicles. Without the WFOE's prior written consent, the VIE cannot, directly or indirectly, accept any consulting services subject to this agreement from any third party. the VIE agrees to pay the WFOE a service fee equal to 100% of the consolidated net profits of the VIE after the VIE turns profitable on a cumulative basis and after netting off certain expenses. Our WFOE has the sole discretion in determining the service fee charged to the VIE under this agreement. Our WFOE has the exclusive ownership of all the intellectual property rights created as a result of the performance of the exclusive consulting and services agreement to the extent permitted by applicable PRC laws. The exclusive consulting and services agreement will remain effective for ten years, unless otherwise terminated by the WFOE with 30 days' prior notice at any time, or by the VIE if the WFOE is grossly negligent.

Agreement that Provides Us with the Option to Purchase the Equity Interests in the VIE

Exclusive Option Agreement. Pursuant to the exclusive option agreement, dated October 21, 2020, among the WFOE, the VIE and the shareholders of the VIE, each of the shareholders of the VIE has irrevocably granted the WFOE an exclusive option to purchase all or part of his equity interests in the VIE. Our WFOE or its designated person may exercise such options at the lowest price permitted under applicable PRC laws. Any proceeds received by the shareholders of the VIE from the exercise of the options shall be remitted to the WFOE or its designated party, to the extent permitted under applicable PRC laws. The shareholders of the VIE undertake that, without the WFOE's prior written consent, they will not, among other things, (i) create any pledge or encumbrance on their equity interests in the VIE, and (ii) transfer or otherwise dispose of their equity interests in the VIE. The exclusive option agreements will remain effective until all equity interests in the VIE have been transferred to the WFOE or our designated person. The WFOE may terminate the agreement at its sole discretion.

In the opinion of AllBright Law Offices, our PRC legal counsel:

- the ownership structures of the WFOE, the VIE and the VIE's subsidiaries are in compliance with applicable PRC laws and regulations; and
- such contractual arrangements constitute valid, legal and binding obligations enforceable against each party of such agreements in accordance with the terms of each agreement from their respective effective dates to the date of this annual report, and will not result in any violation of PRC laws or regulations currently in effect.

However, our PRC legal counsel has also advised us that there are substantial uncertainties regarding the interpretation and application of current and future PRC laws, regulations and rules; accordingly, the PRC regulatory authorities may take a view that is contrary to the opinion of our PRC legal counsel. It is uncertain whether any new PRC laws or regulations relating to variable interest entity structures will be adopted or if adopted, what they would provide. If we or the VIE is found to be in violation of any existing or future PRC laws or regulations, or fail to obtain or maintain any of the required permits or approvals, the relevant PRC regulatory authorities would have broad discretion to take action in dealing with such violations or failures. See "Item 3. Key Information—D. Risk Factors—Risks Relating to Our Corporate Structure—If the PRC government finds that the contractual arrangements between the WFOE, the VIE and the VIE's shareholders do not comply with PRC regulations relating to the relevant industries, or if these regulations or the interpretation of existing regulations change in the future, we could be subject to severe penalties or be forced to relinquish our interests in those operations".

D. Property, plants and equipment.

Our headquarters is located in Guangzhou, China, where we lease and occupy our office space with an aggregate floor area of approximately 66,524 square meters from unrelated third parties under operating lease agreements. Our new AAV production facility in Yunfu city, China has a total planned gross floor area of 24,000 square meters. A substantial majority of our employees are based at our headquarters in Guangzhou. As of the date of this annual report, we do not currently own any of our premises.

We believe that our existing facilities are generally adequate to meet our current needs, but we expect to seek additional space as needed to accommodate our future growth.

Item 4A. Unresolved Staff Comments

Not applicable.

Item 5. Operating and Financial Review Prospects

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

A. Operating Results.

Overview

We are an autonomous aerial vehicle technology platform company. We are pioneering the future of transportation through our proprietarily developed AAVs, related commercial solutions and services.

We, the VIE and the VIE's subsidiaries design, develop, manufacture, sell and operate AAVs and their supporting systems and infrastructure for a broad range of industries and applications, including passenger transportation, logistics, smart city management and aerial media solutions. We aim to make it safe and convenient for both passengers and goods to take to the air.

We delivered our first passenger-carrying AAV to a customer in March 2018. Since then, we and the VIE had delivered 185 units of the EH216 series AAVs as of December 31, 2022. As we continue to refine and commercialize our AAVs and air mobility solutions, we believe we will be able to capture addressable markets across multiple industries and develop AAV commercial applications in new industries.

Our revenues decreased by 68.5% from RMB180.1 million in 2020 to RMB56.8 million in 2021, and decreased by 22% to RMB44.3 million (US\$6.4 million) in 2022. Our net loss increased by 241.0% from RMB92.0 million in 2020 to RMB313.9 million in 2021, and increased by 4.9% to RMB329.3 million (US\$47.7 million) in 2022. In 2022, revenues generated by air mobility solutions, smart city management solutions and aerial media solutions were RMB40.4 million (US\$5.9 million), RMB2.1 million (US\$0.3 million) and RMB1.3 million (US\$0.2 million), representing 91.2%, 4.8% and 3.0% of our total revenues, respectively.

Key Components of Results of Operations

Revenues

We generate revenues from air mobility solutions, smart city management solutions, aerial media solutions and others. The following table sets forth a breakdown of our total revenues in absolute amounts and percentages of our total revenues for the periods presented:

	For the Year Ended December 31,						
	2020		2021		2022		
	RMB	%	RMB	%	RMB	US\$	%
	(in thousands, except for percentages)						
Revenues:							
Air mobility solutions	105,969	58.8	48,156	84.8	40,387	5,856	91.2
Smart city management solutions	8,282	4.6	7,135	12.6	2,133	309	4.8
Aerial media solutions	65,656	36.5	1,100	1.9	1,341	194	3.0
Others	186	0.1	416	0.7	456	66	1.0
Total	180,093	100.0	56,807	100.0	44,317	6,425	100.0

Air mobility solutions. Revenues from air mobility solutions consist of revenues from (i) sales of the EH216 series AAVs and (ii) provision of logistics services. Revenues from sales of the EH216 series AAVs are based on firm customer orders with fixed terms and conditions, including pricing, net of discounts, if any. The performance obligation under the contract is the delivery of AAVs, which is satisfied at a point in time, in general upon our receipt of acknowledgement receipts from customers or under some circumstances upon the AAVs have been shipped to the contractually agreed location when the products are sold to customers outside PRC. Our revenues from air mobility solutions in 2022 were mainly derived from sales of the EH216 series AAVs to customers mainly operated on a limited trial basis in tourism locations in China for testing, training and demonstration purposes. Before regulatory approvals for the commercial operations of our AAVs have been obtained in China and/or other relevant jurisdictions, customer demand will likely be limited in volume. Currently we are working to obtain such approvals in China. However, we are unable to predict the timing of such approvals.

Smart city management solutions. Smart city management solutions mainly include (i) design and development of command-and-control systems and related facilities, and (ii) sale of AAVs and other related products. For design and development of command-and-control systems and related facilities, we recognize revenues using a percentage of completion method. We typically enter into project contracts with customers, according to which they pay project fees based on the agreed schedule. As we provide smart city management solutions on a project basis with high individual transaction values, revenues from smart city management solutions may be more concentrated in certain years or periods, and therefore are subject to greater period-to-period fluctuations.

Aerial media solutions. We recognize revenues from aerial media solutions when the aerial media performance is fulfilled by us or customers purchase aerial media solution packages from us. The service fee for each performance is determined mainly by the length of performance, complexity, number of AAVs involved, manpower and regulatory requirements. The purchase price for aerial media solution packages consists of small-sized aerial media AAVs or component packages, related software, maintenance and/or training services, etc.

Others. We generate other revenues mainly from stand-alone sales of consumer drones and their components and spare parts. We recognize revenues from others when the consumer drones are delivered and the control of the drones has been transferred to the customers. We started to phase out our consumer drone business in late 2016.

We expect that our revenues will increase after obtaining required certificates and approvals in China as we will continue to fulfill existing orders and pre-orders for the EH216 series AAVs, secure new orders for our air mobility solutions, provide air mobility operational services, offer smart city management and aerial media solutions and expand our commercial solutions and sales network. We expect that the increase in revenues generated from air mobility solutions will be the main increase in both domestic and international markets.

Costs of revenues

Costs of revenues consist primarily of aerial vehicles material and manufacturing costs, construction costs of smart city management solutions, depreciation, rental fees, payroll and related costs of operations.

We expect that our costs of revenues will increase in the foreseeable future as we increase our AAV sales volume and expand our commercial solutions business.

Operating expenses

Our total operating expenses consist of sales and marketing expenses, general and administrative expenses and research and development expenses. The following table sets forth the components of our total operating expenses by amounts and percentages of operating expenses for the periods presented:

	For the Year Ended December 31,					
	2020		2021		2022	
	RMB	%	RMB	%	RMB	US\$
	(in thousands, except for percentages)					
Sales and marketing expenses	37,186	18.2	43,229	11.7	53,116	7,701
General and administrative expenses	61,613	30.2	187,388	51.0	151,065	21,902
Research and development expenses	105,252	51.6	137,148	37.3	135,082	19,585
Total operating expenses	204,051	100.0	367,765	100.0	339,263	49,188

Sales and marketing expenses. Our sales and marketing expenses primarily consist of advertising and promotion expenses, payroll and related expenses for personnel in sales and marketing.

General and administrative expenses. Our general and administrative expenses mainly consist of payroll and related costs for employees in general corporate functions, professional fees, allowance for doubtful account expenses, impairment of long-lived assets, and other general corporate expenses, as well as expenses associated with the use by these functions of facilities and equipment, such as depreciation and rental expenses.

Research and development expenses. Our research and development expenses mainly consist of payroll and benefits for our research and development personnel, as well as expenses associated with our research and development activities.

Other operating income

Other operating income mainly consists of financial subsidies that we received from provincial and local governments for operating our business in their jurisdictions in compliance with certain promoted policies.

Taxation

Cayman Islands

We are an exempted company incorporated in the Cayman Islands. The Cayman Islands currently levies no taxes on individuals or corporations based upon profits, income, gains or appreciation and there is no taxation in the nature of inheritance tax or estate duty. There are no other taxes likely to be material to us levied by the government of the Cayman Islands except for stamp duties which may be applicable on instruments executed in, or after execution, brought within the jurisdiction of the Cayman Islands. In addition, the Cayman Islands does not impose withholding tax on dividend payments.

Hong Kong

Our wholly-owned subsidiary, Ehfly Technology Limited, or Ehfly Technology, incorporated in Hong Kong, is subject to Hong Kong profit tax on its profits arising from its business operations carried on in Hong Kong. Hong Kong profits tax for a corporation from the year of assessment 2018/2019 onwards is generally 8.25% on assessable profits up to HK\$2.0 million; and 16.5% on any part of assessable profits over HK\$2.0 million. Under the Hong Kong Inland Revenue Ordinance, profits that we derive from sources outside of Hong Kong are not generally chargeable to Hong Kong profits tax. As such, Ehfly Technology is exempted from the Hong Kong income tax on its foreign-derived income. In addition, payments of dividends from Ehfly Technology to our company are not subject to any withholding tax in Hong Kong. No provision for Hong Kong profits tax was made as we had no estimated assessable profit that was subject to Hong Kong profits tax during 2022.

PRC

Under the Enterprise Income Tax Law, or the EIT Law, our PRC subsidiaries, the VIE and the VIE's subsidiaries are subject to a statutory income tax rate of 25%. The WFOE, the VIE and EHang Egret have each been qualified as a high and new technology enterprise, or HNTE, since December 2017, November 2016 and November 2018, respectively, and are eligible for a 15% preferential tax rate, which will expire in December 2023, and has expired in December 2022 and in November 2021, respectively.

The EIT law also imposes a withholding income tax of 10% on dividends distributed by a foreign invested enterprise, or FIE, to its immediate holding company outside China, if such immediate holding company is considered as a non-resident enterprise without any establishment or place within China or if the received dividends have no connection with the establishment or place of such immediate holding company within China, unless such immediate holding company's jurisdiction of incorporation has a tax treaty with China that provides for a different withholding arrangement. According to the Arrangement Between Mainland China and Hong Kong Special Administrative Region on the Avoidance of Double Taxation and Prevention of Fiscal Evasion in August 2006, dividends paid by an FIE in China to its immediate holding company in Hong Kong will be subject to withholding tax at a rate of no more than 5%, if the immediate holding company owns at least 25% of the equity interest of the FIE and satisfies all other requirements under the tax arrangement and receives approval from the relevant tax authority. We did not record any dividend withholding tax, as our PRC entities have no retained earnings in the periods presented. See "Item 3. Key Information—D. Risk Factors—Risks Relating to Doing Business in China—We may not be able to obtain certain benefits under the relevant tax treaty on dividends paid by our PRC subsidiaries to us through our Hong Kong subsidiary."

The EIT Law also provides that an enterprise established under the laws of a foreign country or region but whose “de facto management body” is located in the PRC be treated as a resident enterprise for PRC tax purposes and consequently be subject to the PRC income tax at the rate of 25% for its global income. The implementing rules of the EIT Law define the location of the “de facto management body” as “the place where the exercising, in substance, of the overall management and control of the production and business operation, personnel, accounting, property, etc., of a non-PRC company is located.” Based on a review of surrounding facts and circumstances, we do not believe that it is likely that our operations outside the PRC should be considered a resident enterprise for PRC tax purposes. If our holding company in the Cayman Islands or any of our subsidiaries outside China were deemed to be a “resident enterprise” under the EIT Law, it would be subject to enterprise income tax on its worldwide income at a rate of 25%. See “Item 3. Key Information—D. Risk Factors—Risks Relating to Doing Business in China—If we are classified as a PRC resident enterprise for PRC income tax purposes, such classification could result in unfavorable tax consequences to us and our non-PRC shareholders or ADS holders.”

Under the EIT Law, research and development expenses that have not formed intangible assets are included in the profit and loss account for the current year. Besides deducting the actual amount of research and development expenses incurred, according to the Notice on Raising the Ratio of Deduction of Research and Development Expenses, effective on September 20, 2018, a qualifying enterprise is allowed an additional deduction of the amount in calculating its taxable income for the relevant year, including a 75% deduction for the years ended December 31, 2020, as well as a 100% deduction for the year ended December 31, 2021 and 2022. For research and development expenses that have formed intangible assets, the tax amortization is based on 175% or 200% of the costs of the intangible assets in the relevant year.

Dividends, interests, rent or royalties payable by our PRC subsidiaries, to non-PRC resident enterprises, and proceeds from any such non-resident enterprise investor’s disposition of assets (after deducting the net value of such assets) shall be subject to 10% withholding tax, unless the respective non-PRC resident enterprise’s jurisdiction of incorporation has a tax treaty or arrangements with PRC that provides for a reduced withholding tax rate or an exemption from withholding tax.

Results of Operations

The following table sets forth a summary of our consolidated results of operations for the periods presented, both in absolute amounts and as percentages of our total revenues, for the periods presented. 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 particular period are not necessarily indicative of our future trends.

	For the Year Ended December 31,					
	2020		2021		2022	
	RMB	%	RMB	%	RMB	US\$
	(in thousands, except for percentages)					
Total revenues	180,093	100.0	56,807	100.0	44,317	6,425
Costs of revenues⁽¹⁾	(73,914)	(41.0)	(20,777)	(36.6)	(15,098)	(2,189)
Gross profit	106,179	59.0	36,030	63.4	29,219	4,236
Operating expenses:						
Sales and marketing expenses ⁽¹⁾	(37,186)	(20.7)	(43,229)	(76.1)	(53,116)	(7,701)
General and administrative expenses ⁽¹⁾	(61,613)	(34.2)	(187,388)	(329.9)	(151,065)	(21,902)
Research and development expenses ⁽¹⁾	(105,252)	(58.4)	(137,148)	(241.4)	(135,082)	(19,585)
Total operating expenses	(204,051)	(113.3)	(367,765)	(647.4)	(339,263)	(49,188)
Other operating income	6,576	3.6	11,199	19.7	6,094	884
Operating loss	(91,296)	(50.7)	(320,536)	(564.3)	(303,950)	(44,068)
Other (expense) income:						
Interest and investment income	3,795	2.1	5,143	9.1	4,669	677
Interest expenses	(2,337)	(1.3)	(1,803)	(3.2)	(3,819)	(554)
Foreign exchange loss	(333)	(0.2)	(827)	(1.5)	(1,488)	(216)
Other income	1,227	0.7	6,086	10.7	1,944	282
Other expense	(3,127)	(1.7)	(1,549)	(2.7)	(26,804)	(3,886)
Total other (expense) income	(775)	(0.4)	7,050	12.4	(25,498)	(3,697)

	For the Year Ended December 31,					
	2020		2021		2022	
	RMB	%	RMB	%	RMB	US\$
	(in thousands, except for percentages)					
Loss before income tax and income (loss) from equity method investment	(92,071)	(51.1)	(313,486)	(551.8)	(329,448)	(47,765)
Income tax expenses	(206)	(0.1)	(134)	(0.2)	(79)	(11)
Loss before income (loss) from equity method investment	(92,277)	(51.2)	(313,620)	(552.1)	(329,527)	(47,776)
Income (loss) from equity method investment	236	0.1	(276)	(0.5)	196	28
Net loss	(92,041)	(51.1)	(313,896)	(552.6)	(329,331)	(47,748)

Note:

- (1) Share-based compensation expense was allocated in costs of revenues and operating expenses as follows:

	For the Year Ended December 31,			
	2020	2021	2022	
	RMB	RMB	RMB	US\$
	(in thousands, except share and share related data)			
Costs of revenues	2,443	—	—	—
Sales and marketing expenses	10,883	18,327	22,125	3,208
General and administrative expenses	14,453	71,147	38,452	5,575
Research and development expenses	27,078	31,657	36,321	5,266
Total	54,857	121,131	96,898	14,049

Year ended December 31, 2022 compared with year ended December 31, 2021

Revenues

Our total revenues decreased by 22.0% from RMB56.8 million in 2021 to RMB44.3 (US\$6.4 million) in 2022, as we have been strategically transitioning from a product sales centric model into an integrated model of both product sales and AAV operational flight services, and we have been progressing the certification process for EH216-S.

Revenues from air mobility solutions decreased by 16.1% from RMB48.2 million in 2021 to RMB40.4 million (US\$5.9 million) in 2022. We sold 21 units of the EH216 series AAVs in 2022, compared with 30 units in 2021.

Revenues from smart city management solutions decreased by 70.1% from RMB7.1 million in 2021 to RMB2.1 million (US\$0.3 million) in 2022. Since the smart city management solutions are on a project basis with different individual transaction values depending on the project nature, project size, etc., revenues from smart city management solutions may be more concentrated in certain years or periods, and therefore are subject to greater period-to-period fluctuations.

Revenues from aerial media solutions increased by 21.9% from RMB1.1 million in 2021 to RMB1.3 million (US\$0.2 million) in 2022.

Costs of revenues

Our costs of revenues decreased by 27.3% from RMB20.8 million in 2021 to RMB15.1 million (US\$2.2 million) in 2022, which resulted from and was in line with the total revenues.

Gross profit and gross profit margin

As a result of the foregoing, our gross profit decreased by 18.9% from RMB36.0 million in 2021 to RMB29.2 million (US\$4.2 million) in 2022. However, our gross profit margin increased from 63.4% in 2021 to 65.9% in 2022 primarily due to higher averaging selling price of EH216 AAVs in 2022.

Operating expenses

Our operating expenses decreased by 7.8% from RMB367.8 million in 2021 to RMB339.3 million (US\$49.2 million) in 2022, primarily due to a decrease in share-based compensation expenses by RMB24.2 million (US\$3.5 million), decrease in provisions for accounts receivable by RMB13.3 million (US\$1.9 million) as well as decrease in professional services fees by RMB3.4 million (US\$0.5 million).

Sales and marketing expenses. Sales and marketing expenses increased by 22.9% from RMB43.2 million in 2021 to RMB53.1 million (US\$7.7 million) in 2022, primarily due to increase in share-based compensation expenses for new grant of share-based awards by RMB3.8 million (US\$0.6 million) and salaries and benefits costs for increased headcounts by RMB2.9 million (US\$0.4 million) as well as increase in marketing expenses for promotional activities in China and overseas markets by RMB2.7 million (US\$0.4 million).

General and administrative expenses. General and administrative expenses decreased by 19.4% from RMB187.4 million in 2021 to RMB151.1 million (US\$21.9 million) in 2022, mainly due to decrease in share-based compensation expenses for a certain portion of share-based awards vested in 2021 by RMB32.7 million (US\$4.7 million), decrease in provisions for accounts receivable by RMB13.3 million (US\$1.9 million) while resulting in ending balance of allowance for doubtful accounts increasing from RMB69.4 million further to RMB115.4 million (US\$16.7 million), as well as reduction in professional services fees by RMB3.4 million (US\$0.5 million), while partially offset by increase in salaries and benefits costs for increased headcounts by RMB6.1 million (US\$0.9 million).

Research and development expenses. Research and development expenses slightly decreased by 1.5% from RMB137.2 million in 2021 to RMB135.1 million (US\$19.6 million) in 2022. The decrease was mainly due to less expenditures on EH216 AAV's hardware and software upgrades and focus more on type certification processes, while offset by increase in share-based compensation for new grant of share-based awards by RMB4.7 million (US\$0.7 million) and salaries and benefits costs by RMB6.4 million (US\$0.9 million).

Other operating income

Other operating income decreased by 45.6% from RMB11.2 million in 2021 to RMB6.1 million (US\$0.9 million) in 2022, primarily due to decrease in government subsidies.

Interest and investment income

We recorded interest and investment income of RMB4.7 million (US\$0.7 million) in 2022 and 5.1 million in 2021, both of which consisted primarily of interest earned from our cash and cash equivalents, short-term investments and long-term loans receivable.

Interest expenses

We recorded interest expenses of RMB3.8 million (US\$0.6 million) in 2022 and RMB1.8 million in 2021, both of which were primarily related to bank loans and loans from third parties. In 2022, we recognized interest expenses RMB1.7 million (US\$0.2 million) as the amortization of debt discounts for the private placement transaction.

Other income

Other income was RMB1.9 million (US\$0.3 million) in 2022 and RMB6.1 million in 2021.

Other expense

Other expenses increased from RMB1.5 million in 2021 to RMB26.8 million (US\$3.9 million) in 2022. Other expenses in 2022 were mainly attributable to the estimated provision of US\$3.375 million for an employment dispute. See “Item 8. Financial Information—A. Consolidated Statements and Other Financial Information—Legal Proceedings.”

Income tax expenses

Our income tax expenses decreased from RMB0.1 million in 2021 to RMB0.08 million (US\$0.01 million) in 2022. We did not have significant income tax expenses because most of our subsidiaries and consolidated affiliated entities were loss making in 2021 and 2022.

Net loss

As a result of the foregoing, our net loss slightly increased by 4.9% from RMB313.9 million in 2021 to RMB329.3 million (US\$47.7 million) in 2022.

Year ended December 31, 2021 compared with year ended December 31, 2020

Revenues

Our total revenues decreased by 68.5% from RMB180.1 million in 2020 to RMB56.8 (US\$8.9 million) in 2021, as we have been strategically transitioning from a product sales centric model into an integrated model of both product sales and AAV operational flight services, and we have been progressing the certification process for EH216-S.

Revenues from air mobility solutions decreased by 54.6% from RMB106.0 million in 2020 to RMB48.2 million (US\$7.5 million) in 2021. We sold 30 units of the EH216 series AAVs in 2021, compared with 70 units in 2020.

Revenues from smart city management solutions decreased by 13.8% from RMB8.3 million in 2020 to RMB7.1 million (US\$1.1 million) in 2021. Since the smart city management solutions are on a project basis with different individual transaction values depending on the project nature, project size, etc. Revenues from smart city management solutions may be more concentrated in certain years or periods, and therefore are subject to greater period-to-period fluctuations.

Revenues from aerial media solutions decreased by 98.3% from RMB65.7 million in 2020 to RMB1.1 million (US\$0.2 million) in 2021, primarily due to strategic adjustment to more focus on the core business air mobility solutions.

Costs of revenues

Our costs of revenues decreased by 71.9% from RMB73.9 million in 2020 to RMB20.8 million (US\$3.3 million) in 2021, which resulted from and was in line with the total revenues.

Gross profit and gross profit margin

As a result of the foregoing, our gross profit decreased by 66.1% from RMB106.2 million in 2020 to RMB36.0 million (US\$5.6 million) in 2021. However, our gross profit margin increased from 59.0% in 2020 to 63.4% in 2021 primarily due to a favorable revenue mix with a contribution from a command-and-control system delivered in 2021.

Operating expenses

Our operating expenses increased by 80.2% from RMB204.1 million in 2020 to RMB367.8 million (US\$57.7 million) in 2021, primarily due to the increase of RMB66.3 million (US\$10.4 million) in share-based compensation expenses and increase of RMB43.2 million (US\$6.8 million) in allowance for doubtful accounts charged to operating expenses. The increase primarily resulted from the new grants of restricted share units as approved by our board of directors in January 2021.

Sales and marketing expenses. Sales and marketing expenses increased by 16.3% from RMB37.2 million in 2020 to RMB43.2 million (US\$6.8 million) in 2021, primarily due to an increase in share-based compensation expenses.

General and administrative expenses. General and administrative expenses increased by 204.1% from RMB61.6 million in 2020 to RMB187.4 million (US\$29.4 million) in 2021. The increase was mainly due to an increase in share-based compensation expenses, one-time additional expenses related to extension of annual report filing and the additional provisions for accounts receivable in light of the impacts from the COVID-19 epidemic and control measures in China.

Research and development expenses. Research and development expenses increased by 30.3% from RMB105.3 million in 2020 to RMB137.2 million (US\$21.5 million) in 2021. The increase was mainly due to continuously growing R&D expenditure for the development of AAV models, including the EH216 series, the VT-30 and new models, and their related operating systems with enhanced functionalities. R&D expenses were also impacted by an increase of the R&D team and related salary and benefit expenses that reflect our commitment to strengthening its product development and certification efforts in order to drive future sales growth and commercial operations.

Other operating income

Other operating income increased by 70.3% from RMB6.6 million in 2020 to RMB11.2 million (US\$1.8 million) in 2021, primarily due to an increase in government subsidies.

Interest and investment income

We recorded interest and investment income of RMB5.1 million (US\$0.8 million) in 2021 and 3.8 million in 2020, both of which consisted primarily of interest earned from our cash and cash equivalents, short-term investments and long-term loans receivable.

Interest expenses

We recorded interest expenses of RMB1.8 million (US\$0.3 million) in 2021 and RMB2.3 million in 2020, both of which were related to bank loans and loans from third parties.

Other income

Other income was RMB6.1 million (US\$1.0 million) in 2021 and RMB1.2 million in 2020.

Other expense

Other expenses decreased from RMB3.1 million in 2020 to RMB1.5 million (US\$0.2 million) in 2021. Other expenses in 2020 were mainly attributable to donations of medical supplies to COVID-19 impacted countries and allowance for doubtful non-operating receivables, while there were no such transactions in 2021.

Income tax expenses

Our income tax expenses decreased from RMB0.2 million in 2020 to RMB0.1 million (US\$0.02 million) in 2021. We did not have significant income tax expenses because most of our subsidiaries and consolidated affiliated entities were loss making in 2020 and 2021.

Net loss

As a result of the foregoing, our net loss increased by 241.0% from 92.0 million in 2020 to RMB313.9 million (US\$49.3 million) in 2021.

B. Liquidity and Capital Resources.

The accompanying consolidated financial statements have been prepared assuming that we will continue as a going concern, which contemplates the realization of assets and the satisfaction of liabilities during the normal course of operations. We have experienced recurring losses from operations since inception. As of December 31, 2021 and 2022, we had an accumulated deficit of RMB1,122.2 million and RMB1,450.4 million (US\$210.3 million). For the years ended December 31, 2020, 2021 and 2022, we incurred net loss of RMB92.0 million, RMB313.9 million and RMB329.3 million (US\$47.7 million) and had net cash used in operating activities of RMB151.7 million, RMB121.6 million and RMB173.5 million (US\$25.1 million). As of December 31, 2022, our cash and cash equivalents balance were RMB249.3 million (US\$36.1 million). Up to the date of this annual report, we had unused loan facilities of RMB10 million with expiration date of February 9, 2024. Our ability to continue as a going concern currently largely dependent on when we will obtain the type certificate of our EH216-S in the near term to launch fully commercial sales of our EH216-S autonomous aerial vehicle, and raising additional funds through debt financings or equity offerings. We expect to obtain the type certificate in the near future as more than 90% of the entire Type Certification processes of EH216-S have been completed, as of the date of this annual report. However, there is uncertainty as to when we will obtain the type certificate of its EH216-S in the near term, which may materially and adversely affect the execution of our business plan. Our primary sources of liquidity have been proceeds from issuance of equity securities offerings, including private placements, as well as customer advances, short-term and long-term bank loans. For example, we had raised a total of US\$50 million from the sale and issuance of our Class A ordinary shares in private placements as of the date of this annual report, including US\$40 million in 2021 and US\$10 million in 2023. With respect to the 2023 private placement, we received the RMB equivalent of US\$10 million as interim funding from the investor prior to closing, and accounted for a significant portion of the funds as short-term debt and the remaining portion as additional paid-in capital. We have repaid the interim funding as of the date of this annual report. As of December 31, 2022, we had RMB249.3 million (US\$36.1 million) in cash and cash equivalents and short-term investments, of which 53.6% were held in Renminbi and the remainder was held in U.S. dollars and other currencies, and of which 96.5% were held in the PRC. Our cash and cash equivalents consist primarily of cash on hand and highly liquid investments which are unrestricted as to withdrawal or use, and which have original maturities of three months or less.

We believe that our current cash and cash equivalents and our anticipated cash flows from operations will be sufficient to meet our anticipated working capital requirements and material cash requirements for at least the next 12 months. However, we may need additional cash resources in the future if we experience changes in business conditions or other developments, or if we pursue opportunities for investment, acquisition, capital expenditure or similar actions. If we determine that our cash requirements exceed the amount of cash we have on hand, we may seek to issue equity or equity linked securities or obtain debt financing. The issuance and sale of additional equity would result in further dilution to our shareholders. The incurrence of indebtedness would result in increased fixed obligations and could result in covenants that would restrict our operations. We cannot assure you that financing will be available in amounts or on terms acceptable to us, if at all. In utilizing the proceeds, we received from our securities offerings including our initial public offering and private placements, we may make additional capital contributions to our PRC subsidiaries, establish new PRC subsidiaries and make capital contributions to these new PRC subsidiaries, make loans to our PRC subsidiaries, or acquire offshore entities with operations in China in offshore transactions. However, most of these uses are subject to PRC regulations. See "Item 3. Key Information—D. Risk Factors—Risks Relating to Doing Business in China—PRC regulation of loans to and direct investment in PRC entities by offshore holding companies and governmental control of currency conversion may delay or prevent us from using the proceeds of our offshore offerings to make loans to or make additional capital contributions to our PRC subsidiaries, the VIE and the VIE's subsidiaries, which could materially and adversely affect our liquidity and our ability to fund and expand our business." and "Item 14. Material Modifications to the Rights of Security Holders and Use of Proceeds—Use of Proceeds."

A majority of our revenues have been, and we expect they are likely to continue to be, in the form of Renminbi. Under existing PRC foreign exchange regulations, payments of current account items, including profit distributions, interest payments and trade and service-related foreign exchange transactions, can be made in foreign currencies without prior SAFE approval as long as certain routine procedural requirements are fulfilled. Therefore, our PRC subsidiaries are allowed to pay dividends in foreign currencies to us without prior SAFE approval by following certain routine procedural requirements. However, current PRC regulations permit our PRC subsidiaries to pay dividends to us only out of its accumulated profits, if any, determined in accordance with Chinese accounting standards and regulations. Our PRC subsidiaries are required to set aside at least 10% of its after-tax profits after making up previous years' accumulated losses each year, if any, to fund certain reserve funds until the total amount set aside reaches 50% of its registered capital. These reserves are not distributable as cash dividends. Historically, our PRC subsidiaries have not paid dividends to us, and it will not be able to pay dividends until it generates accumulated profits. Furthermore, capital account transactions, which include foreign direct investment and loans, must be approved by and/or registered with SAFE, its local branches and certain local banks.

As a Cayman Islands exempted company and offshore holding company, we are permitted under PRC laws and regulations to provide funding to our PRC subsidiaries only through loans or capital contributions, subject to the approval of government authorities and limits on the amount of capital contributions and loans. This may delay us from using the proceeds from our securities offerings to make loans or capital contributions to our PRC subsidiaries. See "Item 3. Key Information—D. Risk Factors—Risks Relating to Doing Business in China—PRC regulation of loans to and direct investment in PRC entities by offshore holding companies and governmental control of currency conversion may delay or prevent us from using the proceeds of our offshore offerings to make loans to or make additional capital contributions to our PRC subsidiaries, the VIE and the VIE's subsidiaries, which could materially and adversely affect our liquidity and our ability to fund and expand our business."

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

	For the Year Ended December 31,			
	2020	2021	2022	
	RMB	RMB	RMB	US\$
	(in thousands)			
Net cash used in operating activities	(151,696)	(121,629)	(173,458)	(25,148)
Net cash (used in) provided by investing activities	(66,209)	(33,401)	56,400	8,176
Net cash provided by financing activities	42,680	266,947	106,740	15,475
Effect of exchange rate changes on cash, cash equivalents and restricted cash	(6,264)	(5,067)	12,605	1,828
Net increase (decrease) in cash, cash equivalents and restricted cash	(181,489)	106,850	2,287	332
Cash, cash equivalents and restricted cash at the beginning of the year	321,662	140,173	247,023	35,815
Cash, cash equivalents and restricted cash at the end of the year	140,173	247,023	249,310	36,147

Operating Activities

Net cash used in operating activities in 2022 was RMB173.5 million (US\$25.1 million). This amount was primarily attributable to net loss of RMB329.3 million (US\$47.8 million), adjusted to add back certain non-cash expenses, principally share-based compensation of RMB96.9 million (US\$14.0 million), allowance for doubtful amounts of RMB47.8 million (US\$6.9 million), amortization of right-of-use assets of RMB12.0 million (US\$1.7 million) and depreciation of property and equipment of RMB8.5 million (US\$1.2 million), and further adjusted upwards due to changes in operating assets and liabilities. The changes in operating assets and liabilities primarily included an increase of RMB10.1 million (US\$1.5 million) in accounts receivable in relation to the receivables that we are entitled to receive, an increase of RMB2.3 million (US\$0.3 million) in inventories in relation to procurement of materials for production and finished goods, an increase of RMB22.9 million (US\$3.3 million) in prepayments in relations of prepayments to suppliers and other service providers, and a decrease of RMB10.1 million (US\$1.5 million) in accounts payable in relation to payments for purchase of materials and offset mainly by a decrease of RMB1.3 million (US\$0.2 million) in amount due from a related party in relation to the receipt of outstanding payment for sale of product, and an increase of RMB4.5 million (US\$0.7 million) in contract liabilities in relation to more payments received before the sale of products or services to customers, and an increase of RMB36.3 million (US\$5.3 million) which was mainly due to the estimated provision of US\$3.375 million for an employment dispute. See "Item 8. Financial Information—A. Consolidated Statements and Other Financial Information—Legal Proceedings."

Net cash used in operating activities in 2021 was RMB121.6 million. This amount was primarily attributable to net loss of RMB313.9 million (US\$49.3 million), adjusted to add back certain non-cash expenses, principally share-based compensation of RMB121.1 million (US\$19.0 million), allowance for doubtful amounts of RMB56.5 million (US\$8.9 million) and depreciation and amortization of RMB7.8 million (US\$1.2 million), and further adjusted upwards due to changes in operating assets and liabilities. The changes in operating assets and liabilities primarily included an increase of RMB36.0 million (US\$5.6 million) in inventories in line with our business expansion, an increase of RMB13.0 million (US\$2.0 million) in prepayments, and a decrease of RMB7.7 million (US\$1.2 million) in accounts payable and offset mainly by a decrease of RMB39.3 million (US\$6.2 million) in accounts receivable resulting from our efforts in collections from customers, a decrease of RMB1.3 million (US\$0.2 million) in amount due from a related party, and an increase of RMB7.1 million (US\$1.1 million) in contract liabilities, and an increase of RMB11.4 million (US\$1.8 million) which was mainly due to an increase in employee benefits-related liabilities resulting from our increased employee headcount. The increases in inventories and prepayments and other current assets were all primarily due to the growth of our business.

Net cash used in operating activities in 2020 was RMB151.7 million. This amount was primarily attributable to net loss of RMB92.0 million, adjusted to add back certain non-cash expenses, principally share-based compensation of RMB54.9 million and depreciation and amortization of RMB6.2 million, allowance for doubtful accounts of RMB13.3 million, and further adjusted downwards due to changes in operating assets and liabilities. The changes in operating assets and liabilities primarily included an increase of RMB134.7 million in accounts receivable resulting from our slower collections from customers due to COVID-19 impacts in 2020, an increase of RMB29.3 million in inventories in line with our business expansion, an increase of RMB5.0 million in prepayments and other current assets, an increase of RMB2.6 million in amount due from a related party, an increase of RMB 16.2 million in other non-current assets, and an increase of RMB2.4 million in contract liabilities, and partially offset by an increase of RMB26.6 million in accounts payable, a decrease of RMB13.5 million in cost and estimated earnings in excess of billings, an increase of RMB7.7 million in accrued expenses and other liabilities, a decrease of RMB4.3 million in unbilled revenue, and an increase of RMB3.7 million in deferred income. The increases in accounts receivable, inventories, amount due from a related party, prepayments and other current assets, other non-current assets, contract liabilities, accounts payable and accrued expenses and other liabilities were all primarily due to the growth of our business. The decrease in cost and estimated earnings in excess of billings was primarily due to incremental billings and collection in connection with two completed smart city management projects. The increase in unbilled revenue was primarily due to certain services provided but unbilled. The increase in deferred income was primarily due to receipt of upfront payment of shared income from a third-party service provider.

Investing Activities

Net cash provided by investing activities in 2022 was RMB56.4 million (US\$8.2 million), mainly consisting of net proceeds of short-term investments of RMB74.6 million (US\$10.8 million) and purchase of property and equipment of RMB12.2 million (US\$1.8 million) for both Yunfu production facility and new headquarter office.

Net cash used in investing activities in 2021 was RMB33.4 million, mainly consisting of net purchase of short-term investments of RMB17.0 million (US\$2.7 million) and purchase of property and equipment of RMB15.6 million (US\$2.5 million) for Yunfu production facility.

Net cash used in investing activities in 2020 was RMB66.2 million, consisting of net purchase of short-term investments of RMB43.4 million, net loans to third parties of RMB13.9 million and purchase of property and equipment of RMB8.7 million.

Financing Activities

Net cash provided by financing activities in 2022 was RMB106.7 million (US\$15.5 million), primarily attributable to RMB69.9 million (US\$10.1 million) from an investor in connection with a private placement of our Class A ordinary shares which had closed in the first quarter of 2023, and net proceeds of RMB36.8 million (US\$5.3 million) from bank loans.

Net cash provided by financing activities in 2021 was RMB266.9 million, primarily attributable to proceeds of RMB257.0 million (US\$40.3 million) from issuance of Class A ordinary shares to a European asset management company in a private placement and net proceeds of RMB15.0 million (US\$2.4 million) from bank loans.

Net cash provided by financing activities in 2020 was RMB42.7 million, primarily attributable to proceeds of RMB7.3 million from issuance of American depository shares pursuant to underwriters' exercise of over-allotment option related to our initial public offering and proceeds of RMB40.0 million from issuance of mandatorily redeemable non-controlling interests of a subsidiary.

Capital Expenditures

Our capital expenditures were RMB9.1 million, RMB15.6 million and RMB13.8 million (US\$2.0 million) in 2020, 2021 and 2022, respectively, which were mainly used for the purchase of property and equipment for the establishment and installation of equipment at our own and new manufacturing facility in Yunfu and decorations for the new offices of our headquarters. We plan to fund our future capital expenditures with our existing cash balance.

Material Cash Requirements

Our material cash requirements as of December 31, 2022 and any subsequent interim period primarily include operating lease commitments, short-term bank loans, short-term debt, long-term bank loans, settlement payments, mandatorily redeemable non-controlling interests and investment obligations.

Our operating lease commitments primarily represent our non-cancelable lease of offices and facilities for business operation. We lease offices under non-cancelable operating lease arrangements with initial terms in excess of one year.

Our settlement payments represent our obligations under a settlement agreement that was entered into in connection with the settlement of an employment dispute. See "Item 8. Financial Information—Consolidated Statements and Other Financial Information—Legal Proceedings" for details.

Our mandatorily redeemable non-controlling interests primarily represent our obligations for the payment to the mandatorily redeemable non-controlling interest investment in a subsidiary.

We intend to fund our existing and future material cash requirements primarily with our existing cash balance and other financing alternatives. We will continue to make cash commitments, including capital expenditures, to support the growth of our business.

The following table sets forth our contractual obligations as of December 31, 2022:

	Payment Due by Period				
	Total	Less than 1 year	1-3 years	3-5 years	More than 5 years
	(in RMB thousands)				
Operating lease commitments	116,305	5,632	9,272	13,265	88,136
Short-term bank loans ⁽²⁾	51,016	51,016	—	—	—
Short-term debt ⁽¹⁾⁽²⁾	69,861	69,861	—	—	—
Long-term bank loans ⁽²⁾	17,381	13,371	3,237	773	—
Mandatorily redeemable non-controlling interests ⁽²⁾	41,496	600	40,896	—	—
Investment obligations	3,500	1,750	1,750	—	—
Total	299,559	142,230	55,155	14,038	88,136

Note:

- (1) In December 2022, we received interim funding from an investor who has subscribed for certain number of our Class A ordinary shares in a private placement. The funds amounted to US\$10 million in total and were made available for our use pending the closing of the private placement. We accounted for a significant portion of the funds as short-term debt and the remaining portion as warrants under additional paid-in capital. Upon closing of the private placement, we received US\$10 million as purchase price for our Class A ordinary shares and has repaid the interim funding in full as of the date of this annual report.
- (2) The short-term bank loans, short-term debt, long-term bank loans and mandatorily redeemable non-controlling interests are presented with the principle and estimated interest calculated based on the contractual interest rate.

As disclosed in our consolidated financial statements included elsewhere in this annual report, we had unrecognized tax benefits. The final outcome of the tax uncertainty is dependent upon various matters including tax examinations, interpretation of tax laws or expiration of statutes of limitation. However, due to the uncertainties associated with the status of examinations, including the protocols of finalizing audits by the relevant tax authorities, there is a high degree of uncertainty regarding the future cash outflows associated with these tax uncertainties.

Other than as shown above, we did not have any significant capital and other commitments, long-term obligations or guarantees as of December 31, 2022.

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 not reflected in our consolidated financial statements. Furthermore, we do not have any retained or contingent interest in assets transferred to an unconsolidated entity that serves as credit, liquidity or market risk support to such entity. We do not have any variable interest in any unconsolidated entity that provides financing, liquidity, market risk or credit support to us or engages in leasing, hedging or product development services with us.

Holding Company Structure

We are a holding company with no material operations on our own. We conduct our operations primarily through the WFOE, the VIE and their respective subsidiaries in China. As a result, our ability to pay dividends depends upon dividends paid by the WFOE. If the WFOE or any newly formed PRC subsidiaries incur debt on their own behalf in the future, the instruments governing their debt may restrict their ability to pay dividends to us. In addition, our wholly foreign-owned subsidiary in China 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. Under PRC law, each of the WFOE, the VIE and their respective subsidiaries in China is required to set aside at least 10% of its after-tax profits each year, if any, to contribute to certain statutory reserve funds until the cumulative amount of such reserve funds reaches 50% of its registered capital. As of December 31, 2022, the total registered capital of the WFOE, the VIE and their respective subsidiaries in China amounted to RMB1,192.2 million (US\$173.0 million), implying a maximum total amount of RMB596.1 million (US\$86.5 million) in statutory reserve funds to be set aside from their after-tax profits, if any. Our WFOE, the VIE and their respective subsidiaries in China had set aside a cumulative amount of RMB1.2 million (US\$0.2 million) for such statutory reserve funds as of December 31, 2022. We believe that setting aside such additional amount will not have a material adverse impact on our business or liquidity because (i) a company is not required to set aside any amount for its statutory reserve fund until it has positive after-tax profits; (ii) the amount to be set aside annually is only 10% of a company's after-tax profits, if any, and (iii) pursuant to the PRC Company Law, the statutory reserve funds can be used for offsetting a company's losses, expanding its business operations and increasing its capital. In addition, our wholly foreign-owned subsidiary in China may allocate a portion of its after-tax profits based on PRC accounting standards to enterprise expansion funds and staff bonus and welfare funds at its discretion, and the VIE may allocate a portion of its after-tax profits based on PRC accounting standards to a surplus fund at its discretion. The statutory reserve funds and the discretionary funds are not distributable as cash dividends. Remittance of dividends by a wholly foreign-owned company out of China is subject to examination by the banks designated by SAFE. Our WFOE has not paid dividends and will not be able to pay dividends until it generates accumulated profits and meets the requirements for statutory reserve funds.

Inflation

Since our inception, inflation in China has not materially affected our results of operations. According to the National Bureau of Statistics of China, the year-over-year percent changes in the consumer price index for December 2020, 2021 and 2022 were increases of 0.2%, 1.5% and 1.8%, respectively. Although we have not been materially affected by inflation in the past, we can provide no assurance that we will not be affected in the future by higher rates of inflation in mainland China. For example, certain operating costs and expenses, such as employee compensation and office operating expenses may increase as a result of higher inflation. We are not able to hedge our exposure to higher inflation in mainland China.

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

See “Item 4. Information on the Company—B. Business Overview—Research and Development Capabilities” and “—Intellectual Property.”

D. Trend Information.

Other than as described elsewhere in this annual report, we are not aware of any trends, uncertainties, demands, commitments or events that are reasonably likely to have a material adverse effect on our revenue, income from continuing operations, profitability, liquidity or capital resources, or that would cause our reported financial information not necessarily to be indicative of future operating results or financial condition.

E. Critical Accounting Estimates

Our consolidated financial statements have been prepared in accordance with U.S. GAAP, which requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities, revenues and expenses, and related disclosures of contingent liabilities in the consolidated financial statements and accompanying notes. We base our estimates on historical experience and on various other assumptions we believe to be reasonable under the circumstances, the results of which form the basis for making judgments about the carrying values of assets and liabilities. Changes in the economic environment, financial markets, and any other parameters used in determining such estimates could cause actual results to differ. Our critical accounting estimates are described below. The critical accounting estimates should be read in conjunction with our risk factors as disclosed in “Item 3. Key Information—D. Risk Factors.” See Note 2 to our consolidated financial statements for the year ended December 31, 2022 for more information on our critical accounting policies.

Allowance for doubtful accounts

We make estimates of allowance for doubtful accounts receivable based upon assessment of various factors, including specific evidence indicating troubled collection, historical experience, accounts aging and other factors that may affect its ability to collect from the customers. Losses on allowance for doubtful accounts are recorded as general and administrative expenses on the consolidated statements of comprehensive income.

We apply management’s judgments and estimates when determining the allowance for doubtful accounts to be recognized. We reassess the allowance at each balance sheet date. Where the basis of judgments and estimates is different from the initial assessment, such differences will impact the allowance for doubtful accounts and the carrying values of the accounts receivable in the year. As of December 31, 2021 and 2022, we assessed the ending balance of allowance for doubtful accounts to be RMB69.4 million and RMB115.4 million (US\$16.7 million), respectively. The significant increase was based on our assessment as of December 31, 2022, with our judgments and estimates that the impacts from the continuous COVID-19 epidemic and control measures in China adversely affected the business of customers and the ability to collect from the customers. Changes in these estimates and assumptions could materially affect the allowance losses.

Valuation allowance for deferred tax assets

We record a valuation allowance to offset deferred tax assets if based on the weight of available evidence, it is more-likely-than-not that some portion, or all, of the deferred tax assets will not be realized. Significant judgment is required in determining the valuation allowance. In assessing the need for a valuation allowance, we consider all sources of taxable income, including projected future taxable income, reversing taxable temporary differences and ongoing tax planning strategies. If it is determined that we are able to realize deferred tax assets in excess of the net carrying value or to the extent we are unable to realize a deferred tax asset, we would adjust the valuation allowance in the period in which such a determination is made, with a corresponding increase or decrease to earnings.

Fair value of warrants and short-term debt

We allocate the proceeds from the sale of a debt instrument with stock purchase to the two elements based on the relative fair values of the debt instrument without the warrants and of the warrants themselves at time of issuance. The relative fair value of the short-term debt is recorded using the discount method of the future payables. The relative fair value of the warrants is estimated based on the difference of the fair value between the present value of the purchase price and market price of the signing date of the share purchase agreement. The expected payment date, the discount rate and the present value of the purchase price rely on our judgement.

Item 6. Directors, Senior Management and Employees

A. Directors and senior management.

The following table sets forth certain information relating to our directors and executive officers as of the date of this annual report.

Directors and Executive Officers	Age	Position/Title
Huazhi Hu	46	Chairman and Chief Executive Officer
Haoxiang Hou	34	Independent Director
Conor Chia-hung Yang	60	Independent Director
Dongming Wu	59	Independent Director
Nick Ning Yang	47	Independent Director
Richard Jian Liu	48	Chief Financial Officer
Xin Fang	48	Chief Operating Officer

Mr. Huazhi Hu is our founder and has served as our chief executive officer and the chairman of the board of directors since our inception. Mr. Hu founded our predecessor company, Beijing Yihang Chuangshi Technology Co., Ltd. in 2005, a leader in providing large-scale command-and-control systems. Mr. Hu also worked as the chief technology officer at Beijing 999 Emergency Rescue Center in charge of the development of the emergency command & control center between 2008 and 2010, and worked at Beijing Jindian Group as a vice president overseeing information management between 2006 and 2008. Mr. Hu is a recipient of the Technology Innovation Award presented at the Living Legends of Aviation event in 2019. Mr. Hu attended Tsinghua University where he studied computer science between 1992 and 1997.

Mr. Haoxiang Hou has served as our director since August 2015. Mr. Hou has served as a senior partner, managing director and member of the investment committee of GP Lingang Hi-tech Fund since January 2017, where he plays a key role in fundraising and investment in new energy and new material sectors. Prior to that, he served as a vice president of investment at GP TMT Fund from 2015 to 2016. Mr. Hou was named on the list of “China Top 30 Venture Capitalists Under the Age of 30 in 2018” by Forbes. Mr. Hou received his bachelor’s degree in information security and international finance and his master’s degree in business administration from Shanghai Jiao Tong University in 2011 and 2015, respectively.

Mr. Conor Chia-hung Yang has served as our director since December 2019. Mr. Yang is the chief financial officer of Sunrate Holdings Limited since February 2023. Mr. Yang was a co-founder and president of Black Fish Group Limited from 2017 to 2021. From 2007 to 2017, Mr. Yang served in several chief financial officer positions at US-listed companies including Tuniu Corporation (Nasdaq: TOUR), E-Commerce China Dangdang Inc., and AirMedia Group Inc. Mr. Yang was the chief executive officer of Rock Mobile Corporation from 2004 to 2007, and the chief financial officer of the Asia Pacific region for CellStar Asia Corporation from 1999 to 2004. Prior to that, Mr. Yang was a senior banker at Goldman Sachs (Asia) L.L.C., Lehman Brothers Asia Limited and Morgan Stanley Asia Limited from 1992 to 1999. Mr. Yang currently also serves as an independent director of EHang Holdings Limited (Nasdaq: EH), I-Mab (Nasdaq: IMAB), iQIYI, Inc. (Nasdaq: IQ), Tongcheng Travel Holdings Limited (HKSE: 0780) and UP Fintech Holding Ltd (Nasdaq: TIGR). Mr. Yang received his master's degree in business administration from the University of California, Los Angeles.

Mr. Dongming Wu has served as our director since June 2020. Mr. Wu has served as a Managing Director of DHL-Sinotrans since May 2003. He also currently serves as the Chief Executive Officer of DHL Express China and a Global Management Board Member of DHL Express. DHL-Sinotrans, a leading international express company in China, is a joint venture between the global delivery and logistics giant DHL and Sinotrans. Mr. Wu has over 30 years of experience in the global delivery and logistics industry. He started his career at Sinotrans in July 1986, where he held various senior management positions and most recently served as the chairman of its supervisory board through March 2017. Mr. Dongming Wu received his bachelor's degree in economics from Beijing International Studies University and his EMBA degree from the BiMBA Business School of the National School of Development at Peking University.

Mr. Nick Ning Yang has served as our director since December 2022. Mr. Yang has served as a founding partner of LeBox Capital, a venture investment fund that focuses on early-stage high growth TMT companies in China, since October 2011. Prior to that, Mr. Yang was a co-founder of KongZhong Corporation, a company focusing on wireless value-added services and listed on Nasdaq in July 2004, and served as Chief Technology Officer from 2002 to 2008. Mr. Yang had also held the position of Vice President of Technology at Nasdaq-listed Sohu from 2000 to 2001. From 1999 to 2000, Mr. Yang served as Chief Technology Officer of ChinaRen.com, a company he co-founded. Mr. Yang received a bachelor's degree in electrical engineering from the University of Michigan in 1997 and a master's degree in electrical engineering from the Stanford University in 1999.

Mr. Richard Jian Liu has served as our chief financial officer since May 2017. Mr. Liu joined our company as a vice president of finance in August 2015. Prior to joining us, Mr. Liu served as group vice president of finance and chief financial officer of the New Business Group at 21Vianet Group, Inc. (Nasdaq: VNET) from May 2014 to August 2015. From March 2008 to May 2014, he also served as the chief financial officer at several industry-leading companies, including Ecoplast Technologies Inc., China Polypeptide Group, Inc. and China Energy Recovery, Inc. Prior to that, he worked as a senior consultant at Arthur Andersen LLP, a public accounting firm, in its China offices between 1996 to 2000. Mr. Liu received his bachelor's degree in engineering from Shanghai Jiao Tong University in 1996 and his master's degree in business administration from the Anderson Graduate School of Management at the University of California, Los Angeles in 2003. Mr. Liu is a member of Chinese Institute of Certified Public Accountants.

Mr. Xin Fang has served as our chief operating officer since February 2022. Prior to joining us, Mr. Fang served as the Chairman of the Board of Directors of Wuning Xinyihang Investment Development Co., Ltd. Mr. Fang is a seasoned business leader with more than 20 years of business administration and operational experience. He has a track record of success in the fields of sales of IT product and system integration solutions, tourism operation and management, tourism real estate development, etc. Mr. Fang obtained his master's degree in business administration from Nanchang University in 2013.

B. Compensation.

Compensation of Directors and Executive Officers

For the fiscal year ended December 31, 2022, we paid an aggregate of approximately RMB3.7 million (US\$0.5 million) in cash to our directors and executive officers. We are not required under Cayman Islands law to disclose, and we have not otherwise disclosed, the compensation of our directors and executive officers on an individual basis. We have not set aside or accrued any amount to provide pension, retirement or other similar benefits to our directors and executive officers. Our PRC subsidiaries and VIE are required by law to make contributions equal to certain percentages of each employee's salary for his or her pension insurance, medical insurance, unemployment insurance and other statutory benefits and a housing provident fund.

Employment Agreements and Indemnification Agreements

We have entered into employment agreements with each of our executive officers. We may terminate employment for cause, at any time, without advance notice or remuneration, for certain acts of the executive officer, such as conviction or plea of guilty to a felony or any crime involving moral turpitude, negligent or dishonest acts to our detriment, or misconduct or a failure to perform agreed duties. In such case of termination by us, we will provide severance payments to the executive officer as expressly required by applicable law of the jurisdiction where the executive officer is based. The executive officer may resign at any time with a 30 days' advance written notice.

Each executive officer has agreed to hold, both during and after the termination or expiry of his or her employment agreement, in strict confidence and not to use, except as required in the performance of his or her duties in connection with the employment or pursuant to applicable law, any of our confidential information or trade secrets, any confidential information or trade secrets of our clients or prospective clients, or the confidential or proprietary information of any third party received by us and for which we have confidential obligations. The executive officers have also agreed to disclose in confidence to us all inventions, designs and trade secrets which they conceive, develop or reduce to practice during the executive officer's employment with us and to assign all right, title and interest in them to us, and assist us in obtaining and enforcing patents, copyrights and other legal rights for these inventions, designs and trade secrets. In addition, each executive officer has agreed to be bound by non-competition and non-solicitation restrictions during the term of his or her employment and typically for one year following the last date of employment.

We have also entered into indemnification agreements with each of our directors and executive officers. Under these agreements, we agree to indemnify our directors and executive officers against certain liabilities and expenses incurred by such persons in connection with claims made by reason of their being a director or officer of our company.

2015 Share Incentive Plan

Our board of directors approved the 2015 Share Incentive Plan, or the 2015 Plan, to attract and retain the best available personnel, provide additional incentives to employees, directors and consultants, and promote the success of our business. The maximum aggregate number of ordinary shares that may be issued under the 2015 Plan pursuant to all awards under the 2015 Plan is 8,867,053 ordinary shares and can be increased up to a number that is equal to 15% of the then total outstanding shares on a fully diluted basis at the discretion of our board of directors. As of March 31, 2023, 119,500 restricted share units and 53,737 share options were outstanding under the 2015 Plan, excluding awards that were forfeited or cancelled after the relevant grant dates.

The following paragraphs describe the principal terms of the 2015 Plan.

Types of Awards. The 2015 Plan permits the awards of options, restricted shares and restricted share units.

Plan Administration. Our board of directors or a committee of one or more members of the board of directors will administer the 2015 Plan. The committee or the full board of directors, as applicable, will determine the participants to receive awards, the type and number of awards to be granted to each participant, and the terms and conditions of each award grant.

Award Agreement. Awards granted under the 2015 Plan are evidenced by an award agreement that sets forth the terms, conditions and limitations for each award which may include the term of an award, the provisions applicable in the event the grantee's employment or service terminates, and our authority to unilaterally or bilaterally amend, modify, suspend, cancel or rescind an award.

Eligibility. We may grant awards to our employees, consultants and directors, as determined by our board of directors or a committee of one or more members of the board of directors.

Vesting Schedule. In general, the plan administrator determines the vesting schedule, which is specified in the relevant award agreement.

Transfer Restrictions. Awards may not be transferred in any manner by the participant other than in accordance with the exceptions provided in the 2015 Plan or the relevant award agreement or otherwise determined by the plan administrator, such as transfers by will or the laws of descent and distribution.

Termination and Amendment of the 2015 Plan. Unless terminated earlier, the 2015 Plan has a term of ten years. With the approval of our board of directors, the plan administrator has the authority to terminate, amend or modify the 2015 Plan. However, without the prior written consent of the participant, no such action may adversely affect in any material way any award previously granted pursuant to the 2015 Plan.

2019 Share Incentive Plan

Our board of directors approved the 2019 Share Incentive Plan, or the 2019 Plan, to attract and retain the best available personnel, provide additional incentives to employees, directors and consultants, and promote the success of our business. The 2019 Plan became effective upon the completion of the Company's initial public offering in 2019. The maximum aggregate number of ordinary shares that may be issued under the 2019 Plan is initially 5,455,346, which may be increased by up to 15% of the then total outstanding shares on a fully diluted basis at the discretion of our board of directors. As of the date of this annual report, the maximum aggregate number of ordinary shares that may be issued under the 2019 Plan is 8,266,949. As of March 31, 2023, 2,759,250 restricted share units were outstanding under the 2019 Plan, excluding awards that were forfeited or cancelled after the relevant grant dates.

The following paragraphs describe the principal terms of the 2019 Plan.

Types of Awards. The 2019 Plan permits the awards of options, restricted shares and restricted share units.

Plan Administration. Our board of directors or a committee of one or more members of the board of directors will administer the 2019 Plan. The committee or the full board of directors, as applicable, will determine the participants to receive awards, the type and number of awards to be granted to each participant, and the terms and conditions of each award grant.

Award Agreement. Awards granted under the 2019 Plan are evidenced by an award agreement that sets forth the terms, conditions and limitations for each award which may include the term of an award, the provisions applicable in the event the grantee's employment or service terminates, and our authority to unilaterally or bilaterally amend, modify, suspend, cancel or rescind an award.

Eligibility. We may grant awards to our employees, consultants and directors, as determined by our board of directors or a committee of one or more members of the board of directors.

Vesting Schedule. In general, the plan administrator determines the vesting schedule, which is specified in the relevant award agreement.

Transfer Restrictions. Awards may not be transferred in any manner by the participant other than in accordance with the exceptions provided in the 2019 Plan or the relevant award agreement or otherwise determined by the plan administrator, such as transfers by will or the laws of descent and distribution.

Termination and Amendment of the 2019 Plan. Unless terminated earlier, the 2019 Plan has a term of ten years. With the approval of our board of directors, the plan administrator has the authority to terminate, amend or modify the 2019 Plan. However, without the prior written consent of the participant, no such action may adversely affect in any material way any award previously granted pursuant to the 2019 Plan.

The following table summarizes, as of March 31, 2023, the number of Class A ordinary shares under outstanding options, restricted share units and other equity awards that we granted to our directors and executive officers, excluding awards that were settled, forfeited or cancelled after the relevant grant dates.

Name	Class A Ordinary Shares underlying Equity Awards	Date of Grant	Date of Expiration
Huazhi Hu	*	January 4, 2021	January 3, 2031
		December 16, 2019	December 15, 2029
Conor Chia-hung Yang	*	January 4, 2021	January 3, 2031
		June 1, 2020	May 31, 2030
Dongming Wu	*	January 4, 2021	January 3, 2031
Haoxiang Hou	*	January 4, 2021	January 3, 2031
Richard Jian Liu	*	January 4, 2021	January 3, 2031
Nick Ning Yang	*	March 27, 2023	March 26, 2033
All directors and officers as a group	2,303,737	Various dates from December 16, 2019 to January 4, 2021	Various dates from December 15, 2029 to January 3, 2031

* Less than 1% of our total outstanding ordinary shares on an as-converted basis.

As of March 31, 2023, our employees other than members of our senior management as a group held 1,983,750 restricted share units.

C. Board Practices.

Board of Directors

Our board of directors consists of five directors. A director is not required to hold any shares in our company by way of qualification. A director may vote with respect to any contract or transaction, or proposed contract or transaction in which he or she is, whether directly or indirectly, interested, provided that (a) such director has declared the nature of his or her interest at the earliest meeting of the board at which it is practicable for him or her to do so, either specifically or by way of a general notice, and (b) if such contract or transaction, or proposed contract or transaction is a transaction with a related party, such transaction has been approved by the audit committee in accordance with the Nasdaq rules. The directors may exercise all the powers of the company to borrow money, mortgage or charge its undertaking, property and assets (present or future) and uncalled capital or any part thereof, and issue debentures, debenture stock, bonds or other securities whether outright or as collateral security for any obligation of the company or of any third party. None of our non-executive directors has a service contract with us that provides for benefits upon termination of service.

Committees of the Board of Directors

A company of which more than 50% of the voting power is held by a single entity is considered a “controlled company” under the Nasdaq Stock Market Rules. A controlled company is not required to comply with the Nasdaq corporate governance rules requiring a board of directors to have a majority of independent directors, to have an independent compensation committee, and to have an independent nominating and corporate governance committee. We are a “controlled company” as defined under the Nasdaq Stock Market Rules, but we have no current intention to rely on the controlled company exemption.

We have established three committees under the board of directors: an audit committee, a compensation committee and a nominating and corporate governance committee. We have adopted a charter for each of the three committees. Each committee’s members and functions are described below.

Audit Committee. Our audit committee consists of Conor Chia-hung Yang, Dongming Wu and Haoxiang Hou. Conor Chia-hung Yang is the chairman of our audit committee. We have determined that each of Conor Chia-hung Yang, Dongming Wu and Haoxiang Hou satisfies the “independence” requirements of Rule 5605(c)(2) of the Listing Rules of the Nasdaq Stock Market and Rule 10A-3 under the Exchange Act, as amended. We have determined that Conor Chia-hung Yang qualifies as an “audit committee financial expert.” 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:

- appointing the independent auditors and pre-approving all auditing and non-auditing services permitted to be performed by the independent auditors;
- reviewing with the independent auditors any audit problems or difficulties and management’s response;
- discussing the annual audited financial statements with management and the independent auditors;
- reviewing the adequacy and effectiveness of our accounting and internal control policies and procedures and any steps taken to monitor and control major financial risk exposures;
- reviewing and approving all proposed related party transactions;
- meeting separately and periodically with management and the independent auditors; and
- monitoring compliance with our code of business conduct and ethics, including reviewing the adequacy and effectiveness of our procedures to ensure proper compliance.

Compensation Committee. Our compensation committee consists of Haoxiang Hou and Conor Chia-hung Yang. Haoxiang Hou is the chairman of our compensation committee. We have determined that each of Haoxiang Hou and Conor Chia-hung Yang satisfies the “independence” requirements of Rule 5605(c)(2) of the Listing Rules of the Nasdaq Stock Market. The compensation committee assists the board in reviewing and approving the compensation structure, including all forms of compensation, relating to our directors and executive officers. Our chief executive officer may not be present at any committee meeting during which his compensation is deliberated. The compensation committee is responsible for, among other things:

- reviewing and approving, or recommending to the board for its approval, the compensation for our chief executive officer and other executive officers;
- reviewing and recommending to the board for determination with respect to the compensation of our non-employee directors;
- reviewing periodically and approving any incentive compensation or equity plans, programs or similar arrangements; and

- selecting compensation consultant, legal counsel or other adviser only after taking into consideration all factors relevant to that person's independence from management.

Nominating and Corporate Governance Committee. Our nominating and corporate governance committee consists of Huazhi Hu and Haoxiang Hou. Huazhi Hu is the chairperson of our nominating and corporate governance committee. We have determined that Haoxiang Hou satisfies the "independence" requirements of Rule 5605(c)(2) of the Listing Rules of the Nasdaq Stock Market. The nominating and corporate governance committee assists the board of directors in selecting individuals qualified to become our directors and in determining the composition of the board and its committees. The nominating and corporate governance committee is responsible for, among other things:

- selecting and recommending to the board nominees for election by the shareholders or appointment by the board;
- reviewing annually with the board the current composition of the board with regards to characteristics such as independence, knowledge, skills, experience and diversity;
- making recommendations on the frequency and structure of board meetings and monitoring the functioning of the committees of the board; and
- advising the board periodically with regards to significant developments in the law and practice of corporate governance as well as our compliance with applicable laws and regulations, and making recommendations to the board on all matters of corporate governance and on any remedial action to be taken.

Duties of Directors

Under Cayman Islands law, our directors owe fiduciary duties to our company, including a duty of loyalty, a duty to act honestly, and a duty to act in what they consider in good faith to be in our best interests. Our directors must also exercise their powers only for a proper purpose. Our directors also owe to our company a duty to exercise skills they actually possess and such care and diligence that a reasonably prudent person would exercise in comparable circumstances. It was previously considered that a director need not exhibit in the performance of his duties a greater degree of skill than may reasonably be expected from a person of his knowledge and experience. However, English and Commonwealth Courts have moved toward an objective standard with regards to the registered skill and care and these authorized are likely to be followed in the Cayman Islands. 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. Our company has the right to seek damages if a duty owed by our directors is breached. In certain limited exceptional circumstances, a shareholder may have the right to seek damages in our name if a duty owed by our directors is breached.

Our board of directors has all the powers necessary for managing, and for directing and supervising, our business affairs. The functions and powers of our board of directors include, among others:

- convening shareholders' annual and extraordinary general meetings and reporting its work to shareholders at such meetings;
- declaring dividends and distributions;
- appointing officers and determining the term of office of the officers;
- exercising the borrowing powers of our company and mortgaging the property of our company; and
- approving the transfer of shares in our company, including the registration of such shares in our share register.

Terms of Directors and Officers

Our directors may be elected by a resolution of our board of directors or by an ordinary resolution of our shareholders. Unless otherwise determined by our company in general meeting, our company shall have not less than three (3) directors, and there shall be no maximum number of directors. An appointment of a director may be on terms that the director shall automatically retire from office (unless he has sooner vacated office) at the next or a subsequent annual general meeting or upon any specified event or after any specified period in a written agreement between our company and the director, if any; but no such term shall be implied in the absence of express provision. Each director whose term of office expires shall be eligible for re-election at a meeting of the Shareholders or re-appointment by our board of directors. Our directors may be removed from office by ordinary resolution of the shareholders. In addition, a director's office will be vacated if the director (i) becomes bankrupt or makes any arrangement or composition with his creditors; (ii) dies or is found by our company to be or becomes of unsound mind; (iii) resigns his office by notice in writing to us; (iv) without special leave of absence from our board, is absent from three consecutive board meetings and our board of directors resolves that his office be vacated; or (v) is removed from office pursuant to any other provisions of our memorandum and articles of association.

Our officers are elected by and serve at the discretion of the board of directors.

Board Diversity Disclosure

Board Diversity

Board Diversity Matrix (As of March 31, 2023)				
Country of Principal Executive Offices:	People's Republic of China			
Foreign Private Issuer	Yes			
Disclosure Prohibited Under Home Country Law	No			
Total Number of Directors	5			
	Female	Male	Non-Binary	Did Not Disclose Gender
Part I: Gender Identity				
Directors	0	5	0	0
Part II: Demographic Background				
Underrepresented Individual in Home Country Jurisdiction			0	
LGBTQ+			0	

Disclosure Pursuant to Rule 5605(f)(3) of the Nasdaq Listing Rules

Rule 5605(f)(2)(B) of the Nasdaq Listing Rules requires us to have, or to explain why we do not have, at least two members of our Board of Directors who are "Diverse" directors, at least one of whom self-identifies as "Female," subject to transition periods specified by Rule 5605(f)(7) of the Nasdaq Listing Rules. For purposes of Rule 5605(f)(2)(B), the term "Diverse" means an individual who self-identifies as one or more of Female, LGBTQ+, or an underrepresented individual based on national, racial, ethnic, indigenous, cultural, religious or linguistic identity in the country of our principal executive offices; and the term "Female" means an individual who self-identifies her gender as a woman, without regard to the individual's designated sex at birth.

Rule 5605(f)(7) of the Nasdaq Listing Rules requires us to have, or explain why we do not have, (i) by December 31, 2023, at least one Diverse director and (ii) by December 31, 2025, at least two Diverse directors, at least one of whom self-identifies as Female.

As of the date of this annual report, our Board of Directors has determined that we will satisfy the requirements of Rule 5605(f)(2)(B) of the Nasdaq Listing Rules by explaining why we will not have any Diverse directors by either December 31, 2023 or December 31, 2025.

We acknowledge and support the general principles behind the diversity objectives set forth in Rule 5606(f)(2)(B) of the Nasdaq Listing Rules. However, the company's Board of Directors does not believe achieving Nasdaq's diversity objectives are feasible given the company's current circumstances. We believe that the current composition of our Board of Directors, is suitable for the current scale of and goals for our business and operations. Most members of our Board of Directors have served as our directors for a number of years and all incumbent directors are familiar with our company's history and business operations; provide us with a variety of personal, professional and industry backgrounds, with appropriate experience and skill sets. We intend to continually assess our industry and the status of our business and may decide in the future, should future circumstances make it appropriate, to seek to meet the diversity objectives contemplated by Rule 5606(f)(2)(B) of the Nasdaq Listing Rules.

D. Employees.

We had 227, 326 and 341 employees as of December 31, 2020, 2021 and 2022, respectively. As of December 31, 2022, we had 315 employees in Guangzhou, 14 employees in Yunfu, 2 employees in Beijing and 10 employees outside China. The following table sets forth the number of our employees categorized by function as of December 31, 2022:

Function	Number	% of Total Employees
Research and product development department	190	55.7%
Marketing and sales department	62	18.2%
General administration department	89	26.1%
Total number of employees	341	100%

We also had 68, 113 and 115 full-time contractors who are involved in the manufacturing of our AAVs as of December 31, 2020, 2021 and 2022, respectively.

As required by laws and regulations in China, we participate in various employee social security plans that are organized by municipal and provincial governments, including housing, pension, medical insurance and unemployment insurance. We are required under PRC law to make contributions to an employee benefit plan at a specified percentage of the salaries, bonuses and certain allowances of our employees, up to a maximum amount specified by the local government from time to time. See "Item 3. Key Information—D. Risk Factors—Risks Relating to Doing Business in China—Increases in labor costs and enforcement of stricter labor laws and regulations in the PRC may adversely affect our business and our profitability."

We typically enter into standard employment and confidentiality agreements with our key employees. In addition, we enter into confidentiality and non-compete agreements with senior management and intellectual property assignment agreements with core technical personnel.

Our success depends on our ability to attract, retain and motivate qualified employees that share our values and vision. We believe that we maintain a good working relationship with our employees.

E. Share Ownership.

Except as specifically noted, the following table sets forth information with respect to the beneficial ownership of our ordinary shares as of March 31, 2023 by:

- each of our directors and executive officers; and

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- each person known to us to beneficially own more than 5% of our ordinary shares on an as-converted basis.

The calculations in the table below are based on 81,758,341 Class A ordinary shares (excluding Class A ordinary shares issued to the depositary bank for bulk issuance of ADSs reserved for future issuances upon the exercise or vesting of awards granted under our share incentive plans) and 39,026,560 Class B ordinary shares outstanding as of March 31, 2023.

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 after March 31, 2023, including through the exercise of any restricted share unit, option, warrant or other right or the conversion of any other security. These shares, however, are not included in the computation of the percentage ownership of any other person.

	Class A Ordinary Shares	Class B Ordinary Shares	Total Ordinary Shares on an as- Converted Basis	% of Beneficial Ownership	% of Aggregate Voting Power***
Directors and Executive Officers:**					
Huazhi Hu ⁽¹⁾	670,258	39,026,560	39,696,818	32.9%	82.8%
Haoxiang Hou ⁽²⁾	*	—	*	*	*
Conor Chia-Hung Yang ⁽³⁾	*	—	*	*	*
Dongming Wu ⁽⁴⁾	*	—	*	*	*
Nick Ning Yang	—	—	—	—	—
Richard Jian Liu ⁽⁵⁾	1,762,500	—	1,762,500	1.5%	0.4%
Xin Fang	—	—	—	—	—
All Directors and Executive Officers as a Group	2,583,995	39,026,560	41,610,555	34.4%	83.2%
Principal Shareholder:					
Genesis Rising Limited ⁽⁶⁾	—	39,026,560	39,026,560	32.3%	82.7%

Notes:

* Less than 1% of our total outstanding shares.

** Messrs. Huazhi Hu, Richard Jian Liu, and Xin Fang's business address is 11/F Building One, EHang Technology Park, No. 29 Bishan Blvd., Huangpu District, Guangzhou, Guangdong Province, 510700, PRC. Mr. Haoxiang Hou's business address is No. 151 Mao Jia Yuan Rd, Huangpu District, Shanghai, PRC. Mr. Conor Chia-Hung Yang's business address is Unit EF, 12th Floor, Lujiazui Finance Plaza, No. 1217 Dongfang Road, Pudong District, Shanghai, PRC. Mr. Dongming Wu's business address is No. 18 Rong Hua South Road, Beijing Economic-Technological Development Area, Daxing District, Beijing, PRC. Mr. Nick Ning Yang's business address is No.107 AI Technology Park, No. 27 Xidawang Road, Chaoyang District, Beijing, PRC.

*** For each person and group included in this column, percentage of voting power is calculated by dividing the voting power beneficially owned by such person or group by the voting power of all of our outstanding Class A and Class B ordinary shares as a single class. Each holder of Class B ordinary shares is entitled to ten votes per share, and while each holder of our Class A ordinary shares is entitled to one vote per share on all matters submitted to them for a vote. Our Class A ordinary shares and Class B ordinary shares vote together as a single class on all matters submitted to a vote of our shareholders. Our Class B ordinary shares are convertible at any time by the holders thereof into Class A ordinary shares on a one-for-one basis.

(1) Represents (i) 39,026,560 Class B ordinary shares held by Genesis Rising Limited, a British Virgin Islands company that is wholly owned by Mr. Huazhi Hu, and (ii) 670,258 Class A ordinary shares represented by 335,129 ADSs held by Mr. Huazhi Hu. The registered address of Genesis Rising Limited is Start Chambers, Wickham's Cay II, P.O. Box 2221, Road Town, Tortola, British Virgin Islands.

- (2) Represents Class A ordinary shares beneficially owned by Mr. Haoxiang Hou.
- (3) Represents Class A ordinary shares beneficially owned by Mr. Conor Chia-Hung Yang.
- (4) Represents Class A Ordinary Shares beneficially owned by Mr. Dongming Wu, including Class A ordinary shares underlying share options and restricted share units held by Mr. Dongming Wu that have vested as of March 31, 2023 or will vest within 60 days after March 31, 2023.
- (5) Represents 1,762,500 Class A ordinary shares beneficially owned by JM Elegance Holdings Limited, a British Virgin Island company that is wholly owned by Mr. Richard Jian Liu. The registered address of JM Elegance Holdings Limited is Drake Chambers, P.O. Box 3321, Road Town, Tortola, British Virgin Islands.
- (6) Represents 39,026,560 Class B ordinary shares held by Genesis Rising Limited, a British Virgin Islands company that is wholly owned by Mr. Huazhi Hu. The registered address of Genesis Rising Limited is Start Chambers, Wickham's Cay II, P.O. Box 2221, Road Town, Tortola, British Virgin Islands.

To our knowledge, as of March 31, 2023, 82,266,591 of our Class A ordinary shares were held by six record holders in the United States, including a total of 508,250 Class A ordinary shares held by The Bank of New York Mellon, the depository of the ADS program. None of our outstanding Class B ordinary shares are held by record holders in the United States. The number of beneficial owners of the 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.

To our knowledge, except as disclosed above, we are not owned or controlled, directly or indirectly, by another corporation, by any foreign government or by any other natural or legal person or persons, severally or jointly. We are not aware of any arrangement that may, at a subsequent date, result in a change of control of our company.

F. Disclosure of a Registrant's Action to Recover Erroneously Awarded Compensation.

Not applicable.

Item 7. Major Shareholders and Related Party Transaction

A. Major Shareholders.

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

B. Related Party Transactions.

Contractual Arrangements with the VIE and its Shareholders

Please refer to "Item 4. Information on the Company—C. Organizational Structure" for a detail description of the contractual arrangements among the WFOE, the VIE and the VIE's shareholders.

In October 2020, the VIE paid a guarantee deposit of RMB2.6 million (US\$0.4 million) to a court in Guangzhou, China to lift a judicial freeze on certain equity interests of the VIE, which were then nominally held under the name of our founder and director, Mr. Huazhi Hu. The judicial freeze was placed in connection with an arbitration in which Mr. Hu was named as a party. As of December 31, 2021, the judicial freeze had been lifted and the VIE has collected the deposit.

Transactions with Related Parties

In 2022, there was no transaction with related parties. As of December 31, 2021, we had amount due from a related party of RMB1.4 million (US\$0.2 million). The amount represented receivables relating to sale of autonomous aerial vehicles owed by Guangzhou Yitong Zhihang Technology Co., Ltd., an equity investee over whom we have significant influence. As of December 31, 2022, we had no amount due from related parties.

Shareholders Agreement and Registration Rights

Shareholders Agreement

We entered into our second amended and restated shareholders agreement on December 27, 2016 with our shareholders, which consisted of holders of ordinary shares and preferred shares.

The shareholders agreement and right of first refusal and co-sale agreement provide for certain special rights, including right of first refusal, co-sale rights, preemptive rights and contain provisions governing our board of directors and other corporate governance matters. Those special rights, as well as the corporate governance provisions, automatically terminated upon the completion of our initial public offering.

Registration Rights

Pursuant to our second amended and restated shareholders agreement dated December 27, 2016, we have granted certain registration rights to our shareholders. Set forth below is a description of the registration rights granted under the agreement.

Demand Registration Rights. At any time after the earlier of (i) the third (3rd) anniversary of the date of the agreement or (ii) six (6) months following the effectiveness of a registration statement for a qualified initial public offering, holders of at least twenty-five percent (25%) of the registrable securities then outstanding have the right to demand that we file a registration statement covering all registrable securities that the holders request to be registered and included in such registration by written notice. Other than as required by the underwriters in connection with our initial public offering, at least fifty percent (50%) of the registrable securities requested by the holders to be included in such underwriting and registration shall be so included. We have the right to defer filing a registration statement for a period of not more than 90 days after the receipt of the request of the initiating holders if the board of directors determines in its good faith judgment that it would be materially detrimental to us and our shareholders for such registration statement to be filed at such time. We are not obligated to effect more than two demand registrations. We are obligated to effect no more than one (1) demand registrations, other than demand registration to be effected pursuant to registration statements on Form F-3, for which an unlimited number of demand registrations shall be permitted.

Registration on Form F-3 or Form S-3. Any holder is entitled to request us to file a registration statement on Form F-3 or Form S-3 if we qualify for registration on Form F-3 or Form S-3. The holders are entitled to an unlimited number of registrations on Form F-3 or Form S-3. We shall effect the registration of the securities on Form F-3 as soon as practicable, except in certain circumstances.

Piggyback Registration Rights. If we propose to file a registration statement for a public offering of our securities, we must offer shareholders an opportunity to include in the registration all or any part of the registrable securities held by such holders. If the managing underwriter(s) of any underwritten offering determine(s) in good faith that marketing factors require a limitation of the number of shares to be underwritten, then the number of shares that may be included in the registration and the underwriting shall be allocated (i) first, to us, (ii) second, to each of the holders requesting inclusion of their registrable securities in such registration statement on a pro rata basis based on the total number of shares of registrable securities then held by each such holder, and (iii) third, to other holders of our securities.

Expenses of Registration. We will bear all registration expenses, other than underwriting discounts and selling commissions.

Termination of Registration Rights. Our shareholders' registration rights will terminate upon the earlier of (i) the fifth (5th) anniversary of a qualified initial public offering, (ii) as to any shareholder when the shareholder together with its affiliates can sell all of its shares subject to registration rights in reliance on Rule 144 without transfer restrictions, and (iii) after the consummation of any liquidation, dissolution or winding up of us.

Employment Agreements and Indemnification Agreements

Please refer to “Item 6. Directors, Senior Management and Employees—B. Compensation—Employment Agreements and Indemnification Agreements.”

Share Incentive Plans

Please refer to “Item 6. Directors, Senior Management and Employees—B. Compensation—2015 Share Incentive Plan” and “Item 6. Directors, Senior Management and Employees—B. Compensation—2019 Share Incentive Plan.”

C. Interests of Experts and Counsel.

Not applicable.

Item 8. Financial Information

A. Consolidated Statements and Other Financial Information.

Please refer to Item 18 “Financial Statements” for our audited consolidated financial statements filed as part of this annual report.

Legal Proceedings

From time to time, we may be involved in disputes and legal or administrative proceedings in the ordinary course of our business, including actions with respect to breach of contract, labor and employment claims, copyright, trademark, patent infringement, bankruptcy and other matters. Other than as described in this annual report, we are not a party to any material ongoing legal or administrative proceedings which may have significant effects on our financial position, results of operations or cash flows.

Between February 17 and 26, 2021, three federal securities class action lawsuits (captioned *Amberber v. EHang Holdings Limited, et al.*, Case No. 1:21-cv-01392-GBD (S.D.N.Y., filed Feb. 17, 2021), *Chaumont v. EHang Holdings Limited, et al.*, Case No. 1:21-cv-01526-GBD (S.D.N.Y., filed Feb. 19, 2021), and *Klein v. EHang Holdings Limited, et al.*, Case No. 2:21-cv-01811-JFW-PVC (C.D. Cal., filed Feb. 26, 2021)) were filed by purported holders of our ADSs in federal court. The complaints asserted claims under Sections 10(b) and 20(a) of the Securities Exchange Act of 1934, as amended, and generally allege that our company and certain of our officers made false and misleading statements regarding the status of its urban air mobility business, its international and domestic regulatory approvals, its relationships with major customers, and its manufacturing facilities. The complaints name as defendants our company and certain of our officers. In addition to costs and attorneys’ fees, the complaints seek compensatory and punitive damages. We believe these claims are without merit and intend to vigorously defend against them. These lawsuits were consolidated into a single class action lawsuit under the caption *In re EHang Holdings Ltd. Securities Litigation 1.21-CV-01392-GBD-GWG* (S.D.N.Y., filed Feb. 19, 2021), and a lead plaintiff and lead counsel were selected in February 2022. The lead plaintiff filed an amended complaint on April 25, 2022, making similar allegations as those in the previous complaints. Defendants filed a motion to dismiss the amended complaint in June 2022. The lead plaintiff filed an opposition to the defendants’ motion to dismiss in August 2022. The defendants filed a reply in support of their motion to dismiss in September 2022. In October 2022, the Court held oral argument on defendants’ motion to dismiss. The Court granted the defendants’ motion to dismiss the amended complaint on December 15, 2022, and entered final judgment dismissing the action in its entirety with prejudice on January 24, 2023. Lead plaintiff did not appeal the final judgment and on February 23, 2023, lead plaintiff’s deadline to appeal expired.

A former employee of our former U.S. subsidiary, EHang, Inc., filed a civil lawsuit against EHang Holdings, the VIE and certain individual defendants, including Mr. Huazhi Hu, chairman and chief executive officer of EHang Holdings, in the United States District Court for the Northern District of California. The plaintiff alleged that he was entitled to receive restricted share units from us. Following a trial by jury in April 2022, the Court entered judgment for the Plaintiff and against EHang Holdings, the VIE and Mr. Huazhi Hu as follows: (i) Judgment is entered against EHang Holdings on claims for breach of contract, false promise and unpaid wages, and EHang Holdings is held jointly and severally liable for compensatory damages in the amount of US\$3,500,000 and is liable for punitive damages in the amount of US\$10,000,000; (ii) Judgment is entered against the VIE on claims for breach of contract, false promise and unpaid wages, and the VIE is held jointly and severally liable for compensatory damages in the amount of US\$3,500,000; and (iii) Judgment is entered against Mr. Huazhi Hu on claims for false promise and unpaid wages, and Mr. Hu is held jointly and severally liable for compensatory damages in the amount of US\$3,500,000 and is liable for punitive damages in the amount of US\$5,000,000. We then filed a Motion for New Trial challenging the finding of false promise, the amount of the compensatory damage award, and the amount of the punitive damage award. The judge granted the Motion as to the false promise claim and set aside the verdict on that cause of action against EHang Holdings and Mr. Hu, and because the false promise claim was the only claim that could give rise to punitive damages, the Court set aside the punitive damage award and ordered a new trial on the false promise claim. The Court denied the motion as to the compensatory damage award. Following the Motion for New Trial, the parties have been engaged in settlement discussions. On April 25, 2023, the parties entered into a settlement agreement involving a total payment to the former employee of \$3,375,000 in four equal quarterly installments within one year.

Dividend Policy

Our board of directors has discretion on whether to distribute dividends, subject to certain requirements of Cayman Islands law. In addition, our shareholders may by ordinary resolution declare a dividend, but no dividend may exceed the amount recommended by our board of directors. In either case, all dividends are subject to certain restrictions under Cayman Islands law, namely that our company may only pay dividends out of profits or share premium, and provided always that in no circumstances may a dividend be paid if this would result in our company being unable to pay its debts as they fall due in the ordinary course of business. Even if we decide to pay dividends, the form, frequency and amount will depend upon 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.

We do not have any present plan to pay any cash dividends on our ordinary shares in the foreseeable future. We currently intend to retain most, if not all, of our available funds and any future earnings to operate and expand our business.

We are a holding company incorporated in the Cayman Islands. We may rely on dividends from our subsidiaries in China for our cash requirements, including any payment of dividends to our shareholders. PRC regulations may restrict the ability of our PRC subsidiaries to pay dividends to us. See “Item 4. Information on the Company—B. Business Overview—PRC Regulation—Dividend Distribution.”

If we pay any dividends on our ordinary shares, we will pay those dividends which are payable in respect of the Class A ordinary shares underlying the ADSs to the depositary, as the registered holder of such ordinary shares, and the depositary then will pay such amounts to the ADS holders in proportion to the Class A ordinary shares underlying the ADSs held by such ADS holders, 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.

B. Significant Changes.

Except as disclosed elsewhere in this annual report, 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.

See “—C. Markets.”

B. Plan of Distribution.

Not applicable.

C. Markets.

The ADSs, each represents two Class A ordinary shares, have been listed on the Nasdaq Global Market since December 12, 2019, under the symbol “EH.”

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.

The following are summaries of material provisions of our currently effective fifth amended and restated memorandum and articles of association, and of the Companies Act, insofar as they relate to the material terms of our ordinary shares.

Objects of Our Company. Under our memorandum and articles of association, the objects of our company are unrestricted and we have the full power and authority to carry out any object not prohibited by the law of the Cayman Islands.

Ordinary Shares. Our ordinary shares are issued in registered form and are issued when registered in our register of shareholders. We may not issue shares to bearer. Our shareholders who are nonresidents of the Cayman Islands may freely hold and vote their shares. Our ordinary shares are divided into Class A ordinary shares and Class B ordinary shares. Holders of our Class A ordinary shares and Class B ordinary shares have the same rights except for voting and conversion rights. Each Class A ordinary share shall entitle the holder thereof to one vote on all matters subject to vote at our general meetings, and each Class B ordinary share shall entitle the holder thereof to ten votes on all matters subject to vote at our general meetings.

Conversion. Each Class B ordinary share is convertible into one Class A ordinary share at any time at the option of the holder thereof. Class A ordinary shares are not convertible into Class B ordinary shares in any event. Upon any sale, transfer, assignment or disposition of any Class B ordinary shares by their holder or upon a change of ultimate beneficial ownership of any Class B ordinary shares to any person other than our founder or an affiliate controlled by our founder, each such Class B ordinary share shall be automatically and immediately converted into one of Class A ordinary share.

Dividends. The holders of our ordinary shares are entitled to such dividends as may be declared by our board of directors. In addition, our shareholders may declare dividends by ordinary resolution, but no dividend shall exceed the amount recommended by our directors. Our amended and restated memorandum and articles of association provide that the directors may, before recommending or declaring any dividend, set aside out of the funds legally available for distribution such sums as they think proper as a reserve or reserves which shall, in the absolute discretion of the directors, be applicable for meeting contingencies or for equalizing dividends or for any other purpose to which those funds may be properly applied. Under the laws of the Cayman Islands, our company may pay a dividend out of either profit or share premium account, provided that in no circumstances may a dividend be paid if this would result in our company being unable to pay its debts as they fall due in the ordinary course of business.

Voting Rights. Holders of our Class A ordinary shares and our Class B ordinary shares shall, at all times, vote together as one class on all matters submitted to a vote by our shareholders at any general meeting of our company. Each Class A ordinary share shall be entitled to one vote, and each Class B ordinary share shall be entitled to ten votes, on all matters subject to a vote on a poll at general meetings of our company. Voting at any shareholders' meeting is by show of hands unless a poll is demanded (before or on the declaration of the result of the show of hands). A poll may be demanded by the chairman of such meeting or any one or more shareholders who together hold not less than 10% of the votes attaching to the total ordinary shares which are present in person or by proxy at the meeting.

An ordinary resolution to be passed at a meeting by the shareholders requires the affirmative vote of a simple majority of the votes attaching to the ordinary shares cast at a meeting, while a special resolution requires the affirmative vote of no less than two-thirds of the votes cast attaching to the outstanding ordinary shares at a meeting. A special resolution will be required for important matters such as a change of name or making changes to our memorandum and articles of association. Holders of the ordinary shares may, among other things, divide or combine their shares by ordinary resolution.

General Meetings of Shareholders. As a Cayman Islands exempted company, we are not obliged by the Companies Act to call shareholders' annual general meetings. Our memorandum and articles of association provide that we may (but are not obliged to) in each year hold a general meeting as our annual general meeting in which case we shall specify the meeting as such in the notices calling it, and the annual general meeting shall be held at such time and place as may be determined by our directors.

Shareholders' general meetings may be convened by a majority of our board of directors. Advance notice of at least ten calendar days is required for the convening of our annual general shareholders' meeting (if any) and any other general meeting of our shareholders. A quorum required for any general meeting of shareholders consists of at least one shareholder present or by proxy, representing not less than one-third of all votes attaching to all of our shares in issue and entitled to vote.

The Companies Act provides shareholders with only limited rights to requisition a general meeting, and does not provide shareholders with any right to put any proposal before a general meeting. However, these rights may be provided in a company's articles of association. Our memorandum and articles of association provide that upon the requisition of shareholders representing in aggregate not less than one-third of the votes attaching to the issued and outstanding shares of our company entitled to vote at general meetings, our board will convene an extraordinary general meeting and put the resolutions so requisitioned to a vote at such meeting. However, our memorandum and articles of association do not provide our shareholders with any right to put any proposals before annual general meetings or extraordinary general meetings not called by such shareholders.

Transfer of Ordinary Shares. Subject to the restrictions set out below, any of our shareholders may transfer all or any of his or her ordinary shares by an instrument of transfer in the usual or common form or any other form approved by our board of directors.

Our board of directors may, in its absolute discretion, decline to register any transfer of any ordinary share which is not fully paid up or on which we have a lien. Our board of directors may also decline to register any transfer of any ordinary share unless:

- the instrument of transfer is lodged with us, accompanied by the certificate for the ordinary shares to which it relates and such other evidence as our board of directors may reasonably require to show the right of the transferor to make the transfer;
- the instrument of transfer is in respect of only one class of ordinary shares;
- the instrument of transfer is properly stamped, if required;
- in the case of a transfer to joint holders, the number of joint holders to whom the ordinary share is to be transferred does not exceed four; and
- a fee of such maximum sum as the Nasdaq Global Market may determine to be payable or such lesser sum as our directors may from time to time require is paid to us in respect thereof.

If our directors refuse to register a transfer they shall, within three months after the date on which the instrument of transfer was lodged, send to each of the transferor and the transferee notice of such refusal.

The registration of transfers may, after compliance with any notice required of the Nasdaq Global Market, be suspended and the register closed at such times and for such periods as our board of directors may from time to time determine, provided, however, that the registration of transfers shall not be suspended nor the register closed for more than 30 days in any year.

Liquidation. On the winding up of our company, if the assets available for distribution amongst our shareholders shall be more than sufficient to repay the whole of the share capital at the commencement of the winding up, the surplus shall be distributed amongst our shareholders in proportion to the par value of the shares held by them at the commencement of the winding up, subject to a deduction from those shares in respect of which there are monies due, of all monies payable to our company for unpaid calls or otherwise. If our assets available for distribution are insufficient to repay the whole of the share capital, the assets will be distributed so that the losses are borne by our shareholders in proportion to the par value of the shares held by them.

Calls on Shares and Forfeiture of Shares. Our board of directors may from time to time make calls upon shareholders for any amounts unpaid on their shares in a notice served to such shareholders at least 14 days prior to the specified time and place of payment. The shares that have been called upon and remain unpaid are subject to forfeiture.

Redemption, Repurchase and Surrender of Shares. We may issue shares on terms that such shares are subject to redemption, at our option or at the option of the holders of these shares, on such terms and in such manner as may be determined by our board of directors. Our Company may also repurchase any of our shares on such terms and in such manner as have been approved by our board of directors or by an ordinary resolution of our shareholders. Under the Companies Act, the redemption or repurchase of any share may be paid out of our Company's profits or out of the proceeds of a new issue of shares made for the purpose of such redemption or repurchase, or out of capital (including share premium account and capital redemption reserve) if our company can, immediately following such payment, pay its debts as they fall due in the ordinary course of business. In addition, under the Companies Act no such share may be redeemed or repurchased (a) unless it is fully paid up, (b) if such redemption or repurchase would result in there being no shares outstanding or (c) if the company has commenced liquidation. In addition, our company may accept the surrender of any fully paid share for no consideration.

Variations of Rights of Shares. If at any time, our share capital is divided into different classes of shares, the rights attached to any class of shares (unless otherwise subject to any rights or restrictions for the time being attached to any class), may only be materially adversely varied with the consent in writing of the holders of two-thirds of the issued shares of that class or with the sanction of a special resolution passed at a separate meeting of the holders of the shares of the class. The rights conferred upon the holders of the shares of any class issued with preferred or other rights shall not, subject to any rights or restrictions for the time being attached to the shares of that class, be deemed to be materially adversely varied by, *inter alia*, the creation or issue of further shares ranking *pari passu* with or subsequent to such existing class of shares or the redemption or purchase of any shares of any class by our company. Further, the rights the holders of shares shall not be deemed to be materially adversely varied by the creation or issue of shares with preferred or other rights including, without limitation, the creation of shares with enhanced or weighted voting rights.

Issuance of Additional Shares. Our memorandum and articles of association authorize our board of directors to issue additional ordinary shares from time to time as our board of directors shall determine, to the extent of available authorized but unissued shares.

Our memorandum and articles of association also authorize our board of directors to establish from time to time one or more series of preference shares and to determine, with respect to any series of preference shares, the terms and rights of that series, including:

- the designation of the series;
- the number of shares of the series;
- the dividend rights, dividend rates, conversion rights, voting rights; and
- the rights and terms of redemption and liquidation preferences.
- Our board of directors may issue preference shares without action by our shareholders to the extent authorized but unissued. Issuance of these shares may dilute the voting power of holders of ordinary shares.

Inspection of Books and Records. Holders of our ordinary shares will have no general right under Cayman Islands law to inspect or obtain copies of our list of shareholders or our corporate records (except for the memorandum and articles of association, our register of mortgages and charges and special resolutions of our shareholders). However, we will provide our shareholders with annual audited financial statements. See "Where You Can Find Additional Information."

Anti-Takeover Provisions. Some provisions of our memorandum and articles of association may discourage, delay or prevent a change of control of our company or management that shareholders may consider favorable, including provisions that:

- authorize our board of directors to issue preference shares in one or more series and to designate the price, rights, preferences, privileges and restrictions of such preference shares without any further vote or action by our shareholders; and
- limit the ability of shareholders to requisition and convene general meetings of shareholders.

However, under Cayman Islands law, our directors may only exercise the rights and powers granted to them under our memorandum and articles of association for a proper purpose and for what they believe in good faith to be in the best interests of our company.

Exempted Company. We are an exempted company with limited liability under the Companies Act. The Companies Act distinguishes between ordinary resident companies and exempted companies. Any company that is registered in the Cayman Islands but conducts business mainly outside of the Cayman Islands may apply to be registered as an exempted company. The requirements for an exempted company are essentially the same as for an ordinary company except that an exempted company:

- does not have to file an annual return of its shareholders with the Registrar of Companies;
- is not required to open its register of members for inspection;
- does not have to hold an annual general meeting;
- may issue shares with no par value;
- may obtain an undertaking against the imposition of any future taxation (such undertakings are usually given for 20 years in the first instance);
- may register by way of continuation in another jurisdiction and be deregistered in the Cayman Islands;
- may register as a limited duration company; and
- may register as a segregated portfolio company.

"Limited liability" means that the liability of each shareholder is limited to the amount unpaid by the shareholder on the shares of the company (except in exceptional circumstances, such as involving fraud, the establishment of an agency relationship or an illegal or improper purpose or other circumstances in which a court may be prepared to pierce or lift the corporate veil).

Differences in Corporate Law

The Companies Act is derived, to a large extent, from the older Companies Acts of England but does not follow recent English statutory enactments and accordingly there are significant differences between the Companies Act and the current Companies Act of England. In addition, the Companies Act differs from laws applicable to U.S. corporations and their shareholders. Set forth below is a summary of certain significant differences between the provisions of the Companies Act applicable to us and the laws applicable to companies incorporated in the United States and their shareholders.

Mergers and Similar Arrangements. The Companies Act permits mergers and consolidations between Cayman Islands companies and between Cayman Islands companies and non-Cayman Islands companies. For these purposes, (i) "merger" means the merging of two or more constituent companies and the vesting of their undertaking, property and liabilities in one of such companies as the surviving company, and (ii) a "consolidation" means the combination of two or more constituent companies into a consolidated company and the vesting of the undertaking, property and liabilities of such companies to the consolidated company. In order to effect such a merger or consolidation, the directors of each constituent company must approve a written plan of merger or consolidation, which must then be authorized by (a) a special resolution of the shareholders of each constituent company, and (b) such other authorization, if any, as may be specified in such constituent company's articles of association. The written plan of merger or consolidation must be filed with the Registrar of Companies of the Cayman Islands together with a declaration as to the solvency of the consolidated or surviving company, a list of the assets and liabilities of each constituent company and an undertaking that a copy of the certificate of merger or consolidation will be given to the members and creditors of each constituent company and that notification of the merger or consolidation will be published in the Cayman Islands Gazette. Court approval is not required for a merger or consolidation which is effected in compliance with these statutory procedures.

A merger between a Cayman parent company and its Cayman subsidiary or subsidiaries does not require authorization by a resolution of shareholders of that Cayman subsidiary if a copy of the plan of merger is given to every member of that Cayman subsidiary to be merged unless that member agrees otherwise. For this purpose, a company is a "parent" of a subsidiary if it holds issued shares that together represent at least ninety percent (90%) of the votes at a general meeting of the subsidiary.

The consent of each holder of a fixed or floating security interest over a constituent company is required unless this requirement is waived by a court in the Cayman Islands.

Save in certain limited circumstances, a shareholder of a Cayman constituent company who dissents from the merger or consolidation is entitled to payment of the fair value of his shares (which, if not agreed between the parties, will be determined by the Cayman Islands court) upon dissenting to the merger or consolidation, provided that the dissenting shareholder complies strictly with the procedures set out in the Companies Act. The exercise of dissenter rights will preclude the exercise by the dissenting shareholder of any other rights to which he or she might otherwise be entitled by virtue of holding shares, save for the right to seek relief on the grounds that the merger or consolidation is void or unlawful.

Separate from the statutory provisions relating to mergers and consolidations, the Companies Act also contains statutory provisions that facilitate the reconstruction and amalgamation of companies by way of schemes of arrangement, provided that the arrangement is approved by (a) 75% in value of the shareholders or class of shareholders, as the case may be, or (b) a majority in number representing 75% in value of the creditors or each class of creditors, as the case may be, with whom the arrangement is to be made, that are, in each case, present and voting either in person or by proxy at a meeting, or meetings, convened for that purpose. The convening of the meetings and subsequently the arrangement must be sanctioned by the Grand Court of the Cayman Islands. While a dissenting shareholder has the right to express to the court the view that the transaction ought not to be approved, the court can be expected to approve the arrangement if it determines that:

- the statutory provisions as to the required majority vote have been met;
- the shareholders have been fairly represented at the meeting in question and the statutory majority are acting bona fide without coercion of the minority to promote interests adverse to those of the class;
- the arrangement is such that may be reasonably approved by an intelligent and honest man of that class acting in respect of his interest; and
- the arrangement is not one that would more properly be sanctioned under some other provision of the Companies Act.

The Companies Act also contains a statutory power of compulsory acquisition which may facilitate the “squeeze out” of dissentient minority shareholder upon a tender offer. When a tender offer is made and accepted by holders of 90.0% of the shares affected within four months, the offeror may, within a two-month period commencing on the expiration of such four-month period, require the holders of the remaining shares to transfer such shares to the offeror on the terms of the offer. An objection can be made to the Grand Court of the Cayman Islands, but this is unlikely to succeed in the case of an offer which has been so approved unless there is evidence of fraud, bad faith or collusion.

If an arrangement and reconstruction by way of scheme of arrangement is thus approved and sanctioned, or if a tender offer is made and accepted, a dissenting shareholder would have no rights comparable to appraisal rights, which would otherwise ordinarily be available to dissenting shareholders of Delaware corporations, providing rights to receive payment in cash for the judicially determined value of the shares.

Shareholders' Suits. In principle, we will normally be the proper plaintiff to sue for a wrong done to us as a company, and as a general rule a derivative action may not be brought by a minority shareholder. However, based on English authorities, which would in all likelihood be of persuasive authority in the Cayman Islands, the Cayman Islands court can be expected to follow and apply the common law principles (namely the rule in *Foss v. Harbottle* and the exceptions thereto) so that a non-controlling shareholder may be permitted to commence a class action against or derivative actions in the name of the company to challenge actions where:

- a company acts or proposes to act illegally or ultra vires;
- the act complained of, although not ultra vires, could only be effected duly if authorized by more than a simple majority vote that has not been obtained; and
- those who control the company are perpetrating a "fraud on the minority."

Indemnification of Directors and Executive Officers and Limitation of Liability. Cayman Islands law does not limit the extent to which a company's memorandum and articles of association may provide for indemnification of officers and directors, except to the extent any such provision may be held by the Cayman Islands courts to be contrary to public policy, such as to provide indemnification against civil fraud or the consequences of committing a crime. Our memorandum and articles of association provide that we shall indemnify our officers and directors against all actions, proceedings, costs, charges, expenses, losses, damages or liabilities incurred or sustained by such directors or officer, other than by reason of such person's dishonesty, wilful default or fraud, in or about the conduct of our company's business or affairs (including as a result of any mistake of judgment) or in the execution or discharge of his duties, powers, authorities or discretions, including without prejudice to the generality of the foregoing, any costs, expenses, losses or liabilities incurred by such director or officer in defending (whether successfully or otherwise) any civil proceedings concerning our company or its affairs in any court whether in the Cayman Islands or elsewhere. This standard of conduct is generally the same as permitted under the Delaware General Corporation Law for a Delaware corporation.

In addition, we have entered into indemnification agreements with our directors and executive officers that provide such persons with additional indemnification beyond that provided in our memorandum and articles of association.

Insofar as indemnification for liabilities arising under the Securities Act may be permitted to our directors, officers or persons controlling us under the foregoing provisions, we have been informed that in the opinion of the SEC, such indemnification is against public policy as expressed in the Securities Act and is therefore unenforceable.

Directors' Fiduciary Duties. Under Delaware corporate law, a director of a Delaware corporation has a fiduciary duty to the corporation and its shareholders. This duty has two components: the duty of care and the duty of loyalty. The duty of care requires that a director act in good faith, with the care that an ordinarily prudent person would exercise under similar circumstances. Under this duty, a director must inform himself of, and disclose to shareholders, all material information reasonably available regarding a significant transaction. The duty of loyalty requires that a director act in a manner he reasonably believes to be in the best interests of the corporation. He must not use his corporate position for personal gain or advantage. This duty prohibits self-dealing by a director and mandates that the best interest of the corporation and its shareholders take precedence over any interest possessed by a director, officer or controlling shareholder and not shared by the shareholders generally. In general, actions of a director are presumed to have been made on an informed basis, in good faith and in the honest belief that the action taken was in the best interests of the corporation. However, this presumption may be rebutted by evidence of a breach of one of the fiduciary duties. Should such evidence be presented concerning a transaction by a director, the director must prove the procedural fairness of the transaction, and that the transaction was of fair value to the corporation.

As a matter of Cayman Islands law, a director of a Cayman Islands company is in the position of a fiduciary with respect to the company and therefore it is considered that he owes the following duties to the company—a duty to act bona fide in the best interests of the company, a duty not to make a profit based on his position as director (unless the company permits him to do so), a duty not to put himself in a position where the interests of the company conflict with his personal interest or his duty to a third party, and a duty to exercise powers for the purpose for which such powers were intended. A director of a Cayman Islands company owes to the company a duty to act with skill and care. It was previously considered that a director need not exhibit in the performance of his duties a greater degree of skill than may reasonably be expected from a person of his knowledge and experience. However, English and Commonwealth courts have moved towards an objective standard with regard to the required skill and care and these authorities are likely to be followed in the Cayman Islands.

Shareholder Action by Written Resolution. Under the Delaware General Corporation Law, a corporation may eliminate the right of shareholders to act by written consent by amendment to its certificate of incorporation. Cayman Islands law and our articles of association provide that our shareholders may approve corporate matters by way of a unanimous written resolution signed by or on behalf of each shareholder who would have been entitled to vote on such matter at a general meeting without a meeting being held.

Shareholder Proposals. Under the Delaware General Corporation Law, a shareholder has the right to put any proposal before the annual meeting of shareholders, provided it complies with the notice provisions in the governing documents. A special meeting may be called by the board of directors or any other person authorized to do so in the governing documents, but shareholders may be precluded from calling special meetings.

The Companies Act provides shareholders with only limited rights to requisition a general meeting, and does not provide shareholders with any right to put any proposal before a general meeting. However, these rights may be provided in a company's memorandum and articles of association. Our memorandum and articles of association allow our shareholders holding in aggregate not less than one-third of all votes attaching to the issued and outstanding shares of our company entitled to vote at general meetings to requisition an extraordinary general meeting of our shareholders, in which case our board is obliged to convene an extraordinary general meeting and to put the resolutions so requisitioned to a vote at such meeting. Other than this right to requisition a shareholders' meeting, our memorandum and articles of association do not provide our shareholders with any other right to put proposals before annual general meetings or extraordinary general meetings. As an exempted Cayman Islands company, we may but are not obliged by law to call shareholders' annual general meetings.

Cumulative Voting. Under the Delaware General Corporation Law, cumulative voting for elections of directors is not permitted unless the corporation's certificate of incorporation specifically provides for it. Cumulative voting potentially facilitates the representation of minority shareholders on a board of directors since it permits the minority shareholder to cast all the votes to which the shareholder is entitled on a single director, which increases the shareholder's voting power with respect to electing such director. There are no prohibitions in relation to cumulative voting under the laws of the Cayman Islands, but our articles of association do not provide for cumulative voting. As a result, our shareholders are not afforded any less protections or rights on this issue than shareholders of a Delaware corporation.

Removal of Directors. Under the Delaware General Corporation Law, a director of a corporation with a classified board may be removed only for cause with the approval of a majority of the outstanding shares entitled to vote, unless the certificate of incorporation provides otherwise. Under our articles of association, directors may be removed with or without cause, by an ordinary resolution of our shareholders. In addition, a director's office shall be vacated if the director (i) becomes bankrupt or makes any arrangement or composition with his creditors; (ii) is found to be or becomes of unsound mind or dies; (iii) resigns his office by notice in writing to the company; (iv) without special leave of absence from our board of directors, is absent from three consecutive meetings of the board and the board resolves that his office be vacated; or (v) is removed from office pursuant to any other provisions of our memorandum and articles of association.

Transactions with Interested Shareholders. The Delaware General Corporation Law contains a business combination statute applicable to Delaware corporations whereby, unless the corporation has specifically elected not to be governed by such statute by amendment to its certificate of incorporation, it is prohibited from engaging in certain business combinations with an “interested shareholder” for three years following the date that such person becomes an interested shareholder. An interested shareholder generally is a person or a group who or which owns or owned 15% or more of the target’s outstanding voting share within the past three years. This has the effect of limiting the ability of a potential acquirer to make a two-tiered bid for the target in which all shareholders would not be treated equally. The statute does not apply if, among other things, prior to the date on which such shareholder becomes an interested shareholder, the board of directors approves either the business combination or the transaction which resulted in the person becoming an interested shareholder. This encourages any potential acquirer of a Delaware corporation to negotiate the terms of any acquisition transaction with the target’s board of directors.

Cayman Islands law has no comparable statute. As a result, we cannot avail ourselves of the types of protections afforded by the Delaware business combination statute. However, although Cayman Islands law does not regulate transactions between a company and its significant shareholders, it does provide that such transactions must be entered into bona fide in the best interests of the company and not with the effect of constituting a fraud on the minority shareholders.

Restructuring. A company may present a petition to the Grand Court of the Cayman Islands for the appointment of a restructuring officer on the grounds that the company:

- (a) is or is likely to become unable to pay its debts; and
- (b) intends to present a compromise or arrangement to its creditors (or classes thereof) either pursuant to the Companies Act, the law of a foreign country or by way of a consensual restructuring.

The Grand Court may, among other things, make an order appointing a restructuring officer upon hearing of such petition, with such powers and to carry out such functions as the court may order. At any time (i) after the presentation of a petition for the appointment of a restructuring officer but before an order for the appointment of a restructuring officer has been made, and (ii) when an order for the appointment of a restructuring officer is made, until such order has been discharged, no suit, action or other proceedings (other than criminal proceedings) shall be proceeded with or commenced against the company, no resolution to wind up the company shall be passed, and no winding up petition may be presented against the company, except with the leave of the court. However, notwithstanding the presentation of a petition for the appointment of a restructuring officer or the appointment of a restructuring officer, a creditor who has security over the whole or part of the assets of the company is entitled to enforce the security without the leave of the court and without reference to the restructuring officer appointed.

Dissolution; Winding up. Under the Delaware General Corporation Law, unless the board of directors approves the proposal to dissolve, dissolution must be approved by shareholders holding 100% of the total voting power of the corporation. Only if the dissolution is initiated by the board of directors may it be approved by a simple majority of the corporation’s outstanding shares. Delaware law allows a Delaware corporation to include in its certificate of incorporation a supermajority voting requirement in connection with dissolutions initiated by the board.

Under Cayman Islands law, a company may be wound up by either an order of the courts of the Cayman Islands or by a special resolution of its members or, if the company is unable to pay its debts as they fall due, by an ordinary resolution of its members. The court has authority to order winding up in a number of specified circumstances including where it is, in the opinion of the court, just and equitable to do so. Under the Companies Act and our articles of association, our company may be dissolved, liquidated or wound up by a special resolution of our shareholders.

Variation of Rights of Shares. Under the Delaware General Corporation Law, a corporation may vary the rights of a class of shares with the approval of a majority of the outstanding shares of such class, unless the certificate of incorporation provides otherwise. Under Cayman Islands law and our articles of association, if our share capital is divided into more than one class of shares, we may vary the rights attached to any class with the written consent of the holders of two-thirds of the issued shares of that class or with the sanction of a special resolution passed at a general meeting of the holders of the shares of that class.

Amendment of Governing Documents. Under the Delaware General Corporation Law, a corporation’s governing documents may be amended with the approval of a majority of the outstanding shares entitled to vote, unless the certificate of incorporation provides otherwise. Under the Companies Act and our memorandum and articles of association, our memorandum and articles of association may only be amended by a special resolution of our shareholders.

Rights of Non-resident or Foreign Shareholders. There are no limitations imposed by our memorandum and articles of association on the rights of non-resident or foreign shareholders to hold or exercise voting rights on our shares. In addition, there are no provisions in our memorandum and articles of association that require our company to disclose shareholder ownership above any particular ownership threshold.

C. Material Contracts.

Other than in the ordinary course of business and other than those described in "Item 4. Information on the Company" or "Item 7. Major Shareholders and Related Party Transactions—B. Related Party Transactions" or elsewhere in this annual report, we have not entered into any material contract during the two years immediately preceding the date of this annual report.

D. Exchange Controls.

See “Item 4. Information on the Company—B. Business Overview—PRC Regulation—Foreign Exchange.”

E. Taxation.

The following summary of the material Cayman Islands, PRC and U.S. federal income tax consequences of an investment in the ADSs or our Class A ordinary shares is based upon laws and relevant interpretations thereof in effect as of the date of this annual report, all of which are subject to change. This summary does not deal with all possible tax consequences relating to an investment in the ADSs or our Class A ordinary shares, such as the tax consequences under U.S. state and local tax laws or under the tax laws of jurisdictions other than the Cayman Islands, PRC and the United States. To the extent that the discussion relates to matters of Cayman Islands tax law, it represents the opinion of Maples and Calder (Hong Kong) LLP, our counsel as to Cayman Islands law, and to the extent it relates to summary or description of PRC tax law, it represents the opinion of AllBright Law Offices, our counsel as to PRC law.

Cayman Islands Taxation

The Cayman Islands currently levies no taxes on individuals or corporations based upon profits, income, gains or appreciation and there is no taxation in the nature of inheritance tax or estate duty. There are no other taxes likely to be material to us levied by the government of the Cayman Islands except for stamp duties which may be applicable on instruments executed in, or, after execution, brought within the jurisdiction of the Cayman Islands. The Cayman Islands is not party to any double tax treaties that are applicable to any payments made to or by our company. There are no exchange control regulations or currency restrictions in the Cayman Islands.

Payments of dividends and capital in respect of our ordinary shares will not be subject to taxation in the Cayman Islands and no withholding will be required on the payment of a dividend or capital to any holder of our ordinary shares, nor will gains derived from the disposal of our ordinary shares be subject to Cayman Islands income or corporation tax.

PRC Taxation

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

We believe that EHang is not a PRC resident enterprise for PRC tax purposes. EHang is not controlled by a PRC enterprise or PRC enterprise group and we do not believe that EHang meets all of the conditions above. EHang is a company incorporated outside the PRC. As a holding company, its key assets are its ownership interests in its subsidiaries, and its key assets are located, and its records (including the resolutions of its board of directors and the resolutions of its shareholders) are maintained, outside the PRC. For the same reasons, we believe our other entities outside of China are not PRC resident enterprises either. However, the tax resident status of an enterprise is subject to determination by the PRC tax authorities and uncertainties remain with respect to the interpretation of the term “de facto management body.” There can be no assurance that the PRC government will ultimately take a view that is consistent with us.

If the PRC tax authorities determine that EHang is a PRC resident enterprise for enterprise income tax purposes, we may be required to withhold a 10% withholding tax from dividends we pay to our shareholders that are non-resident enterprises, including the holders of the ADSs. In addition, non-resident enterprise shareholders (including the ADS holders) may be subject to a 10% PRC tax on gains realized on the sale or other disposition of ADSs or ordinary shares, if such income is treated as sourced from within the PRC. It is unclear whether our non-PRC individual shareholders (including the ADS holders) would be subject to any PRC tax on dividends or gains obtained by such non-PRC individual shareholders in the event we are determined to be a PRC resident enterprise. If any PRC tax were to apply to such dividends or gains, it would generally apply at a rate of 20% unless a reduced rate is available under an applicable tax treaty. It is also unclear whether non-PRC shareholders of EHang would be able to claim the benefits of any tax treaties between their country of tax residence and the PRC in the event that EHang is treated as a PRC resident enterprise. Pursuant to the EIT Law and its implementation rules, if a non-resident enterprise has not set up an organization or establishment in China, or has set up an organization or establishment but the income derived has no actual connection with such organization or establishment, it will be subject to a withholding tax on its PRC-sourced income at a rate of 10%. Pursuant to the Arrangement between Mainland China and the Hong Kong Special Administrative Region for the Avoidance of Double Taxation and Tax Evasion on Income, the tax rate in respect to dividends paid by a PRC enterprise to a Hong Kong enterprise is reduced to 5% from a standard rate of 10% if the Hong Kong enterprise directly holds at least 25% of the PRC enterprise. Pursuant to the Notice of the State Administration of Taxation on the Issues concerning the Application of the Dividend Clauses of Tax Agreements, or SAT Circular 81, a Hong Kong resident enterprise must meet the following conditions, among others, in order to enjoy the reduced tax rate: (i) it must directly own the required percentage of equity interests and voting rights in the PRC resident enterprise; and (ii) it must have directly owned such percentage in the PRC resident enterprise throughout the 12 months prior to receiving the dividends. Furthermore, the Administrative Measures for Non-Resident Enterprises to Enjoy Treatments under Tax Treaties (For Trial Implementation), which became effective in October 2009, require that non-resident enterprises must obtain approval from the relevant tax authority in order to enjoy the reduced tax rate. There are also other conditions for enjoying the reduced tax rate according to other relevant tax rules and regulations. Accordingly, our subsidiary may be able to enjoy the 5% tax rate for the dividends it receives from its PRC incorporated subsidiaries if they satisfy the conditions prescribed under SAT Circular 81 and other relevant tax rules and regulations and obtain the approvals as required. However, according to SAT Circular 81, if the relevant tax authorities determine our transactions or arrangements are for the primary purpose of enjoying a favorable tax treatment, the relevant tax authorities may adjust the favorable tax rate on dividends in the future.

Provided that our Cayman Islands holding company, EHang, is not deemed to be a PRC resident enterprise, holders of the ADSs and ordinary shares who are not PRC residents will not be subject to PRC income tax on dividends distributed by us or gains realized from the sale or other disposition of our shares or ADSs. SAT Public Notice 7 further clarifies that, if a non-resident enterprise derives income by acquiring and selling shares in an offshore listed enterprise in the public market, such income will not be subject to PRC tax. However, there is uncertainty as to the application of SAT Bulletin 37 and SAT Public Notice 7, we and our non-PRC resident investors may be at risk of being required to file a return and being taxed under SAT Bulletin 37 and SAT Public Notice 7 and we may be required to expend valuable resources to comply with SAT Bulletin 37 and SAT Public Notice 7 or to establish that we should not be taxed under SAT Bulletin 37 and SAT Public Notice 7. See “Item 3. Key Information—D. Risk Factors—Risks Relating to Doing Business in China—We face uncertainty with respect to indirect transfers of equity interests in PRC resident enterprises by their non-PRC holding companies.”

U.S. Federal Income Taxation

The following discussion is a summary of certain material U.S. federal income tax considerations generally applicable to the ownership and disposition of the ADSs or ordinary shares by a U.S. Holder (as defined below) that holds the ADSs or ordinary shares as “capital assets” (generally, property held for investment) under the U.S. Internal Revenue Code of 1986, as amended, or the Code. This discussion is based upon existing U.S. federal income tax law, which is subject to differing interpretations or change, possibly with retroactive effect. No ruling has been sought from the Internal Revenue Service, the IRS, with respect to any U.S. federal income tax consequences described below, and there can be no assurance that the IRS or a court will not take a contrary position. This discussion, moreover, does not address the U.S. federal estate, gift, Medicare, and alternative minimum tax considerations, any election to apply Section 1400Z-2 of the Code to gains recognized with respect to sales or other dispositions of the ADSs or ordinary shares, special accounting rules under Section 451(b) of the Code, or any state, local or non-U.S. tax considerations, relating to the ownership or disposition of the ADSs or ordinary shares. The following summary also does not address all aspects of U.S. federal income taxation that may be important to particular investors in light of their individual circumstances or to persons in special tax situations such as:

- banks and other financial institutions;
- insurance companies;
- pension plans;
- cooperatives;
- regulated investment companies;
- real estate investment trusts;
- broker-dealers;
- dealers or traders that elect to use a mark-to-market method of accounting;
- certain former U.S. citizens or long-term residents;
- tax-exempt entities (including private foundations);
- governmental organizations;
- investors who acquire their ADSs or ordinary shares pursuant to any employee share option or otherwise as compensation;
- investors that will hold their ADSs or ordinary shares as part of a straddle, hedge, conversion, constructive sale or other integrated transaction for U.S. federal income tax purposes;
- investors that have a functional currency other than the U.S. dollar;
- investors that actually or constructively own 10% or more of our stock (by vote or value); or
- partnerships or other entities taxable as partnerships for U.S. federal income tax purposes, or persons holding ADSs or ordinary shares through such entities,

- all of whom may be subject to tax rules that differ significantly from those discussed below.

Each U.S. Holder is urged to consult its tax advisor regarding the U.S. federal, state and local and non-U.S. tax considerations of owning and disposing of the ADSs or ordinary shares in its particular circumstances.

General

For purposes of this discussion, a “U.S. Holder” is a beneficial owner of the ADSs or ordinary shares that is, for U.S. federal income tax purposes:

- an individual who is a citizen or resident of the United States;
- a corporation (or other entity treated as a corporation for U.S. federal income tax purposes) created in or organized under the law of the United States or any state thereof or the District of Columbia;
- an estate the income of which is includible in gross income for U.S. federal income tax purposes regardless of its source; or
- a trust (A) the administration of which is subject to the primary supervision of a U.S. court and which has one or more U.S. persons who have the authority to control all substantial decisions of the trust or (B) that has otherwise validly elected to be treated as a U.S. person under the Code.

If a partnership (or other entity treated as a partnership for U.S. federal income tax purposes) is a beneficial owner of ADSs or ordinary shares, the tax treatment of a partner in the partnership will generally depend upon the status of the partner and the activities of the partnership. Partnerships holding the ADSs or ordinary shares and their partners are urged to consult their tax advisors regarding an investment in the ADSs or ordinary shares.

For U.S. federal income tax purposes, it is generally expected that a U.S. Holder of ADSs will be treated as the beneficial owner of the underlying shares represented by the ADSs. The remainder of this discussion assumes that a U.S. Holder of the ADSs will be treated in this manner. Accordingly, deposits or withdrawals of ordinary shares for ADSs will generally not be subject to U.S. federal income tax. The U.S. Treasury has expressed concerns that intermediaries in the chain of ownership between a U.S. Holder of an ADS and the issuer of the underlying share may be taking actions inconsistent with the beneficial ownership of the underlying share. Accordingly, the creditability of foreign taxes, if any, could be affected by actions taken by such intermediaries if, as a result of such actions, the U.S. Holder of the ADS is not properly treated as the beneficial owner of the underlying share.

Dividends

Subject to the discussion below under “—Passive Foreign Investment Company Rules,” distributions paid on the ADSs or ordinary shares out of our current or accumulated earnings and profits, as determined under U.S. federal income tax principles, will generally be includible in the gross income of a U.S. Holder as dividend income on the day actually or constructively received by the U.S. Holder, in the case of ordinary shares, or by the depositary, in the case of ADSs. Because we do not intend to determine our earnings and profits on the basis of U.S. federal income tax principles, any distribution we pay will generally be treated as a “dividend” for U.S. federal income tax purposes. Dividends received on the ADSs or ordinary shares will not be eligible for the dividends received deduction allowed to corporations in respect of dividends received from U.S. corporations. The amount of any dividend income paid in foreign currency will be the U.S. dollar amount calculated by reference to the spot rate in effect on the date of receipt, regardless of whether the payment is in fact converted into U.S. dollars on such date. If the dividend is converted into U.S. dollars on the date of receipt, a U.S. Holder generally should not be required to recognize foreign currency gain or loss in respect of the amount received. A U.S. Holder may have foreign currency gain or loss if the dividend is converted into U.S. dollars after the date of receipt. Subject to applicable limitations, dividends paid to certain non-corporate U.S. Holders may be taxable at reduced rates. Non-corporate U.S. Holders should consult their tax advisers regarding the availability of these reduced tax rates in their particular circumstances.

Dividends will generally be treated as income from foreign sources for United States foreign tax credit purposes and will generally constitute passive category income. In the event that we are deemed to be a PRC resident enterprise under the PRC Enterprise Income Tax Law, a U.S. Holder may be subject to PRC withholding taxes on dividends paid on the ADSs or ordinary shares (see "Item 10. Additional Information—E. Taxation—PRC Taxation"). For U.S. federal income tax purposes, the amount of the dividend income will include amounts withheld in respect of PRC withholding tax, if any.

Depending on the U.S. Holder's individual facts and circumstances, a U.S. Holder may be eligible, subject to a number of complex limitations, to claim a foreign tax credit not in excess of any applicable treaty rate in respect of any foreign withholding taxes imposed on dividends received on the ADSs or ordinary shares. A U.S. Holder who does not elect to claim a foreign tax credit for foreign tax withheld may instead claim a deduction, for U.S. federal income tax purposes, in respect of such withholding, but only for a year in which such holder elects to do so for all creditable foreign income taxes. The rules governing the foreign tax credit are complex and their outcome depends in large part on the U.S. Holder's individual facts and circumstances. Accordingly, U.S. Holders are urged to consult their tax advisors regarding the availability of the foreign tax credit under their particular circumstances.

Sale or Other Disposition

Subject to the discussion below under "—Passive Foreign Investment Company Rules," a U.S. Holder will generally recognize gain or loss upon the sale or other disposition of the ADSs or ordinary shares in an amount equal to the difference between the amount realized upon the disposition and such holder's adjusted tax basis in such ADSs or ordinary shares. The gain or loss will generally be capital gain or loss. Any capital gain or loss will be long-term if the ADSs or ordinary shares have been held for more than one year. The deductibility of a capital loss is subject to limitations.

Any such gain or loss that the U.S. Holder recognizes will generally be treated as U.S.-source income or loss for foreign tax credit limitation purposes, which will generally limit the availability of foreign tax credits. However, in the event we are deemed to be a PRC resident enterprise under the PRC Enterprise Income Tax Law, we may be eligible for the benefits of the United States-PRC income tax treaty. In such event, if PRC tax were to be imposed on any gain from the disposition of the ADSs or ordinary shares, a U.S. Holder that is eligible for the benefits of the United States-PRC income tax treaty may elect to treat such gain as PRC source income. If a U.S. Holder is not eligible for the benefits of the United States-PRC income tax treaty or fails to make the election to treat any gain as foreign source, then such U.S. Holder 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 U.S. federal income tax due on other income derived from foreign sources in the same income category (generally, the passive category). Each U.S. Holder is advised to consult its tax advisors regarding the tax consequences if a foreign tax is imposed on a disposition of the ADSs or ordinary shares, including the availability of the foreign tax credit under its particular circumstances.

Passive Foreign Investment Company Rules

A non-U.S. corporation, such as our company, will be classified as a PFIC if, in the case of any particular taxable year, either (i) 75% or more of its gross income for such year consists of certain types of "passive" income or (ii) 50% or more of the value of its assets (determined on the basis of a quarterly average) during such year is attributable to assets that produce or are held for the production of passive income. For this purpose, cash and assets readily convertible into cash are generally categorized as passive assets and the company's goodwill and other unbooked intangibles associated with active business activities may generally be classified as active assets. Passive income generally includes, among other things, dividends, interest, rents, royalties, and gains from the disposition of passive assets. For purposes of these rules, we will be treated as owning a proportionate share of the assets and earning a proportionate share of the income of any other corporation in which we own, directly or indirectly, more than 25% (by value) of the stock. Although the law in this regard is unclear, we intend to treat the VIE and the VIE's subsidiaries as being owned by us for U.S. federal income tax purposes, not only because we have the power to direct the significant activities of such entities but also because we are entitled to substantially all of their economic benefits and, as a result, we consolidate their results of operations in our consolidated financial statements.

Assuming that we are treated as the owner of the VIE (and its subsidiaries) for U.S. federal income tax purposes, and based upon the nature of our business, the composition of our income and assets and the value of our assets, including goodwill (which is based on the market price of the ADSs), we do not believe we were a PFIC for U.S. federal income tax purposes for the taxable year ended December 31, 2021. However, our PFIC status for any taxable year is a factual determination that can be made only after the end of such year, and will depend on the composition of our income and assets and the value of our assets for such year. Moreover, because we hold, and may continue to hold, a significant amount of cash, our PFIC status for any taxable year may depend on the value of our goodwill which may be determined, in part, by reference to the market price of the ADSs, which may change from time to time. In addition, it is not entirely clear how the contractual arrangements between us and the VIE will be treated for purposes of the PFIC rules. If it were determined that we are not the owner of the stock of the VIE for U.S. federal income tax purposes, we could be treated as a PFIC. In light of the foregoing, there can be no assurance that we were not, or will not be, a PFIC for any taxable year. Our U.S. counsel expresses no opinion with respect to our PFIC status for any taxable year.

If we are a PFIC for any taxable year during which a U.S. Holder holds the ADSs or ordinary shares, and unless the U.S. Holder makes a mark-to-market election (as described below), the U.S. Holder will generally be subject to special tax rules that have a penalizing effect, regardless of whether we remain a PFIC, on (i) any excess distribution that we make to the U.S. Holder (which generally means any distribution paid during a taxable year to a U.S. Holder that is greater than 125 percent of the average annual distributions paid in the three preceding taxable years or, if shorter, the U.S. Holder's holding period for the ADSs or ordinary shares), and (ii) any gain realized on the sale or other disposition of the ADSs or ordinary shares. Under the PFIC rules:

- the excess distribution or gain will be allocated ratably over the U.S. Holder's holding period for the ADSs or ordinary shares;
- the amount allocated to the current taxable year and any taxable years in the U.S. Holder's holding period prior to the first taxable year in which we are classified as a PFIC (each, a "pre-PFIC year") will be taxable as ordinary income;
- the amount allocated to each prior taxable year, other than a pre-PFIC year, will be subject to tax at the highest tax rate in effect for individuals or corporations, as appropriate, for that year; and
- the interest charge generally applicable to underpayments of tax will be imposed on the tax attributable to each prior taxable year, other than a pre-PFIC year.

If we are a PFIC for any taxable year during which a U.S. Holder holds the ADSs or ordinary shares and any of our subsidiaries, the VIE or any of the subsidiaries of the VIE is also a PFIC, such U.S. 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. U.S. Holders are urged to consult their tax advisors regarding the application of the PFIC rules to any of our subsidiaries, the VIE or any of the subsidiaries of the VIE.

As an alternative to the foregoing rules, a U.S. Holder of “marketable stock” (as defined below) in a PFIC may make a mark-to-market election with respect to such stock. If we are a PFIC and a U.S. Holder makes this election with respect to the ADSs, the holder will generally (i) include as ordinary income for each taxable year that we are a PFIC the excess, if any, of the fair market value of the ADSs held at the end of the taxable year over the adjusted tax basis of such ADSs and (ii) deduct as an ordinary loss in each such taxable year the excess, if any, of the adjusted tax basis of the ADSs over the fair market value of such ADSs held at the end of the taxable year, but such deduction will only be allowed to the extent of the amount previously included in income as a result of the mark-to-market election. The U.S. Holder’s adjusted tax basis in the ADSs would be adjusted to reflect any income or loss resulting from the mark-to-market election. If a U.S. Holder makes a mark-to-market election in respect of the ADSs and we cease to be classified as a PFIC, the holder will not be required to take into account the gain or loss described above during any period that we are not classified as a PFIC. If a U.S. Holder makes a mark-to-market election, any gain such U.S. Holder recognizes upon the sale or other disposition of the ADSs in a year when we are a PFIC will be treated as ordinary income and any loss will be treated as ordinary loss, but such loss will only be treated as ordinary loss to the extent of the net amount previously included in income as a result of the mark-to-market election.

The mark-to-market election is available only for “marketable stock,” which is stock that is regularly traded on a qualified exchange or other market as defined in applicable U.S. Treasury Regulations. The ADSs will be treated as “regularly traded” for any calendar year in which more than a *de minimis* quantity of the ADSs are traded on a qualified exchange for at least 15 days during each calendar quarter. The Nasdaq Global Market, where the ADSs are listed, is a qualified exchange for this purpose.

Because a mark-to-market election cannot be made for any lower-tier PFICs that we may own, a U.S. Holder may continue to be subject to the PFIC rules with respect to such U.S. Holder’s indirect interest in any investments held by us that are treated as an equity interest in a PFIC for U.S. federal income tax purposes.

We do not intend to provide information necessary for U.S. Holders to make qualified electing fund elections which, if available, would result in tax treatment different from (and generally less adverse than) the general tax treatment for PFICs described above.

If a U.S. Holder owns the ADSs or ordinary shares during any taxable year that we are a PFIC, the holder must generally file an annual IRS Form 8621 or such other form as is required by the U.S. Treasury Department. Each U.S. Holder is advised to consult its tax advisor regarding the potential tax consequences to such holder if we were, are or become a PFIC, including the possibility of making a mark-to-market election.

Information Reporting and Backup Withholding

Payments of dividends and sales proceeds that are made within the United States or through certain U.S.-related financial intermediaries may be subject to information reporting and backup withholding, unless (i) the U.S. Holder is a corporation or other “exempt recipient” and (ii) in the case of backup withholding, the U.S. Holder provides a correct taxpayer identification number and certifies that it is not subject to backup withholding.

The amount of any backup withholding from a payment to a U.S. Holder will be allowed as a credit against the U.S. Holder’s U.S. federal income tax liability and may entitle it to a refund, provided that the required information is timely furnished to the IRS. Certain U.S. Holders who are individuals (or certain specified entities) may be required to report information relating to their ownership of the ADSs or ordinary shares, unless the ADSs or ordinary shares are held in accounts at financial institutions (in which case the accounts may be reportable if maintained by non-U.S. financial institutions). U.S. Holders should consult their tax advisers regarding their reporting obligations with respect to the ADSs or ordinary shares.

F. Dividends and Paying Agents.

Not applicable.

G. Statement by Experts.

Not applicable.

H. Documents on Display.

We are subject to periodic reporting and other informational requirements of the Exchange Act as applicable to foreign private issuers. Accordingly, we are required to file reports, including annual reports on Form 20-F, and other information with the SEC. As a foreign private issuer, we are exempt from the rules of the Exchange Act prescribing the furnishing and content of proxy statements to shareholders, and our executive officers, directors and principal shareholders are not subject to the insider short-swing profit disclosure and recovery provisions of Section 16 of the Exchange Act.

All information that we have filed with the SEC can be accessed through the SEC's website at www.sec.gov. This information can also be inspected and copied at the public reference facilities maintained by the SEC at 100 F Street, N.E., Washington, D.C. 20549. You can request copies of these documents, upon payment of a duplicating fee, by writing to the SEC. Please call the SEC at 1-800-SEC-0330 for further information on the operation of the public reference rooms.

We will furnish The Bank of New York Mellon, the depositary of the ADSs, with our annual reports, which will include a review of operations and annual audited consolidated financial statements prepared in conformity with U.S. GAAP, and all notices of shareholders' meeting and other reports and communications that are made generally available to our shareholders. The depositary will make such notices, reports and communications available to holders of ADSs and, upon our written request, will mail to all record holders of ADSs the information contained in any notice of a shareholders' meeting received by the depositary from us.

In accordance with Nasdaq Stock Market Rule 5250(d), we will post this annual report on Form 20-F on our website at ir.ehang.com. In addition, we will provide hard copies of our annual report free of charge to shareholders and ADS holders upon request.

I. Subsidiary Information.

Not applicable.

Item 11. Quantitative and Qualitative Disclosures about Market Risk.

Foreign Currency Exchange Rate Risk

As of December 31, 2022, a majority of our revenues and expenses were denominated in RMB. We expect that in the future a substantial portion of our revenues will be denominated in foreign currencies as our business and operations expand in overseas markets. As a result, we are exposed to increased foreign exchange risks for U.S. dollar and other currencies. Any significant revaluation of Renminbi against U.S. dollar may adversely affect our cash flow, earnings, and financial position, and the value of, and any dividends payable on, our ordinary shares and the ADSs. As of December 31, 2022, a 1% strengthening or weakening of Renminbi against U.S. dollars would have increased or decreased our net loss by 0.5%. See "Item 3. Key Information—D. Risk Factors—Risks Relating to Doing Business in China—Future movements in exchange rates between U.S. dollars and Renminbi may adversely affect the value of our ordinary shares or the ADSs."

To the extent that we need to convert U.S. dollars into Renminbi for our operations, appreciation of Renminbi against the U.S. dollar would reduce the Renminbi amount we receive from the conversion. Conversely, if we decide to convert Renminbi into U.S. dollars for the purpose of making payments for dividends on our ordinary shares or ADSs, servicing our outstanding debt, or for other business purposes, appreciation of the U.S. dollar against the Renminbi would reduce the U.S. dollar amounts available to us.

Interest Rate Risk

We have not been exposed to material risks due to changes in interest rates, and we have not used any derivative financial instruments to manage our interest risk exposure.

Our exposure to interest rate risk primarily relates to excess cash invested in short-term investments. Investments in both fixed rate and floating rate interest earning instruments carry a degree of interest rate risk. Fixed rate securities may have their fair market value adversely impacted due to a rise in interest rates, while floating rate securities may produce less income than expected if interest rates fall.

Item 12. Description of Securities Other than Equity Securities.

A. Debt Securities.

Not applicable.

B. Warrants and Rights.

Not applicable.

C. Other Securities.

Not applicable.

D. American Depositary Shares.

Fees and Expenses

The Bank of New York Mellon, as depositary, is responsible for registering and delivering American Depositary Shares, also referred to as ADSs. Each ADS represents two Class A ordinary shares (or a right to receive two Class A ordinary shares) deposited with The Hongkong and Shanghai Banking Corporation Limited, as custodian for the depositary in Hong Kong. Each ADS also represents any other securities, cash or other property that may be held by the depositary. The deposited shares together with any other securities, cash or other property held by the depositary are referred to as the deposited securities. The depositary's office at which the ADSs are being administered and its principal executive office are each located at 240 Greenwich Street, New York, New York 10286.

An ADS holder will be required to pay the following fees under the terms of the deposit agreement:

Persons depositing or withdrawing shares or ADS holders must pay	For
\$5.00 (or less) per 100 ADSs (or portion of 100 ADSs)	<ul style="list-style-type: none"> • 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
\$0.05 (or less) per ADS	<ul style="list-style-type: none"> • 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	<ul style="list-style-type: none"> • Distribution of securities distributed to holders of deposited securities (including rights) that are distributed by the depositary to ADS holders
\$0.05 (or less) per ADS per calendar year	<ul style="list-style-type: none"> • Depositary services
Registration or transfer fees	<ul style="list-style-type: none"> • 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	<ul style="list-style-type: none"> • Cable (including SWIFT) 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 has to pay on any ADSs or shares underlying ADSs, such as stock transfer taxes, stamp duty or withholding taxes	<ul style="list-style-type: none"> • As necessary
Any charges incurred by the depositary or its agents for servicing the deposited securities	<ul style="list-style-type: none"> • As necessary

Fees and Other Payments Made by the Depositary to Us

From time to time, the depositary may make payments to us to reimburse us for costs and expenses generally arising out of establishment and maintenance of the ADS program, waive fees and expenses for services provided to us by the depositary or share revenue from the fees collected from ADS holders. In performing its duties under the deposit agreement, the depositary may use brokers, dealers, foreign currency dealers or other service providers that are owned by or affiliated with the depositary and that may earn or share fees, spreads or commissions. For the year ended December 31, 2022, we received US\$0.3 million in reimbursement from the depositary for our expenses incurred in connection with the establishment and maintenance of the ADS program.

Payment of Taxes

ADS holders will be responsible for any taxes or other governmental charges payable on the ADSs or on the deposited securities represented by any of the ADSs. The depositary may refuse to register any transfer of ADSs or allow holders thereof to withdraw the deposited securities represented by the ADSs until those taxes or other charges are paid. It may apply payments owed to ADS holders or sell deposited securities represented by the ADSs to pay any taxes owed and the ADS holders will remain liable for any deficiency. If the depositary sells deposited securities, it will, if appropriate, reduce the number of ADSs to reflect the sale and pay to ADS holders any proceeds, or send to ADS holders any property, remaining after it has paid the taxes.

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—B. Memorandum and Articles of Association—Ordinary Shares” for a description of the rights of securities holders, which remain unchanged.

Use of Proceeds

None.

Item 15. Controls and Procedures.

Evaluation of Disclosure Controls and Procedures

Our management, with the participation of our chief executive officer and chief financial officer, has performed an evaluation of the effectiveness of our disclosure controls and procedures (as defined in Rule 13a-15(e) under the Exchange Act) as of the end of the period covered by this annual report.

Based upon that evaluation, our management has concluded that, as of December 31, 2022, our disclosure controls and procedures were ineffective because of the material weaknesses in our internal control over financial reporting described in this annual report. Notwithstanding thereof, we believe that our consolidated financial statements included in this annual report fairly present our financial position, results of operations and cash flows for the fiscal years covered thereby in all material respects.

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) under the Securities Exchange Act of 1934, as amended). Our management evaluated the effectiveness of our internal control over financial reporting based on criteria established in 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 has concluded that our internal control over financial reporting was ineffective as of December 31, 2022, due to the material weaknesses in our internal control over financial reporting described below.

A material weakness is a deficiency, or a combination of deficiencies, in internal control over financial reporting, such that there is a reasonable possibility that a material misstatement of the company’s annual or interim financial statements will not be prevented or detected on a timely basis. The material weaknesses in our internal control over financial reporting identified as of December 31, 2022 were (i) the lack of financial reporting policies and procedures that are commensurate with U.S. GAAP and SEC reporting requirements, and (ii) the lack of monitoring of the collection of accounts receivable on a timely basis.

Because of its inherent limitations, internal control over financial reporting may not prevent or detect misstatements. In addition, projections of any evaluation of effectiveness of our internal control over financial reporting to future periods are subject to the risk that controls may become inadequate because of changes in conditions, or that the degree of compliance with the policies and procedures may deteriorate.

Attestation Report of the Registered Public Accounting Firm

As a company with less than US\$1.235 billion in revenues for fiscal year of 2022, we qualify as an “emerging growth company,” as defined in the JOBS Act, we may take advantage of certain temporary exemptions from various reporting requirements, including, but not limited to, not being required to comply with the auditor attestation requirements of Section 404 of the Sarbanes-Oxley Act (and the SEC rules and regulations there under). Therefore, no attestation report by our independent registered public accounting firm regarding our internal control over financial reporting is included in this annual report.

Changes in Internal Control over Financial Reporting

In preparing our consolidated financial statements as of and for the years ended December 31, 2021 included in our annual report on Form 20-F for the year ended December 31, 2021, we identified three material weaknesses in our internal control over financial reporting, as defined in the standards established by the Public Company Accounting Oversight Board of the United States, or PCAOB. The identified material weaknesses arose from our (a) lack of financial reporting policies and procedures that are commensurate with U.S. GAAP and SEC reporting requirements, (b) lack of sufficient controls for properly tracking the shipping records of the AAVs, and (c) lack of monitoring of the collection of accounts receivable on a timely basis.

We implemented the following measures to improve our internal control over financial reporting to address the identified material weaknesses respectively:

- For our lack of financial reporting policies and procedures that are commensurate with U.S. GAAP and SEC reporting and compliance requirements, we (i) hired additional accounting and financial reporting personnel with U.S. GAAP and SEC reporting experience; (ii) provided continuous and appropriate training to the accounting and financial reporting personnel, especially the training related to U.S. GAAP, and SEC rules and regulations; (iii) developed a set of accounting policies, which document the current U.S. GAAP accounting standards and technical accounting guidance that are applicable to our business; and (iv) formalized a period-end closing process to prepare financial statements and related disclosures in compliance with U.S. GAAP and SEC financial reporting requirements.
- For our lack of sufficient controls for properly tracking the shipping records of the AAVs, we (i) replaced the logistics service provider with a reputable and qualified vendor; (ii) optimized the approval process with detailed delivery information and with cross-departmental and multi-level personnel's approval and review before delivery; (iii) strengthened the delivery note with relevant parties' confirmation with signature, date and further evidenced by stamp from the logistics service provider; (iv) developed a detailed delivery ledger to control the delivery information; and (v) reconciled monthly with the logistics service provider on the delivery ledger. We have implemented and reinforced the above key controls for recording and tracking the shipping records of AAVs accurately and timely.
- For our lack of monitoring of the collection of accounts receivable on a timely basis, we implemented controls on (i) issuance of debit note to our customers to notify and acknowledge the payment terms and schedule under the signed contracts; (ii) issuance of letter of collection for those customers with late payment to claim the outstanding and past-due payments on a quarterly basis ; (iii) negotiation with customers with seriously past-due payments over the outstanding balance and signed the letter of payment plan. We also strengthened finance department's monitoring control over the collection of accounts receivable through quarterly assessment with sales department.

As of December 31, 2022, based on an assessment performed by our management on the performance of certain remediation measures mentioned above, we concluded that the material weakness of "lack of sufficient controls for properly tracking the shipping records of the AAVs" in our internal control over financial reporting previously identified as of December 31, 2021 has been remediated.

However, these measures did not fully address all material weaknesses in internal control over financial reporting, and we concluded that the material weakness relating to our lack of financial reporting policies and procedures that are commensurate with U.S. GAAP and SEC reporting requirements and lack of monitoring of the collection of accounts receivable on a timely basis still existed as of December 31, 2022.

Other than as described above, there were no changes in our internal controls over financial reporting that occurred during the period covered by this annual report that have materially affected, or are reasonably likely to materially affect, our internal control over financial reporting.

Item 16A. Audit Committee Financial Expert.

Our board of directors has determined that Mr. Conor Chia-hung Yang, an independent director (under the standards set forth in Nasdaq Stock Market Rule 5605(a)(2) and Rule 10A-3 under the Exchange Act) and member of our audit committee, is an audit committee financial expert.

Item 16B. Code of Ethics.

Our board of directors has adopted a code of ethics that applies to all of the directors, officers and employees of us and our subsidiaries, whether they work for us on a full-time, part-time, consultative, or temporary basis. Certain provisions of the code apply specifically to our chief executive officer, chief financial officer, senior finance officer, controller, senior vice presidents, vice presidents and any other persons who perform similar functions for us. We have posted a copy of our code of business conduct and ethics on our website at ir.ehang.com.

Item 16C. Principal Accountant Fees and Services.

The following table sets forth the aggregate fees by categories specified below in connection with certain professional services rendered by Ernst & Young Hua Ming LLP ("EY"), our previous principal external auditors, and by PricewaterhouseCoopers Zhong Tian LLP ("PwC"), who succeeded EY to become the principal external auditors of our consolidated financial statements on November 29, 2021, our principal external auditors, for the periods indicated.

	For the Year Ended December 31,	
	2021⁽²⁾	2022
	(RMB in thousands)	
Audit fees ⁽¹⁾	9,554	5,608
Total	9,554	5,608

Notes:

- (1) "Audit fees" means the aggregate fees billed in each of the fiscal years for professional services rendered by our principal external auditors for the audit of our annual consolidated financial statements and assistance with review of documents filed with the SEC and other statutory and regulatory filings.
- (2) The audit fees for 2021 include fees RMB7.8 million payable to EY for services rendered between January 1, 2021 and November 29, 2021 and RMB1.8 million payable to PwC from November 29, 2021 to December 31, 2021. See also "Item 16F. Change in Registrant's Certifying Accountant."
- (3) The audit fees for 2022 include fees RMB0.6 million payable to EY for services rendered between April 1, 2022 and April 30, 2022 and RMB5.0 million payable to PwC from January 1, 2022 to December 31, 2022.

The policy of our audit committee is to pre-approve all auditing and non-auditing services permitted to be performed by our independent registered public accounting firm.

Item 16D. Exemptions from the Listing Standards for Audit Committees.

Not applicable.

Item 16E. Purchases of Equity Securities by the Issuer and Affiliated Purchasers.

None.

Item 16F. Change in Registrant's Certifying Accountant.

(a) Previous independent registered public accounting firm

- (i) On November 26, 2021, Ernst & Young Hua Ming LLP ("EY") did not stand for re-election as our independent registered public accounting firm and the decision was not made due to any disagreements between us and EY.
- (ii) The reports of EY on our consolidated financial statements as of and for the fiscal year ended December 31, 2019 and 2020 did not contain an adverse opinion or a disclaimer of opinion and were not qualified or modified as to uncertainty, audit scope or accounting principles.
- (iii) During the fiscal year ended December 31, 2019 and 2020 and the subsequent interim period preceding November 26, 2021, there have been no disagreements (as defined in Item 16F(a)(1)(iv) of Form 20-F and the related instructions therein) with EY on any matter of accounting principles or practices, financial statement disclosure, or auditing scope or procedure, which disagreements, if not resolved to the satisfaction of EY, would have caused it to make reference to the subject matter of the disagreements in its report on the consolidated financial statements for such periods.

- (iv) During the fiscal year ended December 31, 2019 and 2020 and the subsequent interim period preceding November 26, 2021, there have been no "reportable events" (as that term is described in Item 16F(a)(1)(v) of Form 20-F), other than the material weaknesses in our internal control over financial reporting reported in our 2019 and 2020 annual reports on Form 20-F filed with the U.S. Securities and Exchange of Commission on April 20, 2020 and June 15, 2021, respectively.
- (v) We provided a copy of this disclosure in Item 16F to EY and requested that EY furnish us with a letter addressed to the SEC stating whether it agrees with the above statements, and if not, stating the respects in which it does not agree. A copy of the letter from EY addressed to the SEC, dated April 28, 2022, is filed as Exhibit 16.1 of this annual report.

(b) New independent registered public accounting firm

On November 29, 2021, we engaged PricewaterhouseCoopers Zhong Tian LLP ("PwC") as our new independent registered public accounting firm. During the fiscal year ended December 31, 2019 and 2020 and the subsequent interim period prior to engaging PwC, neither we nor anyone on our behalf consulted PwC regarding either (a) the application of accounting principles to a specified transaction, either completed or proposed, or the type of audit opinion that might be rendered on our financial statements, and neither a written report nor oral advice was provided to us by PwC that PwC concluded was an important factor considered by us in reaching a decision as to any accounting, auditing or financial reporting issue, or (b) any matter that was the subject of a disagreement (as defined in Item 16F(a)(1)(iv) of Form 20-F and the related instructions therein) or a reportable event (as defined in Item 16F(a)(1)(v) of Form 20-F).

Item 16G. Corporate Governance.

As a Cayman Islands company listed on the Nasdaq Global Market, we are subject to the Nasdaq Stock Market Rules corporate governance listing standards. However, Nasdaq Stock Market Rules permit a foreign private issuer like us to follow the corporate governance practices of its home country. Certain corporate governance practices in the Cayman Islands, which is our home country, may differ significantly from the Nasdaq Stock Market Rules. While we voluntarily follow most Nasdaq corporate governance rules, we may choose to take advantage of the following exemptions afforded to foreign private issuers:

- exemption from the requirement that a majority of our board of directors consists of independent directors;
- exemption from the requirement that each member of the compensation committee must be an independent director set forth in Nasdaq Rule 5605(d)(2)(A);
- exemption from the requirement that director nomination should be made by a vote in which only independent directors participate or by a nominations committee comprised solely of independent directors as set forth in Nasdaq Rule 5605(e)(1);
- exemption from the requirement to obtain shareholder approval for certain issuances of securities, including shareholder approval of stock option plans;
- exemption from the requirement that our board of directors shall have regularly scheduled meetings at which only independent directors are present as set forth in Nasdaq Rule 5605(b)(2); and
- exemption from the requirement that an annual shareholders meeting must be held no later than one year after the end of the company's fiscal year-end as set forth in Nasdaq Rule 5620(a).

We intend to follow our home country practices in lieu of the foregoing requirements, although (i) a majority of our board of directors consists of independent directors and (ii) each member of our compensation committee satisfies the independence requirements set forth in Nasdaq Rule 5605(d)(2)(A). We may also opt to rely on additional home country practice exemptions in the future. Although we may rely on home country corporate governance practices in lieu of certain of the rules in the Nasdaq Rule 5600 Series and Rule 5250(d), we must comply with Nasdaq's Notification of Noncompliance requirement (Rule 5625), the Voting Rights requirement (Rule 5640) and have an audit committee that satisfies Rule 5605(c)(3), consisting of committee members that meet the independence requirements of Rule 5605(c)(2)(A)(ii). Although we currently intend to comply with the Nasdaq corporate governance rules applicable other than as noted above, we may in the future decide to use the foreign private issuer exemption with respect to some or all the other Nasdaq corporate governance rules. As a result, our shareholders may be afforded less protection than they otherwise would under the Nasdaq corporate governance listing standards applicable to U.S. domestic issuers. We may utilize these exemptions for as long as we continue to qualify as a foreign private issuer.

We are also eligible to rely on exemptions afforded to controlled companies. A company of which more than 50% of the voting power is held by a single entity is considered a "controlled company" under the Nasdaq Stock Market Rules. A controlled company is not required to comply with the Nasdaq corporate governance rules requiring a board of directors to have a majority of independent directors, to have an independent compensation committee, and to have an independent nominations/corporate governance committee. We are a "controlled company" as defined under the Nasdaq Stock Market Rules, but we have no current intention to rely on the controlled company exemption.

Item 16H. Mine Safety Disclosure

Not applicable.

Item 16I. Disclosure Regarding Foreign Jurisdictions that Prevent Inspections

In May 2022, we were conclusively listed by the SEC as a Commission-Identified Issuer under the HFCAA following the filing of our annual report on Form 20-F for the fiscal year ended December 31, 2021. Our auditor, a registered public accounting firm that the PCAOB was unable to inspect or investigate completely in 2021, issued the audit report for us for the fiscal year ended December 31, 2021. On December 15, 2022, the PCAOB issued a report that vacated its December 16, 2021 determination and removed mainland China and Hong Kong from the list of jurisdictions where it is unable to inspect or investigate completely registered public accounting firms. For this reason, we do not expect to be identified as a Commission-Identified Issuer under the HFCAA after we file this annual report on Form 20-F.

As of the date of this annual report, to our knowledge, (i) except for (a) the 3,466,204 Class A ordinary shares of EHang Holdings Limited, or 2.9% of our total outstanding shares as of March 31, 2023, which are beneficially owned by a state-owned enterprise in the Huangdao district of the Qingdao municipality of the Shandong province and (b) the 31.5% of the equity interests in Yunfu EHang Intelligent Technology Limited which are beneficially owned by a state-owned enterprise in the Yunfu municipality of the Guangdong province, no governmental entities in the Cayman Islands or in China own shares of EHang Holdings Limited and its subsidiaries, or of the VIE and the VIE's subsidiaries, (ii) the governmental entities in China do not have a controlling financial interest in EHang Holdings Limited and its subsidiaries, or in the VIE and the VIE's subsidiaries (iii) none of the members of the board of directors of EHang Holdings Limited and its subsidiaries, or of the VIE and the VIE's subsidiaries, is an official of the Chinese Communist Party, and (iv) none of the currently effective memorandum and articles of association (or equivalent organizing document) of EHang Holdings Limited and its subsidiaries, or of the VIE and the VIE's subsidiaries, contains any charter of the Chinese Communist Party.

Item 16J. Insider Trading Policies

Not applicable.

PART III

Item 17. Financial Statements.

We have elected to provide financial statements pursuant to Item 18.

Item 18. Financial Statements.

Our consolidated financial statements are included at the end of this annual report.

Item 19. Exhibits.

Exhibit Number	Description of Document
1.1	Fifth Amended and Restated Memorandum and Articles of Association of the Registrant (incorporated herein by reference to Exhibit 3.2 to our registration statement on Form F-1 (File No. 333-234411) filed with the SEC on October 31, 2019)
2.1	Registrant's Specimen American Depositary Receipt (incorporated herein by reference to Exhibit 4.3 to the registration statement on Form S-8 (File No. 333-237769) filed with the SEC on April 21, 2020)
2.2	Registrant's Specimen Certificate for Class A ordinary shares (incorporated herein by reference to Exhibit 4.2 to the registration statement on Form F-1 (File No. 333-234411) filed with the SEC on October 31, 2019)
2.3	Deposit Agreement among the Registrant, the depositary and the owners and holders of American Depositary Shares, dated as of December 11, 2019 (incorporated herein by reference to Exhibit 4.3 to the registration statement on Form S-8 (File No. 333-237769) filed with the SEC on April 21, 2020)
2.4	Second Amended and Restated Shareholders' Agreement, dated as of December 27, 2016, by and among the Registrant and other parties thereto (incorporated herein by reference to Exhibit 4.4 to the registration statement on Form F-1 (File No. 333-234411) filed with the SEC on October 31, 2019)
2.5	Description of Securities (incorporated herein by reference to Exhibit 2.5 of our Annual Report on Form 20-F for the year ended December 31, 2019 (File No. 001-39151) filed with the SEC on April 20, 2020)
4.1	2015 Share Incentive Plan (incorporated herein by reference to Exhibit 10.1 to the registration statement on Form F-1 (File No. 333-234411) filed with the SEC on October 31, 2019)
4.2	2019 Share Incentive Plan (incorporated herein by reference to Exhibit 10.2 to the registration statement on Form F-1 (File No. 333-234411) filed with the SEC on October 31, 2019)
4.3	Form of Indemnification Agreement between the Registrant and its director and executive officers (incorporated herein by reference to Exhibit 10.3 to the registration statement on Form F-1 (File No. 333-234411) filed with the SEC on October 31, 2019)
4.4	Form of Employment Agreement between the Registrant and its executive officers (incorporated herein by reference to Exhibit 10.4 to the registration statement on Form F-1 (File No. 333-234411) filed with the SEC on October 31, 2019)

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Exhibit Number	Description of Document
4.5	English translation of the Shareholders Voting Proxy Agreement and Power of Attorney among the WFOE, the VIE and shareholders of the VIE dated October 21, 2020 (incorporated herein by reference to Exhibit 4.5 of our Annual Report on Form 20-F for the year ended December 31, 2020 (File No. 001-39151) filed with the SEC on June 15, 2021)
4.6	English translation of the Share Pledge Agreements among the WFOE and shareholders of the VIE dated October 21, 2020 (incorporated herein by reference to Exhibit 4.6 of our Annual Report on Form 20-F for the year ended December 31, 2020 (File No. 001-39151) filed with the SEC on June 15, 2021)
4.7	English translation of the Exclusive Consulting and Service Agreement and the Exclusive Services Agreement between the WFOE and the VIE dated January 29, 2016 (incorporated herein by reference to Exhibit 10.9 to the registration statement on Form F-1 (File No. 333-234411) filed with the SEC on October 31, 2019)
4.8	English translation of the Amendment to Exclusive Consulting and Service Agreement between the WFOE and the VIE dated November 30, 2018 (incorporated herein by reference to Exhibit 10.10 to the registration statement on Form F-1 (File No. 333-234411) filed with the SEC on October 31, 2019)
4.9	English translation of the Exclusive Option Agreement among the WFOE, the VIE and shareholders of the VIE dated October 21, 2020 (incorporated herein by reference to Exhibit 4.9 of our Annual Report on Form 20-F for the year ended December 31, 2020 (File No. 001-39151) filed with the SEC on June 15, 2021)
4.10	English translation of the Special Agreement on the Capital Increase of the VIE among the WFOE, the VIE and shareholders of the VIE dated February 22, 2019 (incorporated herein by reference to Exhibit 10.14 to the registration statement on Form F-1 (File No. 333-234411) filed with the SEC on October 31, 2019)
4.11	English translation of the Amendments to the Special Agreement on the Capital Increase of the VIE among the WFOE, the VIE, Huazhi Hu, Yifang Xiong and shareholders of the VIE dated September 7, 2020 and October 21, 2020, respectively (incorporated herein by reference to Exhibit 4.11 of our Annual Report on Form 20-F for the year ended December 31, 2020 (File No. 001-39151) filed with the SEC on June 15, 2021)
4.12	Subscription Agreement, dated as of January 27, 2021, between the Registrant and certain funds advised by Carmignac (incorporated herein by reference to Exhibit 4.16 of our Annual Report on Form 20-F for the year ended December 31, 2020 (File No. 001-39151) filed with the SEC on June 15, 2021)

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Exhibit Number	Description of Document
4.13*	English Translation of the Subscription Agreement, dated as of December 21, 2022, between the Registrant and Qingdao Ocean Investment Group Co., Ltd.
8.1*	List of Principal Subsidiaries and Consolidated Affiliated Entities
11.1	Code of Business Conduct and Ethics of the Registrant (incorporated herein by reference to Exhibit 99.1 to the registration statement on Form F-1 (File No. 333-234411) filed with the SEC on October 31, 2019)
12.1*	Certification of Chief Executive Officer pursuant to Exchange Act Rules 13a-14(a) and 15d-14(a), as adopted pursuant to Section 302 of the Sarbanes-Oxley Act of 2002
12.2*	Certification of Chief Financial Officer pursuant to Exchange Act Rules 13a-14(a) and 15d-14(a), as adopted pursuant to Section 302 of the Sarbanes-Oxley Act of 2002
13.1**	Certification of Chief Executive Officer pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002
13.2**	Certification of Chief Financial Officer pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002
15.1*	Consent of Ernst & Young Hua Ming LLP
15.2*	Consent of PricewaterhouseCoopers Zhong Tian LLP
15.3*	Consent of AllBright Law Offices
15.4*	Consent of Maples and Calder (Hong Kong) LLP
15.5**	Submission under Item 16I(a) of Form 20-F in relation to the Holding Foreign Companies Accountable Act
16.1	Letter from EY addressed to the Securities and Exchange Commission dated April 28, 2022 (incorporated herein by reference to Exhibit 16.1 of our Annual Report on Form 20-F for the year ended December 31, 2021 (File No. 001-39151) filed with the SEC on April 28, 2022)
101.INS*	Inline XBRL Instance Document (the cover page XBRL tags are embedded within the Inline XBRL document)
101.SCH*	Inline XBRL Taxonomy Extension Schema Document
101.CAL*	Inline XBRL Taxonomy Extension Calculation Linkbase Document
101.DEF*	Inline XBRL Taxonomy Extension Definition Linkbase Document
101.LAB*	Inline XBRL Taxonomy Extension Label Linkbase Document
101.PRE*	Inline XBRL Taxonomy Extension Presentation Linkbase Document
104	Cover Page Interactive Data File (the cover page XBRL tags are embedded within the Exhibit 101 Inline XBRL document set)

* Filed herewith

** Furnished herewith

SIGNATURES

The registrant hereby certifies that it meets all of the requirements for filing on Form 20-F and that it has duly caused and authorized the undersigned to sign this annual report on its behalf.

EHang Holdings Limited

By: /s/ Huazhi Hu

Name: Huazhi Hu

Title: Chairman of the Board of Directors and Chief
Executive Officer

Date: April 27, 2023

EHANG HOLDINGS LIMITED
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REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM

To the Board of Directors and Shareholders of EHang Holdings Limited

Opinion on the Financial Statements

We have audited the accompanying consolidated balance sheets of EHang Holdings Limited and its subsidiaries (the “Company”) as of December 31, 2022 and 2021, and the related consolidated statements of comprehensive loss, of changes in shareholders’ equity and of cash flows for the years then ended, including the related notes (collectively referred to as the “consolidated financial statements”). In our opinion, the consolidated financial statements present fairly, in all material respects, the financial position of the Company as of December 31, 2022 and 2021, and the results of its operations and its cash flows for the years then ended in conformity with accounting principles generally accepted in the United States of America.

Change in Accounting Principle

As discussed in Note 2 to the consolidated financial statements, the Company changed the manner in which it accounts for leases in 2022.

Basis for Opinion

These consolidated financial statements are the responsibility of the Company’s management. Our responsibility is to express an opinion on the Company’s consolidated financial statements based on our audits. We are a public accounting firm registered with the Public Company Accounting Oversight Board (United States) (PCAOB) and are required to be independent with respect to the Company in accordance with the U.S. federal securities laws and the applicable rules and regulations of the Securities and Exchange Commission and the PCAOB.

We conducted our audits of these consolidated financial statements in accordance with the standards of the PCAOB. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the consolidated financial statements are free of material misstatement, whether due to error or fraud. The Company is not required to have, nor were we engaged to perform, an audit of its internal control over financial reporting. As part of our audits we are required to obtain an understanding of internal control over financial reporting but not for the purpose of expressing an opinion on the effectiveness of the Company’s internal control over financial reporting. Accordingly, we express no such opinion.

Our audits included performing procedures to assess the risks of material misstatement of the consolidated financial statements, whether due to error or fraud, and performing procedures that respond to those risks. Such procedures included examining, on a test basis, evidence regarding the amounts and disclosures in the consolidated financial statements. Our audits also included evaluating the accounting principles used and significant estimates made by management, as well as evaluating the overall presentation of the consolidated financial statements. We believe that our audits provide a reasonable basis for our opinion.

Emphasis of Matter

As discussed in Note 1(c) to the consolidated financial statements, there is uncertainty as to when the Company will obtain the type certificate in the near term to launch fully commercial sales of EH216-S, which may materially and adversely affect the execution of management’s business plan and the Company’s future liquidity. Management’s evaluation of the events and conditions and management’s plans to mitigate these matters are also described in Note 1(c).

/s/ PricewaterhouseCoopers Zhong Tian LLP
Guangzhou, the People’s Republic of China

April 27, 2023

We have served as the Company’s auditor since 2021.

REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM

To the Shareholders and the Board of Directors of EHang Holdings Limited

Opinion on the Financial Statements

We have audited the accompanying consolidated statements of comprehensive loss, changes in shareholders' (deficit)/equity and cash flows of EHang Holdings Limited (the "Company") for the year ended December 31, 2020, and the related notes (collectively referred to as the "consolidated financial statements"). In our opinion, the consolidated financial statements present fairly, in all material respects, the results of its operations and its cash flows for the year ended December 31, 2020, in conformity with U.S. generally accepted accounting principles.

Basis for Opinion

These financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on the Company's financial statements based on our audits. We are a public accounting firm registered with the Public Company Accounting Oversight Board (United States) ("PCAOB") and are required to be independent with respect to the Company in accordance with the U.S. federal securities laws and the applicable rules and regulations of the Securities and Exchange Commission and the PCAOB.

We conducted our audits in accordance with the standards of the PCAOB. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement, whether due to error or fraud. The Company is not required to have, nor were we engaged to perform, an audit of its internal control over financial reporting. As part of our audits we are required to obtain an understanding of internal control over financial reporting but not for the purpose of expressing an opinion on the effectiveness of the Company's internal control over financial reporting. Accordingly, we express no such opinion.

Our audits included performing procedures to assess the risks of material misstatement of the financial statements, whether due to error or fraud, and performing procedures that respond to those risks. Such procedures included examining, on a test basis, evidence regarding the amounts and disclosures in the financial statements. Our audits also included evaluating the accounting principles used and significant estimates made by management, as well as evaluating the overall presentation of the financial statements. We believe that our audits provide a reasonable basis for our opinion.

/s/ Ernst & Young Hua Ming LLP

We served as the Company's auditor from 2018 to 2021.
Shanghai, the People's Republic of China

June 15, 2021

EHANG HOLDINGS LIMITED
CONSOLIDATED BALANCE SHEETS
(Amounts in thousands of Renminbi (“RMB”) and U.S. dollars (“US\$”),
except for number of shares and per share data)

	Note	As of December 31,		
		2021	2022	
		RMB	RMB	US\$
				Note 2(e)
ASSETS				
Current assets:				
Cash and cash equivalents		246,863	249,310	36,147
Restricted cash	2(g)	160	—	—
Short-term investments	4	65,108	—	—
Accounts receivable, net of allowance of RMB 69,417 and RMB 115,380 (US\$16,728) as of December 31, 2021 and 2022, respectively	5	56,189	20,298	2,943
Inventories	6	78,075	72,364	10,492
Prepayments and other current assets	7	29,395	45,183	6,550
Amount due from a related party	18	1,360	—	—
Total current assets		477,150	387,155	56,132
Non-current assets				
Property and equipment, net	8	33,821	47,060	6,823
Right-of-use assets, net	2(x)	—	73,482	10,654
Intangible assets, net		745	1,959	284
Long-term loans receivable	9	15,208	9,980	1,447
Long-term investments	10	6,143	9,839	1,427
Other non-current assets		2,367	1,392	202
Total non-current assets		58,284	143,712	20,837
Total assets		535,434	530,867	76,969

EHANG HOLDINGS LIMITED
CONSOLIDATED BALANCE SHEETS (CONTINUED)
(Amounts in thousands of Renminbi ("RMB") and U.S. dollars ("US\$"),
except for number of shares and per share data)

	Note	As of December 31,		
		2021	2022	
		RMB	RMB	US\$
				Note 2(e)
LIABILITIES AND SHAREHOLDERS' EQUITY				
Current liabilities (including current liabilities of the consolidated variable interest entity and its subsidiaries ("VIEs") without recourse to the Company of RMB23,755 and RMB29,993 (US\$4,348) as of December 31, 2021 and 2022, respectively)				
Short-term bank loans	12	10,000	49,794	7,219
Short-term debt	13	—	57,838	8,386
Accounts payable		45,560	35,456	5,141
Contract liabilities		14,831	19,321	2,801
Current portion of long-term bank loans	12	3,000	13,154	1,907
Accrued expenses and other liabilities	11	61,851	97,763	14,175
Current portion of lease liabilities	2(x)	—	5,520	800
Deferred income		733	1,495	217
Deferred government subsidies		468	1,993	289
Income taxes payable		4	7	1
Total current liabilities		136,447	282,341	40,936
Non-current liabilities (including non-current liabilities of the VIEs without recourse to the Company of RMB9,588 and RMB5,234 (US\$759) as of December 31, 2021 and 2022, respectively)				
Long-term bank loans	12	17,000	3,846	558
Mandatorily redeemable non-controlling interests	14	40,000	40,000	5,799
Deferred tax liabilities	17	292	292	42
Unrecognized tax benefit	17	5,480	5,480	795
Lease liabilities	2(x)	—	69,913	10,136
Deferred income		2,169	2,928	425
Other non-current liabilities		—	1,389	201
Total non-current liabilities		64,941	123,848	17,956
Total liabilities		201,388	406,189	58,892
Commitments and Contingencies	24			

EHANG HOLDINGS LIMITED
CONSOLIDATED BALANCE SHEETS (CONTINUED)
(Amounts in thousands of Renminbi (“RMB”) and U.S. dollars (“US\$”),
except for number of shares and per share data)

	Note	As of December 31,		
		2021	2022	
		RMB	RMB	US\$ Note 2(e)
Shareholders' equity:				
Class A ordinary shares (US\$0.0001 par value; 1,904,577,337 shares authorized, 74,309,007 shares issued and 73,723,637 shares outstanding as of December 31, 2021; 1,904,577,337 shares authorized, 78,300,387 shares issued and 77,309,937 shares outstanding as of December 31, 2022)	19	50	51	8
Class B ordinary shares (US\$0.0001 par value; 45,422,663 shares authorized, 40,136,560 shares issued and outstanding as of December 31, 2021; 45,422,663 shares authorized, 39,026,560 shares issued and outstanding as of December 31, 2022)	19	25	24	3
Additional paid-in capital		1,459,374	1,558,356	225,940
Statutory reserves		1,191	1,191	173
Accumulated deficit		(1,122,153)	(1,450,374)	(210,284)
Accumulated other comprehensive (loss) income	19	(5,886)	15,010	2,176
Total EHang Holdings Limited shareholders' equity		332,601	124,258	18,016
Non-controlling interests		1,445	420	61
Total shareholders' equity		334,046	124,678	18,077
Total liabilities and shareholders' equity		535,434	530,867	76,969

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

EHANG HOLDINGS LIMITED
CONSOLIDATED STATEMENTS OF COMPREHENSIVE LOSS
(Amounts in thousands of Renminbi ("RMB") and U.S. dollars ("US\$"),
except for per share data and per ADS data)

	Note	For the year ended December 31,			
		2020	2021	2022	
		RMB	RMB	RMB	US\$
					Note 2(e)
Revenues:					
Products	15	176,060	54,923	40,775	5,912
Services	15	4,033	1,884	3,542	513
Total revenues		180,093	56,807	44,317	6,425
Cost of revenues:					
Products		(72,082)	(19,991)	(15,038)	(2,180)
Services		(1,832)	(786)	(60)	(9)
Total cost of revenues		(73,914)	(20,777)	(15,098)	(2,189)
Gross profit		106,179	36,030	29,219	4,236
Operating expenses:					
Sales and marketing expenses		(37,186)	(43,229)	(53,116)	(7,701)
General and administrative expenses		(61,613)	(187,388)	(151,065)	(21,902)
Research and development expenses		(105,252)	(137,148)	(135,082)	(19,585)
Total operating expenses		(204,051)	(367,765)	(339,263)	(49,188)
Other operating income		6,576	11,199	6,094	884
Operating loss		(91,296)	(320,536)	(303,950)	(44,068)
Other (expense) income					
Interest and investment income		3,795	5,143	4,669	677
Interest expenses		(2,337)	(1,803)	(3,819)	(554)
Foreign exchange loss		(333)	(827)	(1,488)	(216)
Other income		1,227	6,086	1,944	282
Other expenses		(3,127)	(1,549)	(26,804)	(3,886)
Total other (expense) income		(775)	7,050	(25,498)	(3,697)
Loss before income tax and income (loss) from equity method investment		(92,071)	(313,486)	(329,448)	(47,765)
Income tax expenses	17	(206)	(134)	(79)	(11)
Loss before income (loss) from equity method investment		(92,277)	(313,620)	(329,527)	(47,776)
Income (loss) from equity method investment		236	(276)	196	28
Net loss		(92,041)	(313,896)	(329,331)	(47,748)

EHANG HOLDINGS LIMITED
CONSOLIDATED STATEMENTS OF COMPREHENSIVE LOSS (CONTINUED)
(Amounts in thousands of Renminbi ("RMB") and U.S. dollars ("US\$"),
except for per share data and per ADS data)

	Note	For the year ended December 31,			
		2020	2021	2022	
		RMB	RMB	RMB	US\$
Net loss		(92,041)	(313,896)	(329,331)	Note 2(e) (47,748)
Net loss (income) attributable to non-controlling interests		4,422	(63)	1,110	161
Net loss attributable to EHang Holdings Limited's ordinary shareholders		(87,619)	(313,959)	(328,221)	(47,587)
Net loss per ordinary share:					
Basic and diluted	20	(0.80)	(2.78)	(2.86)	(0.41)
Net loss per ADS (2 ordinary shares equal to 1 ADS):					
Basic and diluted	20	(1.60)	(5.56)	(5.72)	(0.82)
Shares used in net loss per ordinary share computation (in thousands of shares):					
Basic and diluted	20	109,563	112,985	114,695	114,695
Other comprehensive (loss) income					
Foreign currency translation adjustments, net of nil tax	19	(9,974)	(6,107)	20,896	3,030
Unrealized (realized) gains on available-for-sale investments, net of nil tax	19	1,729	(1,729)	—	—
Total other comprehensive (loss) income, net of tax		(8,245)	(7,836)	20,896	3,030
Comprehensive loss		(100,286)	(321,732)	(308,435)	(44,718)
Comprehensive (loss) income attributable to non-controlling interests		4,422	(63)	1,110	161
Comprehensive loss attributable to EHang Holdings Limited		(95,864)	(321,795)	(307,325)	(44,557)

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

EHANG HOLDINGS LIMITED
CONSOLIDATED STATEMENTS OF CHANGES IN SHAREHOLDERS' EQUITY
(Amounts in thousands of Renminbi ("RMB") and U.S. dollars ("US\$"),
except for number of shares, per share data and per ADS data)

	Note	Class A ordinary shares		Class B ordinary shares		Additional paid-in capital RMB	Accumulated other comprehensive income RMB	Statutory reserves RMB	Accumulated deficit RMB	Total EHANG Holdings Limited shareholders' equity RMB	Non-controlling interests RMB	Total shareholders' equity RMB
		Number of ordinary shares	Amount RMB	Number of ordinary shares	Amount RMB							
Balance as of December 31, 2019		64,034,573	44	45,422,663	28	1,020,691	10,195	1,035	(720,419)	311,574	3,781	315,355
Issuance of Class A ordinary shares pursuant to underwriters' exercise of over-allotment option	19	170,062	—	—	—	5,751	—	—	—	5,751	—	5,751
Class B ordinary Shares converted to Class A ordinary shares	19	430,108	—	(430,108)	—	—	—	—	—	—	—	—
Net loss		—	—	—	—	—	—	—	(87,619)	(87,619)	(4,422)	(92,041)
Share-based compensation	16	—	—	—	—	54,857	—	—	—	54,857	—	54,857
Issuance of subsidiaries' equity to non-controlling interest holders		—	—	—	—	—	—	—	—	—	2,023	2,023
Other comprehensive loss	19	—	—	—	—	—	(8,245)	—	—	(8,245)	—	(8,245)
Balance as of December 31, 2020		<u>64,634,743</u>	<u>44</u>	<u>44,992,555</u>	<u>28</u>	<u>1,081,299</u>	<u>1,950</u>	<u>1,035</u>	<u>(808,038)</u>	<u>276,318</u>	<u>1,382</u>	<u>277,700</u>

EHANG HOLDINGS LIMITED
CONSOLIDATED STATEMENTS OF CHANGES IN SHAREHOLDERS' EQUITY (CONTINUED)
(Amounts in thousands of Renminbi ("RMB") and U.S. dollars ("US\$"),
except for number of shares and per share data)

		Class A ordinary shares		Class B ordinary shares		Additional paid-in capital RMB	Accumulated other comprehensive (loss) income RMB	Statutory reserves RMB	Accumulated deficit RMB	Total EHang Holdings Limited shareholders' equity RMB	Non-controlling interests RMB	Total shareholders' equity RMB
	Note	Number of ordinary shares	Amount RMB	Number of ordinary shares	Amount RMB							
Balance as of December 31, 2020		64,634,743	44	44,992,555	28	1,081,299	1,950	1,035	(808,038)	276,318	1,382	277,700
Issuance of Class A ordinary shares pursuant to a private placement	19	1,230,769	1	—	—	256,944	—	—	—	256,945	—	256,945
Issuance of ordinary shares to the depository bank	19	2,500,000	—	—	—	—	—	—	—	—	—	—
Issuance of ordinary shares for the vested restricted share units	19	3,002,130	2	—	—	—	—	—	—	2	—	2
Settlement of vested restricted share units with shares held by the depository bank	19	(1,914,630)	—	—	—	—	—	—	—	—	—	—
Class B ordinary shares converted to Class A ordinary shares	19	4,855,995	3	(4,855,995)	(3)	—	—	—	—	—	—	—
Net loss		—	—	—	—	—	—	—	(313,959)	(313,959)	63	(313,896)
Share-based compensation	16	—	—	—	—	121,131	—	—	—	121,131	—	121,131
Other comprehensive loss	19	—	—	—	—	—	(7,836)	—	—	(7,836)	—	(7,836)
Appropriation of statutory reserve		—	—	—	—	—	—	156	(156)	—	—	—
Balance as of December 31, 2021		74,309,007	50	40,136,560	25	1,459,374	(5,886)	1,191	(1,122,153)	332,601	1,445	334,046

EHANG HOLDINGS LIMITED
CONSOLIDATED STATEMENTS OF CHANGES IN SHAREHOLDERS' EQUITY (CONTINUED)
(Amounts in thousands of Renminbi ("RMB") and U.S. dollars ("US\$"),
except for number of shares and per share data)

		Class A ordinary shares		Class B ordinary shares		Additional paid-in capital	Accumulated other comprehensive (loss) income	Statutory reserves	Accumulated deficit	Total EHANG Holdings Limited shareholders' equity	Non-controlling interests	Total shareholders' equity
	Note	Number of ordinary shares	Amount RMB	Number of ordinary shares	Amount RMB	RMB	RMB	RMB	RMB	RMB	RMB	RMB
Balance as of December 31, 2021		74,309,007	50	40,136,560	25	1,459,374	(5,886)	1,191	(1,122,153)	332,601	1,445	334,046
Shares issued to depository bank	19	876,380	—	—	—	—	—	—	—	—	—	—
Issuance of Ordinary Shares for the vested Restricted Share Units	19	2,595,750	—	—	—	—	—	—	—	—	—	—
Settlement of vested Restricted Share Units with shares held by the depository bank	19	(590,750)	—	—	—	—	—	—	—	—	—	—
Class B ordinary shares converted to Class A ordinary shares	19	1,110,000	1	(1,110,000)	(1)	—	—	—	—	—	—	—
Net loss		—	—	—	—	—	—	—	(328,221)	(328,221)	(1,110)	(329,331)
Share based compensation	16	—	—	—	—	96,898	—	—	—	96,898	—	96,898
Clawback of shares under share incentive plan		—	—	—	—	(383)	—	—	—	(383)	—	(383)
Arrangement for employee stock withholding tax	19	—	—	—	—	(11,230)	—	—	—	(11,230)	—	(11,230)
Warrants arising from private placement	13	—	—	—	—	13,697	—	—	—	13,697	—	13,697
Issuance of a subsidiary's equity to a non-controlling interest holder		—	—	—	—	—	—	—	—	—	85	85
Other comprehensive loss		—	—	—	—	—	20,896	—	—	20,896	—	20,896
Balance as of December 31, 2022		78,300,387	51	39,026,560	24	1,558,356	15,010	1,191	(1,450,374)	124,258	420	124,678
Balance as of December 31, 2022 (US\$)	2(e)	78,300,387	8	39,026,560	3	225,940	2,176	173	(210,284)	18,016	61	18,077

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

EHANG HOLDINGS LIMITED
CONSOLIDATED STATEMENTS OF CASH FLOWS
(Amounts in thousands of Renminbi ("RMB") and U.S. dollars ("US\$"),
except for number of shares and per share data)

		For the years ended December 31,			
	Note	2020	2021	2022	
		RMB	RMB	RMB	US\$
					Note 2(e)
CASH FLOWS FROM OPERATING ACTIVITIES					
Net loss		(92,041)	(313,896)	(329,331)	(47,748)
Adjustments to reconcile net loss to net cash used in operating activities:					
Depreciation of property and equipment	8	5,785	7,427	8,478	1,229
Amortization of intangible assets		407	346	439	64
Amortization of right-of-use assets		—	—	11,976	1,736
Deferred income tax expense	17	184	—	—	—
Share-based compensation	16	54,857	121,131	96,898	14,049
Clawback of shares under share incentive plan		—	—	(383)	(56)
Loss on disposal of intangible assets		72	—	—	—
Loss (gains) on disposal of property and equipment	2(m)	456	820	(103)	(15)
Gain on disposal of long-term investment		(288)	—	—	—
Amortization of debt discounts		—	—	1,674	243
Interest and investment income	4	—	(1,367)	(3,131)	(454)
Loss (income) from an equity method investment		52	276	(196)	(28)
Impairment of long-lived assets	2(o)	—	1,627	—	—
Allowance for doubtful accounts		13,313	56,517	47,784	6,928
Write-downs of inventories	2(l)	—	2,640	956	139
Foreign exchange loss		—	827	1,488	216
Changes in operating assets and liabilities:					
Accounts receivable		(134,678)	39,336	(10,072)	(1,460)
Unbilled revenue	15	4,281	2,800	—	—
Cost and estimated earnings in excess of billings		13,495	—	—	—
Inventories		(29,269)	(38,607)	(3,257)	(473)
Prepayments and other current assets		(5,001)	(12,972)	(22,942)	(3,326)
Amounts due from a related party	18	(2,639)	1,279	1,360	197
Other non-current assets		(16,155)	—	—	—
Accounts payable		26,611	(7,748)	(10,104)	(1,465)
Contract liabilities		(2,426)	7,051	4,490	651
Accrued expenses and other liabilities		7,667	11,370	36,252	5,256
Lease liabilities		—	—	(8,783)	(1,273)
Deferred income		3,720	(60)	1,521	221
Deferred government subsidies		(80)	(430)	1,525	221
Income taxes payable		(5)	4	3	—
Unrecognized tax benefits	17	(14)	—	—	—
Net cash flow used in operating activities		(151,696)	(121,629)	(173,458)	(25,148)
CASH FLOWS FROM INVESTING ACTIVITIES					
Deconsolidation of a subsidiary		(54)	—	—	—
Purchase of short-term investments		(115,364)	(157,761)	(76,807)	(11,136)
Proceeds from maturities of short-term investments		71,996	140,756	151,388	21,949
Purchase of property and equipment		(8,742)	(15,645)	(12,166)	(1,764)
Proceeds from disposal of property and equipment		192	—	188	27
Acquisition of intangible assets		(337)	(51)	(1,653)	(240)
Cash paid for long-term investment	10	—	(700)	(4,550)	(660)
Loans to third parties		(53,900)	—	—	—
Repayment of loan to a third party		40,000	—	—	—
Net cash flow (used in) provided by investing activities		(66,209)	(33,401)	56,400	8,176

EHANG HOLDINGS LIMITED
CONSOLIDATED STATEMENTS OF CASH FLOWS (CONTINUED)
(Amounts in thousands of Renminbi ("RMB") and U.S. dollars ("US\$"),
except for number of shares and per share data)

		For the years ended December 31,			
	Note	2020	2021	2022	
		RMB	RMB	RMB	US\$ Note 2(e)
CASH FLOWS FROM FINANCING ACTIVITIES					
Proceeds from short-term bank loans	12	15,000	10,000	49,794	7,219
Repayment of short-term bank loans	12	(5,000)	(15,000)	(10,000)	(1,450)
Proceeds from long-term bank loans	12	—	20,000	—	—
Repayment of a Long-term bank loan	12	—	—	(3,000)	(435)
Repayment of loans from third parties		(2,000)	(5,000)	—	—
Proceeds from the private placement	13	—	—	69,861	10,129
Proceeds from mandatorily redeemable non-controlling interests of a subsidiary	14	40,000	—	—	—
Proceeds from issuance of a subsidiary's equity to a non-controlling interest holder		2,023	—	85	12
Shares issued upon vesting of restricted share units		—	2	—	—
Proceeds from issuance of Class A ordinary shares, net of issuance costs		7,313	256,945	—	—
Payment of underwriters' exercise of over-allotment option's issuance costs		(750)	—	—	—
Payment of issuance costs for IPO		(13,906)	—	—	—
Net cash provided by financing activities		42,680	266,947	106,740	15,475
Effect of exchange rate changes on cash, cash equivalents and restricted cash		(6,264)	(5,067)	12,605	1,828
Net (decrease) increase in cash, cash equivalents and restricted cash		(181,489)	106,850	2,287	332
Cash, cash equivalents and restricted cash at the beginning of the year		321,662	140,173	247,023	35,815
Cash, cash equivalents and restricted cash at the end of the year		140,173	247,023	249,310	36,147
Supplemental disclosures of cash flow information:					
Interest paid		342	1,178	1,502	218
Income taxes paid		40	342	79	11

EHANG HOLDINGS LIMITED
CONSOLIDATED STATEMENTS OF CASH FLOWS (CONTINUED)
(Amounts in thousands of Renminbi ("RMB") and U.S. dollars ("US\$"),
except for number of shares and per share data)

	Note	For the years ended December 31,			
		2020	2021	2022	US\$
		RMB	RMB	RMB	Note 2(e)
Non-cash investing and financing activities:					
Long-term loan from a third party settled by accounts receivable		—	25,000	—	—
Purchase of property and equipment included in Accrued expenses and other liabilities		4,967	1,228	3,327	482
Issuance costs for Series C redeemable convertible preferred shares included in Accrued expenses and other liabilities		48	—	—	—
Issuance costs for IPO included in Accrued expenses and other liabilities		821	—	—	—
Unpaid issuance costs for issuance of Class A ordinary shares pursuant to underwriters' exercise of overallotment option included in Accrued expenses and other liabilities		812	—	—	—
Reconciliation of cash, cash equivalents and restricted cash:					
Cash and cash equivalents		137,840	246,863	249,310	36,147
Restricted cash	2(g)	2,333	160	—	—
Total cash, cash equivalents and restricted cash in the statements of cash flows		140,173	247,023	249,310	36,147

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

EHANG HOLDINGS LIMITED
NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS
(Amounts in thousands of Renminbi (“RMB”) and U.S. dollars (“US\$”),
except for number of shares and per share data)

1. Organization and Nature of Operations

(a) Principal activities

EHang Holdings Limited (the “Company”) was incorporated in the Cayman Islands on December 23, 2014 under the Cayman Islands Companies Law as an exempted company with limited liability. On December 12, 2019, the Company completed its initial public offering (the “IPO”) and got listed on Nasdaq Global Market. The Company through its consolidated subsidiaries, variable interest entity (the “VIE”) and the subsidiaries of the VIE (collectively, the “Group”) are principally engaged in the manufacturing, sales and operations of autonomous aerial vehicles. The Group established its manufacturing facility in Yunfu City in the PRC.

(b) Principal subsidiaries and VIEs

As of December 31, 2022, the Company’s major subsidiaries, VIE and the subsidiaries of the VIE (“VIEs”, refer to VIE and its subsidiaries as a whole, where appropriate) are as follows:

<u>Entities</u> Subsidiaries:	<u>Date of incorporation establishment</u>	<u>Place of incorporation establishment</u>	<u>Percentage of direct or indirect ownership</u>		<u>Principal activities</u>
			Direct	Indirect	
Ehfly Technology Limited (“Ehfly”)	December 5, 2014	Hong Kong	100%	—	Product sales investment holding
EHang Intelligent Equipment (Guangzhou) Co., Ltd. (“EHang Intelligent” or the “WFOE”)	October 15, 2015	PRC	100%	—	Research and development, manufacturing and product sales
Yunfu EHang Intelligent Technology Limited (“EHang Yunfu”)	June 15, 2020	PRC	68.5%	—	Research and development, manufacturing and product sales
<u>Variable Interest Entity</u>					
Guangzhou EHang Intelligent Technology Co., Ltd. (“EHang GZ” or the “VIE”)	August 8, 2014	PRC	—	100%	Research and development, manufacturing and product sales

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1. Organization and Nature of Operations (Continued)

As of December 31, 2022, the Company's major subsidiaries and the VIEs are as follows (continued):

<u>Entities</u> VIE's Subsidiaries	<u>Date of incorporation establishment</u>	<u>Place of incorporation establishment</u>	<u>Percentage of direct or indirect ownership</u>		<u>Principal activities</u>
			Direct	Indirect	
Guangdong EHang General Aviation Co., Ltd. ("EHang Aviation")	March 11, 2021	PRC	—	100%(a)	Operational flight services

(a) EHang GZ and EHang Intelligent hold 51% and 49% equity interests in EHang Aviation, respectively.

Summary of the VIE contractual arrangements (the "VIE Contractual Agreements")

The Group conducts all of its business in China through its subsidiaries and the VIEs in the PRC. The Company's subsidiary EHang Intelligent, or the WFOE, has entered into contractual arrangements with the VIE and its shareholder described below, which are referred to as the VIE Contractual Agreements. As of December 31, 2019, the equity interests of the VIE were legally held by Mr. Huazhi Hu and Mr. Derrick Yifang Xiong (the "Former Shareholders"). For the year ended December 31, 2020, the Former Shareholders transferred their equity interests to Mr. Shuai Feng and Mr. Weixian Xia, both are the Group's employees (the "Nominee Shareholders"). The Nominee Shareholders then signed the Contractual Agreements with terms essentially the same as the ones signed before. Through the Contractual Agreements, the Nominee Shareholders of the VIE effectively assigned all of their voting rights underlying their equity interests in the VIE to the WFOE, which is a wholly-owned entity by the Company, who further assigned the voting rights underlying their equity interests in the VIE to the Company. Therefore, the Company has the power to direct the activities of the VIE that most significantly impact their economic performance. The Company also has the right to receive economic benefits via the WFOE, and the obligation to absorb losses of the VIE, that potentially could be significant to the VIE. Through the VIE Contractual Agreements, the Company is considered the primary beneficiary of the VIEs for accounting purposes only and thus consolidates each of these entities under ASC810-10, *Consolidation: Overall*.

The following is a summary of the Contractual Agreements among the Former Shareholders, the VIE and the WFOE, and then amended in 2020 to the Nominee Shareholders:

Loan Agreement

The WFOE has granted interest-free loans with an aggregate amount of RMB 60,000 to the Nominee Shareholders of the VIE for the sole purpose of providing funds necessary for the capital injection of the VIE. The loans are repayable by such Nominee Shareholder through a transfer of their equity interests in the VIE to the WFOE, in proportion to the amount of the loans to be repaid.

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1. Organization and Nature of Operations (Continued)

Summary of the VIE contractual arrangements (the “VIE Contractual Agreements”) (Continued)

Power of Attorney and Shareholders Voting Proxy

Pursuant to the Power of Attorney and Shareholders Voting Proxy entered into between the Nominee Shareholders, the VIE and the WFOE, the Nominee Shareholders authorized the WFOE to act on behalf of the Nominee Shareholders as exclusive agent and attorney with respect to all matters concerning the VIE’s equity interests, including but not limited to: (1) attend shareholders’ meetings of the VIE; (2) exercise all the shareholders’ rights, including voting rights; and (3) designate and appoint the senior management members of the VIE. The proxy is irrevocable and continuously valid from the date of execution. The WFOE is entitled to re-authorize or assign its rights related to the equity interest to any other person or entity at its own discretion and without giving prior notice to the Nominee Shareholders or obtaining their consents. In 2019, the WFOE reassigned its rights under the Power of Attorney and Shareholders Voting Proxy to the Company, pursuant to the Commitment Letter below.

Exclusive Option Agreements

Pursuant to the Exclusive Option Agreements entered amongst the Nominee Shareholders, the VIE and WFOE, the Nominee Shareholders granted to WFOE or their designees an irrevocable and exclusive right to purchase all or part of the equity interests held by the Nominee Shareholders in the VIE at the WFOE’s sole discretion, to the extent permitted under the PRC laws, at an amount equal to the minimum consideration permitted under the applicable PRC law and administrative regulations. Any proceeds received by the Nominee Shareholders from the exercise of the options shall be remitted to the WFOE or its designated party, to the extent permitted under PRC laws. In addition, the VIE and the Nominee Shareholders have agreed that without prior written consent of the WFOE, they will not create any pledge or encumbrance on their equity interests in the VIE, or transfer or otherwise dispose of their equity interests in the VIE. The term of the agreement remains effective as long as each Nominee Shareholder remains a shareholder of the VIE. The WFOE may terminate the agreement at its sole discretion, whereas under no circumstances may the VIE or the Nominee Shareholders terminate the agreement.

Exclusive Consulting and Service Agreement

Pursuant to the Exclusive Consulting and Service Agreement between the WFOE and the VIE, the WFOE has the exclusive right to provide services to the VIE related to the VIE’s and the VIE’s subsidiaries’ business, including but not limited to the development, manufacturing and sales of intelligent aerial vehicles. In return, the VIE agrees to pay a service fee equal to 100% of the consolidated net profits of the VIE after the VIE turns cumulative profitable and after certain expenses. The WFOE has sole discretion in determining the service fee charged to the VIE under this agreement. Without the WFOE’s prior written consent, the VIE shall not, directly and indirectly, obtain the same or similar services as provided under this agreement from any third party. The WFOE will have the exclusive ownership of all intellectual property rights developed by performance of this agreement. The Exclusive Consulting and Service Agreement is valid for 10 years and renewable at the WFOE’s option. This agreement can be terminated by the WFOE with 30 days’ notice at any time but cannot be terminated by the VIE unless the WFOE is found to be in gross negligence.

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1. Organization and Nature of Operations (Continued)

Summary of the VIE contractual arrangements (the “VIE Contractual Agreements”) (Continued)

Share Pledge Agreements

Pursuant to the Share Pledge Agreements entered amongst the WFOE and the Nominee Shareholders, the Nominee Shareholders pledged all of their equity interests in the VIE to the WFOE in favor of the WFOE to secure the VIE and their obligations under the various contractual agreements, including the Exclusive Consulting and Service Agreements and Exclusive Option Agreements described above. The WFOE shall have the right to collect dividends generated by the pledged equity interests during the term of the pledge. If the Nominee Shareholders breach their respective contractual obligations under the Share Pledge Agreements, the WFOE, as pledgee, will be entitled to rights, including the right to dispose of the pledged equity interests entirely or partially. The Nominee Shareholders of the VIE agree not to create any encumbrance on or otherwise transfer or dispose of their respective equity interests in the VIE, without the prior consent of the WFOE. The Share Pledge Agreements will remain effective until all the contractual obligations have been satisfied in full under all the agreements mentioned above. In March 2021, the Company has completed the registration of the share pledge with the relevant office of Administration for the Industry and Commerce in accordance with the PRC Property Rights Law.

Commitment Letter

Pursuant to the Commitment Letter, the WFOE irrevocably and unconditionally commits to execute its rights and obligations under the Power of Attorney and Shareholders Voting Proxy under the instruction of the Company. In addition, the Company is obligated and undertakes to provide unlimited financial support to the VIE, to the extent permissible under applicable PRC laws and regulations.

As of December 31, 2020, a judicial freeze was placed on the equity interests of the VIE in connection with an arbitration filed by a third party against Mr. Huazhi Hu, one of the Former Shareholders of the VIE. The arbitration arose from a financial dispute between the third party and Mr. Huazhi Hu, and was unrelated to the Group. The third party did not have any claim against the VIE. The VIE was named as a party in the arbitration only because the third party regarded equity interests of the VIE as potential assets of Mr. Huazhi Hu. The third party and Mr. Huazhi Hu reached a settlement and as a result, in March 2021, the third party filed a petition with the court and the judicial freeze on the VIE's equity interests has been released since then.

Based on the opinion of the Company's PRC legal counsel, (i) the ownership structure of the WFOE and the VIEs are in compliance with applicable PRC laws and regulations, (ii) such Contractual Agreements constitute valid, legal and binding obligations enforceable against each party of such agreements in accordance with the terms of each agreement, and will not result in any violation of PRC laws or regulations currently in effect.

However, uncertainties in the PRC legal system could cause the relevant regulatory authorities to find the current Contractual Agreements and businesses to be in violation of any existing or future PRC laws or regulations. If the Company, the WFOE or any of their current or future VIE are found in violation of any existing or future laws or regulations, or fail to obtain or maintain any of the required permits or approvals, the relevant PRC regulatory authorities would have broad discretion in dealing with such violations, which may include, but not limited to, revocation of business and operating licenses, being required to discontinue or restrict its business operations, restriction of the Group's right to collect revenues, being required to restructure its operations, imposition of additional conditions or requirements with which the Group may not be able to comply, or other regulatory or enforcement actions against the Group that could be harmful to its business. The imposition of any of these or other penalties may result in a material and adverse effect on the Group's ability to conduct its business. In addition, if the imposition of any of these penalties causes the Company to lose the rights to direct the activities of the VIE or the right to receive their economic benefits, the Company would no longer be able to consolidate the VIE.

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NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (CONTINUED)
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1. Organization and Nature of Operations (Continued)

The following financial statement balances and amounts of the Group's VIEs were included in the accompanying consolidated financial statements:

	As of December 31,		
	2021	2022	
	RMB	RMB	US\$
ASSETS			
Cash and cash equivalents	8,014	11,404	1,653
Accounts receivable, net	10,959	202	29
Inventories	839	837	121
Prepayments and other current assets	4,302	3,653	530
Amounts due from the Company and its subsidiaries	25,774	6,911	1,002
Property and equipment, net	2,032	1,273	185
Right-of-use assets, net	—	799	116
Intangible assets, net	77	229	33
Other non-current assets	97	39	6
Total assets	52,094	25,347	3,675
LIABILITIES			
Accounts payable	3,025	3,100	449
Contract liabilities	1,677	2,027	294
Current portion of long-term bank loans	1,000	5,154	747
Accrued expenses and current liabilities	18,053	19,712	2,858
Amounts due to the Company and its subsidiaries	45,991	55,451	8,040
Long-term bank loans	9,000	3,846	558
Unrecognized tax benefit	588	588	85
Lease liabilities	—	800	116
Total liabilities	79,334	90,678	13,147

EHANG HOLDINGS LIMITED
NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (CONTINUED)
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1. Organization and Nature of Operations (Continued)

The following financial statement balances and amounts of the Group's VIEs were included in the accompanying consolidated financial statements (continued):

	For the year ended December 31,			
	2020	2021	2022	
	RMB	RMB	RMB	US\$
Revenues	68,372	28,399	10,147	1,471
- Third-party revenue	35,280	230	6	1
- Inter-company revenue	33,092	28,169	10,141	1,470
Net profit (loss)	25,755	(8,534)	(38,091)	(5,523)
Net cash (used in) provided by operating activities	(5,118)	(3,482)	4,627	671
Net cash used in investing activities	(107)	(878)	(237)	(34)
Net cash provided by (used in) financing activities	—	5,000	(1,000)	(145)
Net (decrease) increase in cash, cash equivalents and restricted cash	(5,225)	640	3,390	492

Other than the amounts due to the Company and its subsidiaries (which are eliminated upon consolidation), all remaining liabilities of the VIE are without recourse to the primary beneficiary. The Company did not provide or intend to provide financial or other supports that are not previously contractually required to the VIEs during the years presented.

The revenue-producing assets that are held by the VIEs comprise mainly of permits, domain names, IP rights, operating licenses, intangible assets and fixed assets. The VIEs contributed an aggregate of 19.6%, 0.4% and 0.01% of the Group's consolidated revenues for the years ended December 31, 2020, 2021 and 2022, respectively, after elimination of inter-company transactions. The VIEs contributed RMB507, RMB36,371 and RMB47,683 (US\$6,913) of the Group's consolidated net loss for the years ended December 31, 2020, 2021 and 2022, respectively, after elimination of inter-company transactions. There are no consolidated VIE's assets that are pledged or collateralized for the VIE's obligations which can only be used to settle the VIE's obligations, except for the registered capital and the statutory reserves. Relevant PRC laws and regulations restrict the VIE from transferring a portion of its net assets, equivalent to the balance of its statutory reserves and its share capital, to the Company in the form of loans and advances or cash dividends (Note 21). Creditors of the VIE do not have recourse to the general credit of the Company for any of the liabilities of the VIE. There were no other pledges or collateralization of the VIE's assets.

(c) Liquidity and Going Concern

The Group has been incurring losses from operations since inception. The Group incurred net losses of RMB 92,041, RMB313,896 and RMB329,331 (US\$47,748) for the years ended December 31, 2020, 2021 and 2022, respectively. Accumulated deficit amounted to RMB1,122,153 and RMB1,450,374 (US\$210,284) as of December 31, 2021 and 2022, respectively. Net cash used in operating activities was RMB151,696, RMB121,629 and RMB173,458 (US\$25,148) for the years ended December 31, 2020, 2021 and 2022, respectively.

As of December 31, 2021 and 2022, the Group's balance of cash and cash equivalents was RMB 246,863 and RMB249,310 (US\$36,147), respectively. Up to the date of this report, the Group had unused loan facilities of RMB 10,000 with expiration date of February 9, 2024.

The Group's ability to continue as a going concern is currently largely dependent on when the Group will obtain the type certificate of its EH216-S in the near term to launch fully commercial sales of its EH216-S autonomous aerial vehicle, and raising additional funds through debt financings or equity offerings.

The Group's management expect to obtain the type certificate in the near future as the Group has completed majority of the compliance tests of the EH216-S as of the date of this report. However, there is uncertainty as to when the Group will obtain the type certificate of its EH216-S in the near term, which may materially and adversely affect the execution of management's business plan and the Company's future liquidity.

If the Group would be unsuccessful in obtaining the type certificate of EH216-S in a timely manner in the near term, or raising sufficient funds, the Group's management will continue to tighten its cash management, further undertake significant cost-cutting measures, adjust the pace of its R&D projects, expand revenues from smart city management solutions and aerial media solutions and utilize the unused loan facilities of RMB 10,000. This will help maintain the liquidity of the Group within the twelve-month period from the issuance date of these consolidated financial statements and provide additional time for the Group to obtain the type certificate of its EH216-S and raise sufficient funds.

Management has concluded, after giving consideration to its plans as noted above and existing balance of cash and cash equivalents as of December 31, 2022, that the Group has sufficient funds for sustainable operations and it will be able to meet its payment obligations from operations and debt related commitments for the next twelve months from the issuance of the consolidated financial statements. Accordingly the consolidated financial statements have been prepared on a going concern basis, which contemplates the realization of assets and satisfaction of liabilities during the normal course of operations.

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NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (CONTINUED)
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2. Summary of Significant Accounting Policies

(a) Basis of presentation

The accompanying consolidated financial statements have been prepared in accordance with the accounting principles generally accepted in the United States of America ("US GAAP") to reflect the financial position, results of operations and cash flows of the Group. Significant accounting policies followed by the Group in the preparation of the accompanying consolidated financial statements are summarized below.

(b) Principles of consolidation

The consolidated financial statements include the financial statements of the Company, its subsidiaries and the VIEs, for which the Company is the ultimate primary beneficiary. All significant inter-company transactions and balances between the Company, its subsidiaries, and the VIEs have been eliminated upon consolidation.

A subsidiary is an entity in which the Company, directly or indirectly, controls more than one half of the voting power: has the power to appoint or remove the majority of the members of the board of directors (the "Board"): to cast majority of votes at the meeting of the Board or to govern the financial and operating policies of the investee under a statute or agreement among the shareholders or equity holders.

A VIE is an entity in which the Company, or its subsidiary, through contractual arrangements, bears the risks of, and enjoys the rewards normally associated with, ownership of the entity, and therefore the Company or its subsidiary is the primary beneficiary of the entity. In determining whether the Company or its subsidiaries are the primary beneficiary, the Company considered whether it has the power to direct activities that are significant to the VIE's economic performance, and also the Company's obligation to absorb losses of the VIE that could potentially be significant to the VIE or the right to receive benefits from the VIE that could potentially be significant to the VIE.

(c) Use of estimates

The preparation of financial statements in conformity with US GAAP requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities at the balance sheet date and revenues and expenses during the reporting periods in the consolidated financial statements and accompanying notes. Significant estimates and assumptions reflected in the Group's consolidated financial statements include, but not limited to expected total costs of command-and-control revenue contracts, allowance for doubtful accounts, the determination of warranty cost, lower of cost and net realizable value of inventory, useful lives of long-lived assets, impairment of long-lived assets, valuation allowance for deferred tax assets, uncertain tax positions, fair value of the warrants and short-term debt, fair value of share-based awards and fair value of financial instruments. Management bases the estimates on historical experience and on various other assumptions that are believed to be reasonable, the results of which form the basis for making judgments about the carrying values of assets and liabilities. Changes in facts and circumstances may result in revised estimates. Actual results could differ from those estimates, and as such, differences may be material to the consolidated financial statements.

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NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (CONTINUED)
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2. Summary of Significant Accounting Policies (Continued)

(d) Foreign currency

The functional currency of the Company, Ehfly, and EHANG Investment (HK) Limited ("EHang HK") is the United States dollar ("US\$"). The functional currency of EHang Holding GmbH ("EHang GmbH"), EHANG TECHNOLOGIES SPAIN & LATAM, S.L. ("EHang Spain") and Ehang EUROPE SAS ("EHang France") is the euro ("€"). The functional currency of the Company's PRC subsidiaries and the VIEs is the Renminbi ("RMB"). The Group uses the RMB as its reporting currency. The determination of the respective functional currency is based on the criteria set out by ASC 830, *Foreign Currency Matters*.

Transactions denominated in foreign currencies are re-measured into the functional currency at the exchange rates prevailing on the transaction dates. Monetary assets and liabilities denominated in foreign currencies are re-measured at the exchange rates prevailing at the balance sheet date. Non-monetary items that are measured in terms of historical cost in foreign currency are re-measured using the exchange rates at the dates of the initial transactions. Exchange gains and losses are included in the consolidated statements of comprehensive loss.

The financial statements of the Group' entities of which the functional currency is not RMB use the periodic average exchange rates and the exchange rate at the balance sheet date to translate the operating results and financial position, respectively. Translation differences are recorded in accumulated other comprehensive income (loss), a component of shareholders' (deficit) equity.

(e) Convenience translation

Amounts in US\$ are presented for the convenience of the reader and are translated at the noon buying rate of US\$1.00 to RMB 6.8972 as set forth in the H.10 statistical release of the U.S. Federal Reserve Board. No representation is made that the RMB amounts represent or could have been, or could be, converted, realized or settled into US\$ at that rate on December 30, 2022, or any other rate.

(f) Cash and cash equivalents

Cash and cash equivalents consist of cash on hand, deposits and highly liquid investments placed with bank and other financial institutions, which are unrestricted as to withdrawal or use, and which have original maturities of three months or less when purchased.

(g) Restricted cash

As of December 31, 2021, restricted cash amounting to RMB 160 mainly represents cash frozen by People's Court of Nansha District in Guangzhou city in request by a third-party plaintiff regarding a lawsuit against one of the Group's subsidiaries. The lawsuit has come to a sentence and the Company has fulfilled its obligation. The Company filed a request with the court to release the judicial freeze on the Group's cash which had been released in January 2022.

As of December 31, 2022, there was no restricted cash in the Group.

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2. Summary of Significant Accounting Policies (Continued)

(h) Short-term investments

All highly liquid investments with original maturities of greater than three months but less than twelve months, are classified as short-term investments. Investments that are expected to be realized in cash during the next twelve months are also included in short-term investments. As of December 31, 2021, the Group's short-term investments comprised of debt instruments issued by international financial institutions (Note 4). The Group accounts for short-term investments in accordance with ASC 320 ("ASC 320"), *Investments—Debt and Equity Securities*. The Group classifies its short-term investments as "held-to-maturity," "trading" or "available-for-sale," whose classification determines the respective accounting methods stipulated by ASC 320. Debt investments that the Group has the positive intent and ability to hold to maturity are classified as held-to-maturity and stated at amortized cost. Securities that are bought and held principally for the purpose of selling them in the near term are classified as trading. Unrealized holding gains and losses for trading securities are included in earnings. Debt investments not classified as trading or as held-to-maturity are classified as available-for-sale, which are reported at fair value, with unrealized gains and losses recorded in "Accumulated other comprehensive income (loss)". Dividend and interest income for all categories of short-term investments are included in earnings. Any realized gains or losses on the sale of the short-term investments are determined on a specific identification method, and such gains and losses are reflected in earnings during the period in which gains or losses are realized.

(i) Accounts receivable and allowance for doubtful accounts

Accounts receivable are carried at net realizable value. An allowance for doubtful accounts is recorded in the period when loss is probable based on an assessment of specific evidence indicating troubled collection, historical experience, accounts aging and other factors. Accounts receivable are written off after all collection effort has ceased.

(j) Loans receivable and allowance for credit loss

The long-term loans receivable represents the loans to third parties (Note 9). Such amount is recorded at the principal net of allowance for credit loss, if any, and includes accrued interest receivable as of the balance sheet date. The Group reviews and monitors the credit worthiness of the third parties. An allowance for credit loss is recorded in the period in which a loss is determined to be probable and the amount of the loss can be reasonably estimated. RMB1,704 (US\$247) of allowance for credit losses were incurred for the year ended December 31, 2022.

(k) Cost and estimated earnings in excess of billings

Design and construction of customized command-and-control center contracts generally extend over longer periods of time and revenue is recognized using the cost-to-cost method. The Group's right to receive payments depends on its performance in accordance with the contractual agreements. Billings are issued based on milestones specified in the contracts negotiated with customers. In general, there are five milestones: 1) signing of the contract, 2) delivery and acceptance of hardware, 3) completion of software integration into hardware and the related testing, 4) delivery and acceptance of a completed command-and-control center, and 5) expiration of the one-year warranty period. The amounts to be billed at each milestone are specified in the contract. The length of each interval between two continuous billings under a command-and-control center contract varies depending on the duration of the contract and the last billing to be issued for the contract is scheduled at the end of a warranty period.

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2. Summary of Significant Accounting Policies (Continued)

(k) Cost and estimated earnings in excess of billings (Continued)

Revenue in excess of billings on the contracts is recorded as costs and estimated earnings in excess of billings. Billings in excess of revenues recognized on the contracts are recorded as deferred income until the above revenue recognition criteria are met. The carrying value of the Group's costs and estimated earnings in excess of billings, net of the allowance for doubtful accounts, represents their estimated net realizable value. The Group recognizes an allowance for doubtful accounts on costs and estimated earnings in excess of billings when it is probable that it will not collect the amount and writes off any balances in the period when deemed uncollectible. The Group periodically reviews the status of contracts and decides how much of an allowance for doubtful accounts should be made based on factors surrounding the credit risk of customers and historical experience. The Group does not require collateral from its customers and does not charge interest for late payments by its customers.

As of December 31, 2021, the decrease in cost and estimated earnings in excess of billings was in accordance with the achievement of milestones in the pre-determined billing terms for command-and-control centers, corresponding RMB717 was reclassified from Cost and estimated earnings in excess of billings to Accounts receivable in 2021. As of December 31, 2022, there were no cost and estimated earnings in excess of billings.

(l) Inventories

Inventories are comprised of raw materials, work in progress and finished goods. The Group's raw materials consist of accessories and hardware parts used to produce autonomous aerial vehicles and hardware for building the command-and-control centers. Work in progress primarily consist of autonomous aerial vehicles and hardware parts in production which will be transferred into production cost when incurred. Finished goods consist of autonomous aerial vehicles. Cost is determined using the weighted average method and includes all costs to acquire and other costs to bring the inventories to their present location and condition. Inventories are stated at the lower of cost or net realizable value. This requires the determination of the estimated selling price of the vehicles less the estimated cost to convert inventory on hand into a finished product. Once inventory is written down, a new, lower-cost basis for that inventory is established and subsequent changes in facts and circumstances do not result in the restoration or increase in that newly established cost basis. Adjustments to reduce the cost of inventory to its net realizable value are made, if required, to record the decreases in sales prices, obsolescence or similar reductions in the estimated net realizable value. Inventory write-downs of RMB1,344, RMB2,640 and RMB956 (US\$139) were recognized in cost of revenues for the years ended December 31, 2020, 2021 and 2022.

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2. Summary of Significant Accounting Policies (Continued)

(m) Property and equipment, net

Plant and equipment are stated at cost and are depreciated using the straight-line method over the estimated useful lives of the assets, as follows:

Category	Estimated useful life	Residual value
Mold and tooling	2-5 years	0%
Office equipment	5 years	5%
Machinery and electronic equipment	3-10 years	5%
Transportation equipment	4 years	5%
Leasehold improvements	Shorter of lease term or the estimated useful lives of the assets	0%

Repair and maintenance costs are charged to expense as incurred, whereas the costs of renewals and betterments that extend the useful lives of property and equipment are capitalized as additions to the related assets. Retirements, sales and disposals of assets are recorded by removing the cost and accumulated depreciation from the asset and accumulated depreciation accounts with any resulting gain or loss reflected in the consolidated statements of comprehensive loss. The loss on the disposal of property and equipment amounting to RMB456 and RMB820 were recognized in other expenses for the years ended December 31, 2020 and 2021. The gain on the disposal of property and equipment amounting to RMB103 (US\$15) was recognized in other income for the year ended December 31, 2022.

Direct costs that are related to the construction of property and equipment and incurred in connection with bringing the assets to their intended use are capitalized as construction-in-progress.

Construction-in-progress is transferred to specific property and equipment accounts and commences depreciation when these assets are ready for their intended use.

(n) Intangible assets, net

Intangible assets consist of software, patents and trademarks. Intangible assets with finite lives, including software, patents and trademarks are carried at acquisition cost less accumulated amortization and impairment, if any. Finite lived intangible assets are tested for impairment if impairment indicators arise.

Amortization of intangible assets with finite lives are computed using the straight-line method over the estimated useful lives as below:

Category	Estimated useful life
Software	3-5 years
Patents and trademarks	5 years

The estimated useful lives of intangible assets with finite lives are reassessed if circumstances occur that indicate the original estimated useful lives have changed.

There are no intangible assets with indefinite lives for the years ended December 31, 2020, 2021 and 2022.

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(Amounts in thousands of Renminbi ("RMB") and U.S. dollars ("US\$"),
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2. Summary of Significant Accounting Policies (Continued)

(o) Impairment of long-lived assets other than goodwill

The Group evaluates its long-lived assets or asset group, including intangible assets with finite lives, for impairment whenever events or changes in circumstances (such as a significant adverse change to market conditions that will impact the future use of the assets) indicate that the carrying amount of an asset or a group of long-lived assets may not be recoverable. When these events occur, the Group evaluates for impairment by comparing the carrying amount of the assets to future undiscounted net cash flows expected to result from the use of the assets and their eventual disposition. If the sum of the expected undiscounted cash flow is less than the carrying amount of the assets, the Group would recognize an impairment loss based on the excess of the carrying amount of the asset group over its fair value. Fair value is generally determined by discounting the cash flows expected to be generated by the long-lived assets or asset group, when the market prices are not readily available. Nil, RMB 1,627 and nil impairment of long-lived assets were recognized for the years ended December 31, 2020, 2021 and 2022, respectively.

(p) Long-term investments

The Group's long-term investments consist of an equity investment without readily determinable fair value and an equity investment accounted for using the equity method.

Equity Investments without Readily Determinable Fair Values

According to ASC 321, the Group elected to use the measurement alternative to measure the investment at cost, less any impairment, plus or minus changes resulting from observable price changes in orderly transactions for identical or similar investments of the same issuer, if any. The Group's management regularly evaluates the impairment of its investments based on the performance and financial position of the investee as well as other evidence of estimated market values. Such evaluation includes, but is not limited to, reviewing the investee's cash position, recent financing, projected and historical financial performance, cash flow forecasts and current and future financing needs. An impairment loss is recognized in the consolidated statements of comprehensive loss equal to the excess of the investment's cost over its fair value at the balance sheet date of the reporting period for which the assessment is made. The fair value would then become the new cost basis of the investment.

Equity Investments Accounted for Using the Equity Method

Investments in equity investees represent investments in entities in which the Group can exercise significant influence but does not own a majority equity interest or control are accounted for using the equity method of accounting in accordance with ASC 323-10, *Investments-Equity Method and Joint Ventures: Overall* ("ASC 323-10"). Under the equity method, the Group initially records its investment at cost and prospectively recognizes its proportionate share of each equity investee's net profit or loss. The difference between the cost of the equity investee and the amount of the underlying equity in the net assets of the equity investee is recognized as goodwill included in long-term investments on the consolidated balance sheets. The Group evaluates its equity method investments for impairment under ASC 323-10. An impairment loss on equity method investments is recognized in the consolidated statements of comprehensive loss when the decline in value is determined to be other-than-temporary. No impairment was charged in any of the presented periods.

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2. Summary of Significant Accounting Policies (Continued)

(q) Fair value measurements of financial instruments

The Group applies ASC 820 (“ASC 820”), *Fair Value Measurements and Disclosures*. ASC 820 defines fair value, establishes a framework for measuring fair value and expands disclosures about fair value measurements. ASC 820 requires disclosures to be provided on fair value measurement.

ASC 820 establishes a three-tier fair value hierarchy, which prioritizes the inputs used in measuring fair value as follows:

Level 1 — Observable inputs that reflect quoted prices (unadjusted) for identical assets or liabilities in active markets.

Level 2 — Other inputs that are directly or indirectly observable in the marketplace.

Level 3 — Unobservable inputs which are supported by little or no market activity.

ASC 820 describes three main approaches to measuring the fair value of assets and liabilities: (1) market approach; (2) income approach; and (3) cost approach. The market approach uses prices and other relevant information generated from market transactions involving identical or comparable assets or liabilities. The income approach uses valuation techniques to convert future amounts to a single present value amount. The measurement is based on the value indicated by current market expectations about those future amounts. The cost approach is based on the amount that would currently be required to replace an asset.

When available, the Group uses quoted market prices to determine the fair value of an asset or liability. If quoted market prices are not available, the Group will measure fair value using valuation techniques that use, when possible, current market-based or independently sourced market parameters.

The Group's financial instruments primarily consist of cash and cash equivalents, restricted cash, short-term investments, loans receivable, accounts receivable and payable, other current assets, bank loans, short-term debt, accrued expenses and other liabilities and mandatorily redeemable non-controlling interests. The carrying values of these financial instruments, except for short-term debt, long-term loans and mandatorily redeemable non-controlling interests, are approximated to their fair values due to their short-term maturities.

As of December 31, 2021, Financial assets that are measured at fair value on a recurring basis consist of a debt investment, which was classified within Level II of the fair value hierarchy because the quoted market price of underlying asset is not fully observable. As of December 31, 2022, the Group had no financial assets that are measured at fair value.

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2. Summary of Significant Accounting Policies (Continued)

(r) Revenue recognition

The Group's revenues are primarily derived from the sale of Autonomous Aerial Vehicles (“AAVs”) and related commercial solutions, mainly including air mobility solutions, smart city management solutions, and aerial media solutions.

The Group enters into legally enforceable and binding agreements with its customers with fixed terms and conditions, including pricing. The Group recognizes revenue at the amount to which it expects to be entitled when control of the products or services are transferred to its customers. Revenues are presented net of taxes collected on behalf of the government.

When either party to a contract has performed, the Group presents the contract in the consolidated balance sheets as a contract asset or a contract liability, depending on the relationship between the entity's performance and the customer's payment.

A contract asset is the Group's right to consideration in exchange for goods and services that the Group has transferred to a customer when the consideration is conditioned other than the passage of time, which is recorded as unbilled revenue. A receivable is recorded when the Group has an unconditional right to consideration. A right to consideration is unconditional if only the passage of time is required before payment of that consideration is due.

If a customer pays consideration or the Group has a right to an amount of consideration that is unconditional, before the Group transfers a good or service to the customer, the Group presents the contract liability when the payment is made or a receivable is recorded (whichever is earlier). A contract liability is the Group's obligation to transfer goods or services to a customer for which the Group has received consideration (or an amount of consideration is due) from the customer. The Group's contract liabilities primarily result from the advance received of sales of AAVs and related commercial solutions, which are recognized as revenue based on the consumption of the services or the delivery of the goods.

The Group generally does not separately bill its customers for shipping and handling fees and charges. The Group elects to record the costs incurred for shipping and handling in “sales and marketing expenses” in its consolidated statements of comprehensive loss. The shipping and handling costs for the years ended December 31, 2020, 2021 and 2022 were RMB1,409, RMB1,067 and RMB848 (US\$123), respectively.

Practical Expedients

The transaction price allocated to the performance obligations that are unsatisfied, or partially unsatisfied, has not been disclosed as substantially all of the Group contracts have a duration of one year or less.

Air mobility solutions

Revenues from air mobility solutions are primarily product revenues from the sales of passenger-grade AAVs based on firm customer orders with fixed terms and conditions, including pricing, net of discounts, if any. The performance obligation under the contract is the delivery of passenger-grade AAVs, which is satisfied at a point in time, in general upon the Group's receipt of acknowledgement receipts from customers or under some circumstances upon the products have been shipped to the contractually agreed location when the products are sold to customers outside PRC. The Group only provides the right of return for defective goods in connection with its warranty policy which is accounted for as an assurance-type warranty (Note 11). For the extended warranty beyond the standard policy, the Group considers it provides a level of protection beyond defects that existed at the time and accounts it as a separate performance obligation.

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2. Summary of Significant Accounting Policies (Continued)

(r) Revenue recognition (Continued)

The Group also sells software components of the passenger-grade AAVs. As the hardware and software components are highly interdependent, the entire bundle of promised goods is considered one performance obligation within the context of the contract. The single performance obligation is satisfied at a point in time, which is upon customer acceptance of the products.

Service revenues from air mobility solutions are primarily provision of logistics services which are satisfied over time.

Smart city management solutions

The Group enters into contracts with its customers for designing, building and delivering customized integrated command-and-control centers. The duration of the contracts depends on the contract size and ranges from three months to one year, excluding the duration of warranty accounted for as an assurance-type warranty (Note 11), which ranges from one year to three years. The Group provides a significant service of integrating goods and services including the project design, hardware and software promised in the contract into a combined output; therefore, the goods and services in the contracts are not distinct from each other and the Group determines there is one performance obligation, which is the delivery of the customized integrated command-and-control center. The performance obligation is satisfied, and control is transferred to the customer over time because there is no alternative use for the highly customized and integrated command-control-center and the Group has an enforceable right to payment for performance completed to date. The Group has determined the cost-to-cost method best depicts the measure of progress towards fulfilling the performance obligation. Under this method, revenue is recognized based on the estimated extent of progress, which is determined by dividing costs incurred to date by the total amount of costs expected to be incurred for designing, building and delivering a customized integrated command-and-control center. Revisions in the estimated total costs of command-and-control center contracts are made in the period in which the circumstances requiring the revision become known. Provisions, if any, are made in the period when anticipated losses become evident on uncompleted contracts.

The Group reviews and updates the estimated total costs of command-and-control center contracts periodically. The Group accounts for revisions to contract revenue and estimated total costs of command-and-control center contracts, in the period in which the facts that cause the revision become known as changes in estimates. Unapproved change orders are considered claims. Claims are recognized only when they have been awarded by customers.

Contract modifications, defined as changes in the scope or price (or both) of a contract that are approved by the parties to the contract, such as a contract amendment, exist when the parties to a contract approve a modification that either creates new or changes existing enforceable rights and obligations of the parties to the contract. Contract modifications, if any, will be accounting for as one of the following: (i) a separate contract; (ii) a termination of the existing contract and a creation of a new contract; or (iii) a combination of the preceding treatments. A contract modification is accounted for as a separate contract if the scope of the contract increases because of the addition of promised goods or services that are distinct and the price of the contract increases by an amount of consideration that reflects the Group's standalone selling prices of the additional promised goods or services. When a contract modification is not considered a separate contract and the remaining goods or services are distinct from the goods or services transferred on or before the date of the contract modification, the Group accounts for the contract modification as a termination of the existing contract and a creation of a new contract. When a contract modification is not considered a separate contract and the remaining goods or services are not distinct, the Group accounts for the contract modification as an add-on to the existing contract and as an adjustment to revenue on a cumulative catch-up basis.

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2. Summary of Significant Accounting Policies (Continued)

(r) Revenue recognition (Continued)

Aerial media solutions

The Group generates revenue by providing aerial media performance services and related products. Aerial media performance services allow multiple smart control-based drones to demonstrate and transform their formation to display diversified messages and images in specific airspace, that is tailor made based on different branding or advertising requirements. The Group uses self-produced drones and customizes the fleet formation performances based on customer's needs and availability of airspace approval in the area. The performance is usually completed within a day and revenue is recognized when the service is delivered.

The Group also sells hardware and software components of the aerial media performance drones. As the hardware and software components are highly interdependent, the entire bundle of promised goods is considered one performance obligation within the context of the contract. The single performance obligation is satisfied at a point in time, which is upon customer acceptance of the products.

Others

The Group generates other revenues mainly from stand-alone sales of consumer drones and their components and spare parts. Revenues are recognized when the consumer drones are shipped and the control of the drones are transferred to the customers. The Group started to phase out the consumer drone business in late 2016.

(s) Cost of revenue

Cost of revenue consists primarily of autonomous aerial vehicle material and manufacturing costs, construction costs of smart city management solutions, product warranty costs, provision for inventories, payroll, employee benefits, rental fees, depreciation and related costs of operations.

(t) Product warranty liability

The Group offers standard warranties to replace or repair defects on certain hardware parts of its passenger-grade AAVs for a period of six months to three years. The Group does not provide warranties to guarantee that the AAVs will perform as expected or in accordance with published specifications or provide expected benefits. The Group also provides a standard warranty for hardware and software for the command-and-control centers for a period ranging from one year to three years. The Group accrues for the estimated costs to repair or replace defective hardware parts and costs to assure software effectiveness as costs of revenues when revenue is recognized. The Group estimates its warranty costs by considering its historical experience of having to replace or repair hardware parts and for software de-bugging and the historical costs incurred have been insignificant to date. The estimates of warranties are inherently uncertain given the Group's relatively short history of sales, and changes to the Group's historical or projected warranty experience may cause material changes to the warranty reserve in the future. The Group reassesses whether warranty accruals are adequate based on actual experience as it becomes available and adjusts its estimates on a prospective basis.

Product warranty accrual is included in accrued expenses and other current liabilities (Note 11) and other non-current liabilities in the accompanying consolidated balance sheets.

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2. Summary of Significant Accounting Policies (Continued)

(u) Advertising expenditures

Advertising expenditures are expensed as incurred and are included in sales and marketing expenses, which amounted to RMB 1,965, RMB2,114 and RMB2,945 (US\$427) for the years ended December 31, 2020, 2021 and 2022, respectively.

(v) General and administrative expenses

General and administrative expenses consist primarily of payroll, employee benefits, share-based compensation, legal and other professional services fees, long-lived assets impairment, allowance for doubtful accounts, payroll and other general corporate related expenses.

(w) Research and development expenses

Research and development expenses include materials and supplies, payroll, employee benefits, share-based compensation and other operating expenses such as rent, depreciation and other related expenses.

The Group capitalizes costs to develop or obtain internal-use software and costs of significant upgrades and enhancements resulting in additional functionality of internal-use software in accordance with ASC 350-40 (“ASC 350-40”), *Internal-Use Software*. Costs incurred for internally developed internal-use software used for a particular research and development project are expensed as incurred, regardless of whether the software has alternative future uses. Costs incurred for maintenance, training, and minor modifications or enhancements are also expensed as incurred. Capitalized software development costs are amortized on a straight-line basis over the estimated useful life of the applicable software. Capitalized software development costs have not been material for the periods presented.

The Group also incurs cost to develop software embedded in its products. The software components cannot function or be sold separately from the AAV as a whole. The Group accounts for costs incurred in the development of software embedded in its products in accordance with ASC 985-20 (“ASC 985-20”), *Costs of Software to be Sold, Leased, or Marketed*. Such software development costs consist primarily of salaries and related payroll costs and are capitalized once technological feasibility is established, which is when a completed detail program design or in the absence of a completed detail program design, a working model of the product is available. As a result, capitalized software development costs were immaterial for the years ended December 31, 2020, 2021 and 2022.

(x) Leases

The Group leases facilities under non-cancellable operating leases expiring on different dates. On January 1, 2022, the Group adopted ASU No.2016-02 (Topic 842) “Leases” using the modified retrospective transition method. Results and disclosure requirements for reporting periods beginning after January 1, 2022 are presented under Topic 842, while prior period amounts have not been adjusted and continue to be reported in accordance with the Group’s historical accounting under Topic 840. Under Topic 842, lessees are required to recognize assets and liabilities on the balance sheet for most leases. A contract is or contains a lease if the contract conveys the right to control the use of identified property or equipment (an identified asset) for a period of time in exchange for consideration. The Group determines whether a contract conveys the right to control the use of an identified asset for a period of time by assessing whether the Group has both the right to obtain substantially all of the economic benefits from use of the identified asset and the right to direct the use of the identified asset.

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2. Summary of Significant Accounting Policies (Continued)

(x) Leases (Continued)

Based on the portfolio of leases as of December 31, 2021, a right-of-use asset of approximately RMB 24,670 and a lease liability of approximately RMB24,661 was recognized on the Group's consolidated balance sheet upon its adoption date of January 1, 2022, primarily relating to the rental of office and production facilities with terms of more than 12 months.

The Group has elected not to present short-term leases on the consolidated balance sheet as these leases have a lease term of 12 months or less at commencement date of the lease and do not include options to purchase or renew that the Group is reasonably certain to exercise. The Group accounts for short-term leases with terms less than 12 months in accordance with ASC 842-20-25-2 to recognize the lease payments in profit or loss on a straight-line basis over the lease term and variable lease payments in the period in which the obligation for those payments is incurred. The adoption of the standard did not have a significant impact on the Group's net assets and the consolidated statement of comprehensive loss.

Operating leases are included in right-of-use assets, current lease liabilities and non-current lease liabilities on the consolidated balance sheet. Renewal options are considered within the right-of-use assets and lease liability when it is reasonably certain that the Group will exercise that option.

The Group elected the package of practical expedients permitted under the transition guidance within the new standard, which allowed the Group to carry forward the historical determination of contracts as leases, lease classification and not reassess initial direct costs for historical lease arrangements. In addition, the Group also elected the practical expedient to apply consistently to all of the Group's leases to use hindsight in determining the lease term (that is, when considering lessee options to extend or terminate the lease and to purchase the underlying asset) and in assessing impairment of the Group's right-of-use assets.

The Group has lease agreements with lease and non-lease components, and has elected to utilize the practical expedient to account for the non-lease components together with the associated lease component as a single combined lease component.

As most of the Group's leases do not provide an implicit rate, the Group uses its incremental borrowing rate based on the information available at lease commencement date in determining the present value of lease payments. The incremental borrowing rate is a hypothetical rate based on the Group's understanding of what its credit rating would be to borrow and resulting interest the Group would pay to borrow an amount equal to the lease payments in a similar economic environment over the lease term on a collateralized basis.

(i) Right-of-use assets

Right-of-use assets, which mainly comprise of office and production facilities, are initially measured at the present value of the lease payments. Amortization of the right-of-use assets is made over the lease term on a generally straight-line basis.

(ii) Lease liabilities

Lease liabilities are lessees' obligations to make the lease payments arising from a lease, measured on a discounted basis.

As a lessee, the weighted average remaining lease terms of the right-of-use assets was 18 years and the discount rate for the lease is the rate implicit in the lease unless that rate cannot be readily determined. The weighted-average discount rate of the operating lease was 4.40%.

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2. Summary of Significant Accounting Policies (Continued)

(x) Leases (Continued)

For the year ended December 31, 2022, operating lease cost and short-term lease cost were RMB 13,986 (US\$2,028) and RMB305 (US\$44), respectively. There was no other lease cost other than operating lease cost and short-term lease cost for the year ended December 31, 2022. For the year ended December 31, 2022, cash paid for operating leases included in operating cash flows was RMB11,164. For the year ended December 31, 2022, leased assets obtained in exchange for operating lease liabilities was RMB 64,869 (US\$9,405).

A maturity analysis of the Company's operating lease liabilities and reconciliation of the undiscounted cash flows to the operating lease liabilities recognized on the consolidated balance sheet was as below:

	Office and production facilities rental	
	RMB	US\$
2023	5,632	817
2024	4,290	622
2025	4,982	721
2026	6,448	935
2027	6,817	988
2028 and thereafter	88,136	12,779
Minimum lease payments	116,305	16,862
Less: imputed interest	(40,872)	(5,926)
Present value of lease liabilities	75,433	10,936
Less: Current portion	(5,520)	(800)
Non-current portion of lease liabilities	69,913	10,136

As of December 31, 2021, future minimum lease payments under non-cancellable operating leases with initial terms in excess of one year consisted of the following:

	Office and production facilities rental
	RMB
2022	11,530
2023	5,926
2024	791
2025	1,252
2026	2,635
2027 and thereafter	4,612
Total	26,746

For the years ended December 31, 2020 and 2021, the Group recognized operating lease expenses for all operating leases of RMB9,019 and RMB10,460, respectively, under ASC 840.

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2. Summary of Significant Accounting Policies (Continued)

(y) Government subsidies

Government subsidies primarily consist of financial subsidies received from provincial and local governments for operating a business in their jurisdictions and compliance with specific policies promoted by the local governments. There are no defined rules and regulations to govern the criteria necessary for companies to receive such benefits, and the amount of financial subsidy is determined at the discretion of the relevant government authorities. The government subsidies of operating nature with no further conditions to be met are recorded in “other operating income” when received. The government subsidies with certain operating conditions are recorded as “deferred government subsidies” on the consolidated balance sheets when received and are recorded as operating income when the conditions are met.

On January 1, 2022, the Group adopted ASU No. 2021-10, Government Assistance (Topic 832). This ASU requires business entities to disclose information about government assistance they receive if the transactions were accounted for by analogy to either a grant or a contribution accounting model. The disclosure requirements include the nature of the transaction and the related accounting policy used, the line items on the balance sheets and statements of operations that are affected and the amounts applicable to each financial statement line item and the significant terms and conditions of the transactions. The disclosure requirements can be applied either retrospectively or prospectively to all transactions in the scope of the standard that are reflected in the financial statements at the date of initial application and new transactions that are entered into after the date of initial application. The adoption of the standard did not have a material impact on the Group’s consolidated balance sheets and the consolidated statements of comprehensive loss.

(z) Income taxes

The Group follows the liability method of accounting for income taxes in accordance with ASC 740 (“ASC 740”), *Income Taxes*. Under this method, deferred tax assets and liabilities are determined based on the difference between the financial reporting and tax bases of assets and liabilities using enacted tax rates that will be in effect in the period in which the differences are expected to reverse. The Group records a valuation allowance to offset deferred tax assets if based on the weight of available evidence, it is more-likely-than-not that some portion, or all, of the deferred tax assets will not be realized. The effect on deferred taxes of a change in tax rate is recognized in tax expense in the period that includes the enactment date of the change in tax rate.

The Group accounted for uncertainties in income taxes in accordance with ASC 740. Interest and penalties arising from underpayment of income taxes shall be computed in accordance with the related PRC tax law. The amount of interest expense is computed by applying the applicable statutory rate of interest to the difference between the tax position recognized and the amount previously taken or expected to be taken in a tax return. Interest and penalties recognized in accordance with ASC 740 are classified in the consolidated statements of comprehensive loss as income tax expense.

(aa) Share-based compensation

The Group applies ASC 718 (“ASC 718”), *Compensation—Stock Compensation* to account for its employee share-based payments. In accordance with ASC 718, the Group determines whether an award should be classified and accounted for as a liability award or an equity award. All of the Group’s share-based awards granted to employees were classified as equity awards.

The Group has elected to recognize compensation expense using the straight-line method for share-based awards granted with service conditions that have a graded vesting schedule. Prior to the completion of the IPO, with the assistance of an independent third-party valuation firm, the group determined the grant date fair value of the awards granted to employees. Subsequent to the completion of the IPO, share-based awards granted were measured based on the fair value of ordinary share as of grant date. The Group accounts for forfeitures as they occur.

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2. Summary of Significant Accounting Policies (Continued)

(aa) Share-based compensation (Continued)

A change in any of the terms or conditions of share-based payment awards is accounted for as a modification of awards. The Group measures the incremental compensation cost of a modification as the excess of the fair value of the modified awards over the fair value of the original awards immediately before its terms are modified, based on the share price and other pertinent factors at the modification date. For vested awards, the Group recognizes incremental compensation cost in the period the modification occurred. For unvested awards, the Company recognizes, 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. If the fair value of the modified award is lower than the fair value of the original award immediately before modification, the minimum compensation cost the Group recognizes is the cost of the original award.

The Group doesn't reflect reload features and contingent features in the grant-date fair value of an equity award. Reload features and contingent features are that require a grantee to transfer equity shares earned, or realized gains from the sale of equity instruments earned, to the issuing entity for consideration that is less than fair value on the date of transfer (including no consideration), such as a claw back feature. The Group accounted for these features if and when the contingent event occurs by recognizing the consideration received in the corresponding balance sheet account and a credit in the income statement equal to the lesser of the recognized compensation cost of the share-based payment arrangement that contains the contingent feature and the fair value of the consideration received, and debits in additional paid-in capital, and treasury shares, if any.

(ab) Employee benefit expenses

Full time employees of the Group in the PRC participate in a government mandated multi-employer defined contribution plan pursuant to which certain pension benefits, medical care, unemployment insurance, employee housing fund, maternity insurance and employment injury insurance are provided to employees. Chinese labor regulations require that PRC subsidiaries and VIEs of the Group make contributions to the government for these benefits based on certain percentages of the employees' salaries. The Group has no legal obligation for the benefits beyond the contributions. The total expenses the Group incurred for the plan were RMB4,022, RMB10,262 and RMB12,361 (US\$1,792) for the years ended December 31, 2020, 2021 and 2022, respectively.

(ac) Statutory reserve

The Group's PRC entities are required to make appropriations to certain non-distributable reserve funds.

In accordance with the laws applicable to China's Foreign Investment Enterprises, the Group's subsidiaries registered as WFOEs have to make appropriations from its after-tax profit (as determined under the Accounting Standards for Business Enterprises as promulgated by the Ministry of Finance of the People's Republic of China ("PRC GAAP")) to reserve funds including general reserve fund, and staff bonus and welfare fund. The appropriation to the general reserve fund must be at least 10% of the after-tax profits calculated in accordance with PRC GAAP. Appropriation is not required if the reserve fund has reached 50% of the registered capital of the company. Appropriation to the staff bonus and welfare fund is at the company's discretion.

In addition, in accordance with the Company Laws of the PRC, the Group's entities registered as PRC domestic companies must make appropriations from its after-tax profit as determined under the PRC GAAP to non-distributable reserve funds including a statutory surplus fund and a discretionary surplus fund. The appropriation to the statutory surplus fund must be at least 10% of the after-tax profits as determined under the PRC GAAP. Appropriation is not required if the surplus fund has reached 50% of the registered capital of the company. Appropriation to the discretionary surplus fund is made at the discretion of the company.

The use of the general reserve fund, statutory surplus fund and discretionary surplus fund are restricted to the off-setting of losses or increasing capital of the respective company. The staff bonus and welfare fund are a liability in nature and is restricted to fund payments of special bonus to staff and for the collective welfare of employees. All these reserves are not allowed to be transferred to the Company in terms of cash dividends, loans or advances, nor can they be distributed except under liquidation.

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2. Summary of Significant Accounting Policies (Continued)

(ac) Statutory reserve (Continued)

For the year ended December 31, 2020, 2021 and 2022, appropriations to general reserve fund and statutory surplus fund amounted to nil, RMB156 and nil respectively.

(ad) Comprehensive income (loss)

Comprehensive income (loss) is defined as the changes in equity of the Group during a period from transactions and other events and circumstances excluding transactions resulting from investments by owners and distributions to owners. Among other disclosures, ASC 220, *Comprehensive Income*, requires that all items that are required to be recognized under current accounting standards as components of comprehensive income (loss) be reported in a financial statement that is displayed with the same prominence as other financial statements. For each of the periods presented, the Group's comprehensive income (loss) includes net loss, foreign currency translation adjustments and unrealized and realized gains on available-for-sale debt securities and is presented in the consolidated statements of comprehensive loss.

(ae) Dividends

Dividends are recognized when declared. No dividends were declared for the years ended December 31, 2020, 2021 and 2022, respectively.

(af) Loss per share

In accordance with ASC 260 ("ASC 260"), *Earnings per Share*, basic loss per share is computed by dividing net loss attributable to ordinary shareholders by the weighted average number of ordinary shares outstanding during the period using the two-class method. Under the two-class method, net loss is allocated between ordinary shares, and other participating securities based on their participating rights.

For the years ended December 31, 2020, 2021 and 2022, the two-class method is applicable because the Group has two classes of ordinary shares outstanding, Class A and Class B ordinary shares, respectively. The participating rights (liquidation and dividend rights) of the holders of the Company's Class A and Class B ordinary shares are identical, except with respect to voting and conversion (Note 19). As a result, and in accordance with ASC 260, the undistributed loss for each year is allocated based on the contractual participation rights of the Class A and Class B ordinary shares, respectively. As the liquidation and dividend rights are identical, the undistributed loss is allocated on a proportionate basis.

Ordinary equivalent shares consist of unvested restricted shares units, and ordinary shares issuable upon the exercise of outstanding share options (using the treasury stock method). Ordinary equivalent shares are excluded from the computation of diluted loss per share for all periods presented as their effects would be anti-dilutive.

(ag) Short-term debt

In December 2022, the Group entered into a share purchase agreement (the "SPA") with an investor (the "Investor") to issue predetermined number of Class A ordinary shares (the "Underlying Shares") of the Company, at a fixed consideration in US\$ (the "Private Placement"), upon meeting the specified preconditions, of which the substantial one is the Investor obtaining the Outbound Direct Investment ("ODI") approval.

In December 2022, a transitional agreement has been reached to supplement the Private Placement (the "Supplemental Agreement"), according to which before the ODI approval, the Investor provided RMB proceeds (the "RMB Proceeds") as an interim funding, equivalent to consideration in U.S. dollar of the Private Placement, to the designated subsidiary of the Company.

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2. Summary of Significant Accounting Policies (Continued)

(ag) Short-term debt (Continued)

The RMB Proceeds and associated subsequent repayment obligation was accounted for as a liability to the Company, since:

- (i) The RMB Proceeds are a loan provided by the Investor to the subsidiary of the Company under the Supplemental Agreement. The Investor is entitled to receive the money back after at least three months if the ODI approval is not obtained due to force majeure or other situations agreed by the Company and Investor.
- (ii) It is within the Investor's control that it can stop pursuing the ODI approval, and therefore it can make the repayment obligation to happen.
- (iii) Upon the occurrence of dissolution, windup or liquidation of the onshore subsidiary, the Investor could claim its creditor right in accordance with PRC bankruptcy law.

Therefore the instrument is accounted for as a short-term debt under ASC 470, *Debt*.

(ah) Warrants

According to the SPA, the Company issued a purchase right to the Investor under which the Company will issue predetermined ordinary shares for a fixed cash consideration at a future date (the "Warrants").

The Warrants were accounted for as equity instruments to the Company, since:

- i) The Warrants were indexed to the Company's own stock, since:
 - The Warrants will be exercised upon the ODI approval, which is not based on an observable market, or an observable index.
 - The exercise price is fixed by the SPA and Supplement Agreement, and the number of Underlying Shares to be issued is also fixed divided by the fixed purchase price per share.
- ii) The Warrants were classified in shareholders' equity, since:
 - The Warrants will be settled only by gross physical delivery of ordinary shares by the Company.
 - The Company has the ability to settle the Private Placement in ordinary shares.
 - The number of Underlying Shares to be issued is explicitly fixed at the total consideration divided by the fixed purchase price per share, with no adjustment provision.
 - No requirement for cash settlement in the agreements.
 - There are no cash settled top-off or make-whole provisions.

The Group received the Proceeds and issued short-term debt and Warrants in a bundled transaction in 2022. The RMB Proceeds shall be allocated to the two elements based on the relative fair values of the debt instrument without the Warrants and of the Warrants themselves at time of issuance. The portion of the RMB Proceeds so allocated to the Warrants shall be accounted for as additional paid-in capital. The remainder of the proceeds shall be allocated to the debt instrument portion of the transaction, the short-term debt. This results in a discount which shall be accounted for as interest expense in the following three months.

On January 1, 2022, The Group has elected to early adopt the ASU No. 2020-06, *Debt—Debt with Conversion and Other Options* (Subtopic 470-20) and *Derivatives and Hedging—Contracts in Entity's Own Equity* (Subtopic 815-40): *Accounting for Convertible Instruments and Contracts in an Entity's Own Equity* (ASU 2020-06), which simplifies the accounting for convertible instruments by reducing the number of accounting models available for convertible debt instruments. This adoption of the new guidance had no material impact on the treatment of the Warrants or Short-term debt in Note 2(ag).

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2. Summary of Significant Accounting Policies (Continued)

(ai) Segment reporting

In accordance with ASC 280 ("ASC 280"), *Segment Reporting*, operating segments are defined as components of an enterprise about which separate financial information is available that is evaluated regularly by the chief operating decision maker ("CODM"), or decision-making group, in deciding how to allocate resources and in assessing performance. The Group's Chief Executive Officer as the CODM reviews the consolidated financial results when making decisions about allocating resources and assessing the performance of the Group as a whole and hence, the Group has only one reportable segment. The Group's long-lived assets are substantially all located in the PRC.

The following table presents revenue by customer incorporation location for the years ended December 31, 2020, 2021 and 2022, respectively:

	For the year ended December 31,					
	2020		2021		2022	
	RMB	%	RMB	%	RMB	US\$ %
PRC	164,153	91%	49,683	87%	33,975	4,926 77%
West Asia	2,124	1%	—	—	4,630	671 10%
Europe	2,388	1%	2,199	4%	2,638	382 6%
East Asia	4,550	3%	4,404	8%	798	116 2%
Other	6,878	4%	521	1%	2,276	330 5%
Total net revenues	<u>180,093</u>	<u>100%</u>	<u>56,807</u>	<u>100%</u>	<u>44,317</u>	<u>6,425 100%</u>

(aj) Development and purchase cooperative arrangement

In April 2016, the Group entered into a development and purchase cooperative arrangement with a U.S. biotechnology company ("Biotech Customer") to design, develop, test-run and manufacture an organ transport e-helicopter system, which includes an operational interface with air traffic control, associated customized passenger-grade AAVs and recharging infrastructure. The Biotech Customer is responsible for obtaining the approvals of the Federal Aviation Administration ("FAA") and the Food and Drug Administration ("FDA") relating to the import and operations of the AAV products. Upon the Group's achievement of agreed-upon milestones in the agreement, Biotech Customer will make investments of US\$14,000 and payments totaling US\$36,000. The agreement may be terminated at Biotech Customer's discretion upon written notice. In February 2019, although the first milestone was not yet achieved, the Group and the Biotech Customer entered into an amendment whereby the Biotech Customer made the initial investment of US\$7,000 (RMB 48,733 equivalent) to subscribe for 1,189,397 Series C redeemable convertible preferred shares of the Company in full satisfaction of its obligation to invest in the Group following the successful attainment of the first milestone, and all other terms and conditions of the agreement remain unchanged. As of December 31, 2022, none of the milestones have been achieved and the agreement, as amend, remains in effect.

As part of the same arrangement, the Group may sell 1,000 units of customized AAVs with the organ transport e-helicopter system conforming to the functional specifications by the Biotech Customer for according to a 15-year delivery schedule subject to subsequent purchase amendments. Purchase orders are conditional on the Group achieving a number of performance milestones and the Biotech Customer obtaining required approvals from the FAA and FDA for the internal testing of the AAVs. In December 2018, two amendment contracts were signed to specify the sale of five units of passenger-grade AAVs by the Group to the Biotech Customer for the latter's testing and training purposes in partial satisfaction of the original agreement. For the years ended December 31, 2020, 2021 and 2022, three, zero and zero units of the AAVs were delivered, respectively. Because the Biotech Customer purchased these AAVs as a customer, the Group accounted for the sales of individual AAVs as separate units of account for which revenue from air mobility solutions of RMB5,137, nil and nil were recorded for the years ended December 31, 2020, 2021 and 2022, respectively under ASC 606 following the revenue recognition policy noted above.

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2. Summary of Significant Accounting Policies (Continued)

(ak) Recent accounting pronouncements

The Company is an emerging growth company (“EGC”) as defined by the Jumpstart Our Business Startups Act (“JOBS Act”). The JOBS Act provides that an EGC can take advantage of an extended transition period for complying with new or revised accounting standards. This allows an EGC to delay adoption of certain accounting standards until those standards would otherwise apply to private companies. The Group elected to take advantage of the extended transition period. However, this election will not apply should the Group cease to meet the definition of an EGC.

In June 2016, the FASB issued ASU 2016-13 (“ASU 2016-13”), *Financial Instruments — Credit Losses* (Topic 326), Measurement of Credit Losses on Financial Instruments. ASU 2016-13 changes the impairment model for most financial assets and certain other instruments. The standard will replace the “incurred loss” approach with an “expected loss” model for instruments measured at amortized cost. For available-for-sale debt securities, entities will be required to record allowances rather than reduce the carrying amount, as they do today under the other-than-temporary impairment model. Per ASU 2019-10, ASU 2016-13 is effective for the Group for annual reporting periods beginning January 1, 2023, and interim periods within that year. Early adoption is permitted. In February 2020, the FASB issued ASU 2020-02, *Financial Instruments—Credit Losses* (Topic 326) and *Leases* (Topic 842) —Amendments to SEC Paragraphs Pursuant to SEC Staff Accounting Bulletin No. 119 and Update to SEC Section on Effective Date Related to Accounting Standards Update No. 2016-02, *Leases* (Topic 842). For *Credit Losses* (Topic 326), it added the accounting for loan losses by registrants engaged in lending activities subject to FASB ASC Topic 326. This staff interpretation applies to all registrants that are creditors in loan transactions that, individually or in the aggregate, have a material effect on the registrant’s financial condition. The Group will adopt the ASU with modified retrospective method on January 1, 2023, and the Group assessed that adoption of the ASU would have no material impact on the Group’s consolidated financial statements.

In October 2021, the FASB issued ASU No. 2021-08, *Business Combinations* (Topic 805): *Accounting for Contract Assets and Contract Liabilities from Contracts with Customers* (ASU 2021-08), which clarifies that an acquirer of a business should recognize and measure contract assets and contract liabilities in a business combination in accordance with Topic 606, *Revenue from Contracts with Customers*. The new guidance is effective for public business entities 1 for fiscal years beginning after December 15, 2022, including interim periods within those fiscal years. For all other entities, the new guidance is effective for fiscal years beginning after December 15, 2023, including interim periods within those fiscal years. The amendments should be applied prospectively to business combinations occurring on or after the effective date of the amendments, with early adoption permitted. The Group does not plan to early adopt ASU 2021-08 and the ASU is currently not expected have a material impact on the Group’s consolidated financial statements.

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2. Summary of Significant Accounting Policies (Continued)

(ak) Recent accounting pronouncements (Continued)

In March 2022, the FASB issued ASU 2022-02, Troubled Debt Restructurings and Vintage Disclosures. This ASU eliminates the accounting guidance for troubled debt restructurings by creditors that have adopted ASU 2016-13, Measurement of Credit Losses on Financial Instruments, which the Company will adopt on January 1, 2023. This ASU also enhances the disclosure requirements for certain loan refinancing and restructurings by creditors when a borrower is experiencing financial difficulty. In addition, the ASU amends the guidance on vintage disclosures to require entities to disclose current period gross write-offs by year of origination for financing receivables and net investments in leases within the scope of ASC 326-20. The ASU is effective for annual periods beginning after December 15, 2022, including interim periods within those fiscal years. Adoption of the ASU would be applied prospectively. Early adoption is also permitted, including adoption in an interim period. The Group will adopt this update on January 1, 2023 and does not expect the adoption to have a material impact to the Group's consolidated financial statements.

3. Concentration of Risks

(a) Concentration of credit risk

Financial instruments that potentially subject the Group to significant concentration of credit risk consist primarily of cash and cash equivalents, restricted cash, short-term investments. As of December 31, 2021, the aggregate amount of cash and cash equivalents, restricted cash and short-term investments of RMB36,825 were held at major financial institutions located in the PRC and RMB 275,306 were deposited with international financial institutions located outside the PRC, among which included short-term debt investments of RMB65,108 issued by a private equity fund outside the PRC that are mandatorily redeemable (Note 4). As of December 31, 2022, the aggregate amount of cash and cash equivalents RMB240,542 (US\$34,876) was held at major financial institutions located in the PRC and RMB8,768 (US\$1,271) was deposited with international financial institutions located outside the PRC. The maximum exposure of such assets to credit risk is their carrying amounts as of the balance sheet dates. Management believes that these financial institutions are of high credit quality and continually monitors the credit worthiness of these financial institutions. Historically, deposits in Chinese banks are secure due to the state policy on protecting depositors' interests. The Group selected reputable international financial institutions with high credit ratings to deposit its foreign currencies. The Company regularly monitors the credit ratings of the international financial institutions to avoid any potential defaults. In the event of bankruptcy of one of these financial institutions, the Group may not be able to claim its cash and demand deposits back in full. The Group continues to monitor the financial strength of the financial institutions. There has been no recent history of default in relation to these financial institutions.

(b) Business supplier risk

The Group relies on external supplies for raw materials and certain components and parts used in the Group's products. Some of the components for AAVs are currently selected to be purchased from a single source to improve cost-efficiency. As the result of the COVID-19 pandemic, the Group has experienced delayed fulfillments from suppliers in 2021. Disruption in the supply of components, whether or not from a single-source supplier, could temporarily disrupt commercial production of the Group's AAVs.

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3. Concentration of Risks (Continued)

(b) Business supplier risk (Continued)

Suppliers accounting for 10% or more of total purchases of materials were:

Supplier	As of December 31,		
	2021	2022	
	RMB	RMB	US\$
A	7,807	3,056	443
B	8,405	*	*
C	7,596	*	*

* less than 10% of total purchase of materials of the Group.

(c) Customer risk

The success of the Group's business going forward will rely in part on the Group's ability to continue to obtain and expand its business from existing customers while also attracting new customers. For the year end December 31, 2022, the majority of the Group's revenue generated from sales of passenger-grade AAVs are from a limited number of customers that mainly operate the AAVs on a limited trial basis in tourism locations in China, rather than in broad, mainstream commercial operations. The COVID-19 outbreak has had a particularly severe impact on the global tourism industry. Some customers have been materially adversely affected, which resulted in failing to make payments owed to the Group in a timely manner or at all. This may further result in these customers to ceasing purchases, canceling or reducing orders for the Group's products or services or failing to make payments owed to us in a timely manner or at all, which would materially and adversely impact the Group's business and result of operations.

External customers with 10% or more of the Group's revenues are:

Customer	For the year ended December 31,			
	2020	2021	2022	
	RMB	RMB	RMB	US\$
A	22,655	*	*	*
B	92,331	*	*	*
C	24,071	7,080	*	*
D	*	19,646	*	*
E	*	*	9,217	1,336
F	*	*	5,611	814
G	*	*	4,630	671

* less than 10% of total revenues of the Group.

As of December 31, 2021, accounts receivable (including the non-current portion recorded in other non-current assets), net of allowances, from the top three customers amounted to RMB32,385, accounting for 58% of the Group's total balance. As of December 31, 2022, accounts receivable, net of allowances, from the top two customers amounted to RMB8,095 (US\$1,174), accounting for 40% of the Group's total balance.

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3. Concentration of Risks (Continued)

(d) Currency convertibility risk

The Group primarily transacts its business in RMB, which is not freely convertible into foreign currencies. On January 1, 1994, the PRC government abolished the dual rate system and introduced a single rate of exchange as quoted daily by the People's Bank of China (the "PBOC"). However, the unification of the exchange rates does not imply that the RMB may be readily convertible into US\$ or other foreign currencies. All foreign exchange transactions continue to take place either through the PBOC or other banks authorized to buy and sell foreign currencies at the exchange rates quoted by the PBOC. Approval of foreign currency payments by the PBOC or other institutions requires submitting a payment application form together with suppliers' invoices, shipping documents and signed contracts.

(e) Foreign currency exchange rate risk

From July 21, 2005, the RMB is permitted to fluctuate within a narrow and managed band against a basket of certain foreign currencies. The functional currency and the reporting currency of the Company are the US\$ and the RMB, respectively. Most of the Group's revenues and costs are denominated in RMB, while a portion of cash and cash equivalents is denominated in U.S. dollars. Any significant revaluation of RMB may materially and adversely affect the Group's loss and shareholders' equity in U.S. dollars.

4. Short-term Investments

Short-term investments as of December 31, 2021 consisted of the following:

	As of December 31, 2021				
	Cost or Amortized cost RMB	Gross unrecognized holding gains RMB	Gross unrecognized holding losses RMB	Gross unrealized gains RMB	Gross unrealized losses RMB
Trading debt investments	63,741	1,367	—	—	—
	63,741	1,367	—	—	—
					65,108

The Group had no short-term investments as of December 31, 2022.

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4. Short-term Investments (Continued)

Trading debt investments include debt investments issued by a private equity fund outside the PRC amounting to RMB 65,108 as of December 31, 2021. The Company disposed of the debt investments in 2022.

For the years ended December 31, 2020, 2021 and 2022, the Group recognized interest and investment income of RMB 478, RMB1,818 and RMB2,771 (US\$402) from short-term investments, respectively.

For the year ended December 31, 2021, the realized gain on the available-for-sale debt investments held by the Group that was reclassified from Accumulative other comprehensive income to Interest and investment income amounted RMB1,729. There was no such reclassification in 2020 and 2022.

5. Accounts Receivable, Net

Accounts receivable, net, consisted of the following:

	As of December 31,		
	2021	2022	
	RMB	RMB	US\$
Accounts receivable	125,606	135,678	19,671
Allowance for doubtful accounts	(69,417)	(115,380)	(16,728)
	<u>56,189</u>	<u>20,298</u>	<u>2,943</u>

The movements in the allowance for doubtful accounts were:

	For the year ended December 31,			
	2020	2021	2022	
	RMB	RMB	RMB	US\$
Balance at the beginning of the year	(862)	(10,051)	(69,417)	(10,064)
Additional provision charged to expense	(9,217)	(59,347)	(46,045)	(6,676)
Foreign currency translation	28	(19)	82	12
Balance at the end of the year	<u>(10,051)</u>	<u>(69,417)</u>	<u>(115,380)</u>	<u>(16,728)</u>

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6. Inventories

Inventories consisted of the following:

	As of December 31,		
	2021	2022	
	RMB	RMB	US\$
Raw materials	62,462	49,127	7,123
Work in progress	17,134	4,939	716
Finished goods	27,168	28,188	4,087
Inventories, total	106,764	82,254	11,926
Inventories provision	(28,689)	(9,890)	(1,434)
	<u>78,075</u>	<u>72,364</u>	<u>10,492</u>

7. Prepayments and Other Current Assets

Prepayments and other current assets consisted of the following:

	As of December 31,		
	2021	2022	
	RMB	RMB	US\$
Prepayment for service	1,672	11,157	1,618
Unbilled revenue (Note 15)	—	10,800	1,566
Deductible value-added tax input	16,487	8,976	1,301
Prepayment for acquisition of inventories	8,286	6,910	1,002
Loans receivable – current portion (Note 9)	—	4,000	580
Staff advances	1,257	940	136
Others	1,693	2,400	347
	<u>29,395</u>	<u>45,183</u>	<u>6,550</u>

As of December 31, 2021 and 2022, the Group recorded the allowance for doubtful accounts of RMB 1,537 and RMB 1,655 (US\$240), respectively.

8. Property and Equipment, Net

	As of December 31,		
	2021	2022	
	RMB	RMB	US\$
Leasehold improvements	30,250	32,634	4,731
Machinery and electronic equipment	22,547	29,061	4,214
Transportation equipment	3,643	3,249	471
Office equipment	2,511	2,641	383
Construction in progress	1,720	1,885	273
Mold and tooling	—	2,290	332
	<u>60,671</u>	<u>71,760</u>	<u>10,404</u>
Less: accumulated depreciation	(25,223)	(23,240)	(3,369)
Less: accumulated impairment	(1,627)	(1,460)	(212)
	<u>33,821</u>	<u>47,060</u>	<u>6,823</u>

For the years ended December 31, 2020, 2021 and 2022, the Group recorded depreciation expense of RMB 5,785, RMB 7,427 and RMB 8,478 (US\$ 1,229), respectively.

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9. Long-Term Loans Receivable

In January 2020, the Group entered into a three-year loan agreement with a third-party supplier of key AAV components with a principal amount of RMB52,000 and an interest rate of 3% per annum. The use of loan proceeds is limited to expanding supplier's production capacity. This long-term loan can be repaid by the borrower at any time. The outstanding loan balance was guaranteed by the borrower's sole shareholder and his spouse and would mature in January 2023. In 2020, RMB40,000 of the loan's principal was repaid by the borrower. Subsequent to December 31, 2022, the Group entered into a supplementary agreement with the third-party supplier to extend the term of the loan of the outstanding amount of RMB12,000 (US\$1,740) as follows: (1) RMB2,000 (US\$290) of the outstanding amount is extended to September 30, 2023. (2) RMB2,000 (US\$290) of the outstanding amount is extended to December 31, 2023. (3) RMB8,000 (US\$1,160) of the outstanding amount is extended to December 31, 2024. RMB 4,000 (US\$580) of the loan was included in current assets in Prepayments and Other Current Assets (Note 7).

In March 2020, the Group provided a two-year loan to a third-party entity with a principal amount of EUR 243 (equivalent to RMB 1,900) and an interest rate of 3.5% per annum. In March 2022, the Group entered into a supplementary letter with the third-party entity to extend the term of the loan by two years. The usage of the loan proceeds is limited to assisting the Group with the application of the necessary permits from the aviation authority in a European country for the commercial operations of AAVs in a European country.

For the years ended December 31, 2020, 2021 and 2022, the Group recognized interest income of RMB 984, RMB418 and RMB423 (US\$61) from the long-term loans receivable, respectively.

10. Long-term Investments

	As of December 31,		
	2021	2022	
	RMB	RMB	US\$
Equity method investments (a)	3,224	6,920	1,004
Equity investments without readily determinable fair values (b)	2,919	2,919	423
	6,143	9,839	1,427

- (a) In June 2021, the Group and a third-party investor entered into an investment agreement to establish an entity for establishing the 5G Intelligent Air Mobility Experience Center as well as local urban air mobility route planning and AAV operations, with total cash consideration of RMB10,500 and RMB 19,500, respectively. The Group has made the investment of cash amounting RMB 700 and RMB4,550 (US\$660) in 2021 and 2022, respectively, and recorded RMB 2,800 and RMB1,750 (US\$254) in accrued expenses and other liabilities (Note 11), which was investment payable as of December 31, 2021 and 2022, respectively, pursuant to the investment agreement. The Group holds 35% of the equity interests and has significant influence on the investee, and accounted for the investment with equity method. For the year ended December 31, 2021, the Group recognized the loss from equity method investment in the amount of RMB276. For the year ended December 31, 2022, the Group recognized the income from equity method investment in the amount of RMB196 (US\$28). For the remaining consideration amounting to RMB 3,500 (US\$508), the Company will settle in accordance with the agreed terms and therefore it was disclosed in Capital commitments (Note 24(a)).
- (b) In 2017, the Group provided facilitating services to a third party to acquire a land use right from the Guangzhou City government. In exchange for such services, the Group received a cash consideration of RMB41,117 and 5% equity interests in a corporation, the sole asset of which was the aforementioned land use right. The Group elected to use the measurement alternative to measure this investment at cost, less any impairment, plus or minus changes resulting from observable price changes in orderly transactions for identical or similar investments of the same issuer. As of December 31, 2021 and 2022, the carrying value of this investment was RMB2,919 and RMB2,919 (US\$423).

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11. Accrued Expenses and Other Liabilities

Accrued expenses and other liabilities consisted of the following:

	As of December 31,		
	2021	2022	
	RMB	RMB	US\$
Payroll and welfare payables	32,532	39,268	5,693
Provision for litigation settlement (a)	—	23,506	3,408
Payables for service fees	10,919	15,572	2,258
Other taxes payables	5,014	6,070	880
Product warranty liabilities	4,758	3,306	479
Payables for acquisition of property and equipment	1,237	3,040	441
Consideration payable to an equity method investment (Note 10(a))	2,800	1,750	254
Accrued interests	769	749	109
Others	3,822	4,502	653
	61,851	97,763	14,175

A reconciliation of the changes in the Group's product warranty liability is as follows:

	For the year ended December 31,		
	2021	2022	
	RMB	RMB	US\$
Balance as of the beginning of the year	4,856	4,758	690
Accruals during the year	1,258	880	128
Claims during the year	(319)	(661)	(96)
Reversal during the year	(1,037)	(1,197)	(174)
Balance as of the ending of the year	4,758	3,780	548
Less: Non-current portion of warranty	—	(474)	(69)
Current portion of warranty	4,758	3,306	479

- (a) As detailed in Note 24(b) (ii), the Company made a total provision of US\$ 3,375 based on the ongoing settlement agreement and corresponding amount was recognized in other expenses for the year ended December 31, 2022.

12. Bank Loans

As of December 31, 2021 and 2022, certain bank loans were pledged by some of Group's Intangible assets.

Short-term bank loans

The outstanding short-term bank loans of RMB 10,000 as of December 31, 2021 was fully repaid upon maturity in 2022.

In 2022, the Group obtained bank loans amounting to RMB49,794 (US\$7,219) from several financial institutions in the PRC. The weighted average effective interest rate of the short-term bank loans was 3.9% per annum. The loans are repayable within one year with interests paid on a monthly or quarterly basis and guaranteed by the Group's founder and director, Mr. Huazhi Hu.

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12. Bank Loans (Continued)

Long-term bank loans

In 2021, the Group entered into long-term agreements with a bank in the PRC of total principals of RMB 20,000, subject to an effective interest rate of 3.8% per annum, and with a maturity date from April 2, 2022 to March 15, 2026. As of December 31, 2021 and 2022, the principal amount of RMB3,000 and RMB13,154 (US\$1,907), respectively, was due within 12 months after the balance sheet date and presented as current liabilities in the consolidated balance sheet.

The carrying value of the long-term bank loans approximates its fair value as of December 31, 2021 and 2022. The interest rates under the loan agreements with the banks were determined based on the prevailing interest rates in the market. The Group classifies the valuation techniques that use these inputs as Level II.

13. Short-term Debt

In December 2022, the Company entered into an SPA with the Investor to sell Underlying Shares to the investor for a total consideration of US\$10,000, on the condition that the Investor will obtain ODI approval for the investment. The Underlying Shares consist of 3,466,204 Class A ordinary shares of the Company, determined by the total consideration and average closing price of the Company's ordinary shares for the previous 30 days upon the sign-off of SPA. A Supplemental Agreement has been entered into and agreed that the Investor would pay a cash consideration of RMB69,861, equivalent to total consideration of US\$ 10,000, to the designated subsidiary of the Company. Concurrently, the Company would issue the Underlying Shares to the Investor or its designated offshore entities. Up to December 31, 2022, the Investor provided the Proceeds of RMB69,861 to the Group, while the Underlying Shares haven't been issued yet.

Pursuant to the Supplemental Agreement, the Group is obligated to repay the RMB Proceeds to the investor three months after the sign-off of SPA or a longer period agreed by both parties (the "Maturity Date"). The RMB Proceeds were loan from the investor and accounted for as a short-term debt under ASC 470, *Debt*.

Pursuant to the SPA, the Company agreed to sell the Underlying Shares to the investor at a future date, which was accounted for as Warrants issued by the Company and classified as equity because it would be settled with equity in the future according to the accounting policy as detailed in Note 2(ah).

The Group received the RMB Proceeds for the short-term debt and Warrants in a bundled transaction. Management allocated Proceeds to the short-term debt and the Warrants based on their relative fair values. As a result, RMB13,697 (US\$1,986) was allocated to the Warrants and recorded as additional paid-in capital, and RMB56,164 (US\$8,143) was allocated to the debt on the initial recognition date. The difference between the amount to be repaid on Maturity Date and the initial recognition date was accounted for as interest expenses. For the year ended December 31, 2022, interest expenses of RMB1,674 (US\$243) were recognized.

Up to the date of issuance of the consolidated financial statement, the Company completed issuance of the Underlying shares to the investor, repaid RMB69,861 and received the total consideration of US\$ 10,000 after the investor obtained the ODI approval in 2023 (Note 25).

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14. Mandatorily Redeemable Non-controlling Interests

On June 15, 2020, the Group established a subsidiary named EHang Yunfu (Note 1). On June 30, 2020, the Group entered into an agreement with a new investor who subscribed 30% of the equity interests of EHang Yunfu for cash consideration of RMB 40,000. At the sole discretion of the investor, the Group is obligated to repurchase the 30% non-controlling interest or with the consent of the investor, guarantee a third-party to repurchase the 30% non-controlling interests at the investor's investment cost at the end of the five-year investment term. The non-controlling interests do not participate in any dividend distributions of EHang Yunfu but earn an after-tax interest of 1.5% per year, payable on a quarterly basis. Interest payable amounted to RMB 200 and RMB 180 (US\$26) as of December 31, 2021 and 2022, respectively. As EHang Yunfu's non-controlling interests are mandatorily redeemable at the sole discretion of the investor, it is classified as liability and subsequently measured at the amount that would be paid if settlement occurred at the reporting date.

The carrying value of Mandatorily redeemable non-controlling interests approximates its fair value as of December 31, 2021 and 2022.

15. Revenues

The following table presents the disaggregation of revenue from contracts with the customers:

	For the year ended December 31,			
	2020 RMB	2021 RMB	2022 RMB	US\$
Revenues - Products				
Air mobility solutions	105,351	46,854	38,061	5,519
Smart city management solutions	8,282	7,135	2,133	309
Aerial media solutions	62,241	518	125	18
Others	186	416	456	66
Subtotal-Products	176,060	54,923	40,775	5,912
Revenues - Services				
Air mobility solutions	618	1,302	2,326	337
Aerial media solutions	3,415	582	1,216	176
Subtotal-Services	4,033	1,884	3,542	513
Total Revenues	180,093	56,807	44,317	6,425

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15. Revenues (Continued)

Payment terms

For the Group's Air mobility solutions and Aerial media solutions, the Group typically requires a portion of payments upfront and the remaining amounts are contractually due ranging from three to six months. Due to the COVID-19 impacts, the Group signed subsequent commitment letters with certain customers and extended the payment terms in 2021 and 2022. However, the Company has collected or is in the process of collecting accounts receivable after the due dates agreed in commitment letters. In light of the impacts from the continuous COVID-19 epidemic and control measures in China, the Group recognized additional provision for accounts receivable for the year ended December 31, 2021 and 2022 (Note 5). Regarding the Smart city management solutions, the timing of billing varies depending on contractual payment schedules with milestone billings and the completion of the quality-assurance warranty period. In instances where the timing of revenue recognition differs from the timing of invoicing, the Group has determined that its contracts do not include a significant financing component at the inception of the contracts.

Contract balances

Contract balances include Accounts receivable, Unbilled revenue and Cost and estimated earnings in excess of billings. Accounts receivable represents the billed and unbilled amounts related to the Company's rights to consideration as performance obligations are satisfied and the rights to payment become unconditional but for the passage of time. In 2021 and 2022, the decrease in Accounts receivable was mainly due to impairment of balances amounted to RMB59,347 and RMB46,045 (US\$6,676) provided in the general and administrative expenses in the Group's consolidated statements of comprehensive loss. The Unbilled revenue was previously recognized from services provided in Aerial media solution. In 2021, the Unbilled revenue was collected, corresponding impairment of balances amounted to RMB2,800 was reversed. In 2022, the increase in Unbilled revenue was primarily due to sales of certain passenger-grade AAVs but unbilled. The receipt of the consideration is subject to conditions other than the passage of time, which is included in Prepayments and Other Current Assets (Note 7). The decrease in Cost and estimated earnings in excess of billings in accordance with the achievement of milestones in the pre-determined billing terms for command-and-control centers, corresponding RMB717 was reclassified from Cost and estimated earnings in excess of billings to Accounts receivable in 2021.

Contract liabilities represent payments received from customers for which the corresponding products or services have not yet been transferred to customers. In 2022, the increase in Contract liabilities was primarily contributed by advance from customers of sales of passenger-grade AAVs. Revenue of RMB3,828 (US\$555) was recognized during the year ended December 31, 2022 from the balance included in the contract liabilities on January 1, 2022.

16. Share-based Compensation

In order to provide additional incentives to employees and to promote the success of the Group's business, the Group adopted a share incentive plan that was approved by the Board of Directors on December 23, 2016 (the "2015 Plan"). Under the 2015 Plan, the aggregate number of ordinary shares that may be issued pursuant to all share-based awards (including restricted shares, RSUs and share options) is 8,867,053 ordinary shares and can be increased up to a number that is equal to 15% of the then total outstanding shares on a fully diluted basis at the discretion of the Company's Board of Directors.

In September 2019, the Company's Board of Directors approved the 2019 Share Incentive Plan (the "2019 Plan"), which become effective upon the completion of the Company's IPO on December 12, 2019. Under the 2019 Plan, the aggregate number of ordinary shares that may be issued pursuant to all share-based awards (including restricted shares, RSUs and share options) is 7,747,019 ordinary shares and can be increased up to a number that is equal to 15% of the then total outstanding shares on a fully diluted basis at the discretion of the Company's Board of Directors.

Pursuant to both 2015 Plan and 2019 Plan (collectively, the "Plans"), the members of the Board, consultant or employees are entitled to be granted share-based awards.

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16. Share-based Compensation (Continued)

The Company granted a total of 750,000, nil and nil RSU to the Group's employees under the 2015 Plan and a total of 1,613,000, 4,790,000 and 876,380 RSUs to the Group's employees under the 2019 Plan for the years ended December 31, 2020, 2021 and 2022. A total of 5,000 RSUs are subject to service conditions and vest over one-year period starting from the vesting inception date. A total of 451,380 RSUs are subject to service conditions and vest over a two-year period starting from the vesting inception date. A total of 7,573,000 RSUs are subject to service conditions and vest over a four-year period starting from the vesting inception date.

RSUs

The following table summarizes the Company's RSUs activity under the Plans:

	Number of RSUs	Weighted average grant date fair value (US\$)	Weighted average remaining contractual life (Years)
Unvested, December 31, 2019	735,476	4.7523	3.02
Granted	2,363,000	4.2912	
Vested	(1,819,726)	4.1359	
Forfeited	—	—	
Unvested, December 31, 2020	1,278,750	4.7774	2.68
Granted	4,790,000	10.6200	
Vested	(1,949,250)	9.2469	
Forfeited	—	—	
Unvested, December 31, 2021	4,119,500	9.4561	2.67
Granted	876,380	1.8800	
Vested	(2,034,880)	7.2254	
Forfeited	(283,000)	7.5431	
Unvested, December 31, 2022	2,678,000	8.8740	1.90
Expected to vest as of December 31, 2022	2,678,000		

The total share-based compensation expenses relating to RSUs for the years ended December 31, 2020, 2021 and 2022 were RMB54,036, RMB121,131 and RMB96,898 (US\$14,049), respectively. Total share-based compensation expense capitalized to inventory was not material for any of the periods presented.

As of December 31, 2022, there was RMB 158,870 (US\$23,034) of unrecognized share-based compensation expenses related to RSUs which is expected to be recognized over a weighted average vesting period of 1.90 years. Total unrecognized compensation cost may be adjusted for actual forfeitures occurring in the future.

Share options

The following table summarizes the Company's share options activity under the 2015 Plan:

	Number of share options	Weighted average grant date fair value (US\$)	Weighted average exercise price (US\$)
Outstanding as of January 1 and December 31, 2022	53,737	2.2624	5.8853
Vested and expected to vest as of December 31, 2022	53,737	2.2624	5.8853
Exercisable as of December 31, 2022	53,737	2.2624	5.8853

The share-based compensation expense relating to the share options recognized were RMB 821, nil and nil for the years ended December 31, 2020, 2021 and 2022. There was no unrecognized share-based compensation expenses relating to the shares options as of December 31, 2020, 2021 and 2022.

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16. Share-based Compensation (Continued)

The Group calculated the estimated fair value of the share options under the 2015 Plan on the grant date using the Black-Scholes valuation model. Assumptions used to determine the fair value of the share options granted under the 2015 Plan is summarized in the following table:

	For the year ended December 31, 2020
Term in years	5
Volatility	53.73%
Discount rate	0.85%
Fair value per ordinary share	US\$ 5.24

Total share-based compensation expenses relating to RSUs and options granted to employees recognized for the years ended December 31, 2020, 2021 and 2022 were as follows:

	For the year ended December 31,			
	2020	2021	2022	
	RMB	RMB	RMB	US\$
Cost of revenues	2,443	—	—	—
Sales and marketing expenses	10,883	18,327	22,125	3,208
General and administrative expenses	14,453	71,147	38,452	5,575
Research and development expenses	27,078	31,657	36,321	5,266
	54,857	121,131	96,898	14,049

17. Income Taxes

Cayman Islands

Under the current laws of the Cayman Islands, the Company is not subject to tax on income or capital gain arising in Cayman Islands.

Austria

EHang GmbH is subject to Austria profits tax of 25% on its activities conducted in Austria.

France

EHang France is subject to France profits tax of 28% on its activities conducted in France.

Spain

EHang Spain is subject to Spain profits tax of 25% on its activities conducted in Spain.

Hong Kong

Ehfly and EHang HK are incorporated in Hong Kong and are subject to Hong Kong profits tax. Hong Kong profits tax for a corporation from the year of assessment 2018 and 2019 onwards is generally 8.25% on assessable profits up to HK\$2.0 million; and 16.5% on any part of assessable profits over HK\$2.0 million.

PRC

The Company's subsidiaries and the VIEs in the PRC are subject to the statutory rate of 25%, in accordance with the Enterprise Income Tax law (the "EIT Law"), which was effective since January 1, 2008 except for certain entities eligible for preferential tax rates.

In accordance with the PRC Income Tax Laws, an enterprise awarded with the High and New Technology Enterprise ("HNTE") certificate may enjoy a reduced EIT rate of 15%. Qualified as an HNTE, EHang Intelligent was eligible for a 15% preferential rate from

2020 to 2022, EHang GZ was eligible for a 15% preferential rate from 2019 to 2024 and Guangdong EHang Egret Media Technology Co. Ltd. ("EHang Egret GD") is eligible for 15% preferential rate from 2018 to 2020, EHang Egret GD has not reapplied for HNTE after 2020.

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17. Income Taxes (Continued)

PRC (Continued)

From January 1, 2010 to December 31, 2020, the newly established enterprises in Xinjiang Kashgar and Khorgos, which are two special economic development zones belong to the Xinjiang Difficult Areas Key Encouraged Development Industry Enterprise Income Tax Preferential Catalogue (the “Catalogue”), shall be exempted from corporate income tax for five years from the tax year in which the first operating income is obtained. Kashi EHang Egret Media Technology Co., Ltd. (“EHang Egret KS”) established in 2017, engaged in industries that belong to Software Development and Business Service Industry in the catalogue. As the first operating income generated in 2018, EHang Egret KS may enjoy a reduced EIT rate of 0%.

According to a policy promulgated by the State Tax Bureau of the PRC and effective from 2008 onwards, enterprises engaged in R&D activities are entitled to claim an additional tax deduction amounting to 50% of the qualified R&D expenses incurred in determining its tax assessable profits for that year. The additional tax deduction amount of the qualified R&D expenses has been increased from 50% to 75%, effective from 2018 to 2020, according to a new tax incentives policy promulgated by the State Tax Bureau of the PRC in September 2018 (“Super Deduction”). According to Announcement of the Ministry of Finance and the State Taxation Administration [2021] No.13 (“Circular 13”), manufacturing enterprise with qualified R&D expenses could enjoy R&D Super Deduction, i.e. to claim additional 100% R&D expenses on top of those actually incurred. EHang Intelligent and Yunfu EHang were subject to 100% super deduction while R&D expenses for other entities within the group remain deducted additionally at 75%.

Dividends, interests, rent or royalties payable by the Company’s PRC subsidiaries, to non-PRC resident enterprises, and proceeds from any such non-resident enterprise investor’s disposition of assets (after deducting the net value of such assets) shall be subject to 10% withholding tax, unless the respective non-PRC resident enterprise’s jurisdiction of incorporation has a tax treaty or arrangements with China that provides for a reduced withholding tax rate or an exemption from withholding tax.

The Group’s loss before income taxes consisted of:

	For the year ended December 31,			
	2020	2021	2022	
	RMB	RMB	RMB	US\$
PRC	(30,412)	(185,000)	(192,495)	(27,909)
Non-PRC	(61,423)	(128,762)	(136,757)	(19,828)
	(91,835)	(313,762)	(329,252)	(47,737)

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17. Income Taxes (Continued)

PRC (Continued)

Income tax expense (benefit) comprises of:

	For the year ended December 31,			
	2020	2021	2022	
	RMB	RMB	RMB	US\$
Income tax expenses (benefits) applicable to PRC operations				
Current income tax expenses	22	113	62	9
Deferred income tax (benefits) expenses	184	—	—	—
Subtotal income tax expenses applicable to PRC operations	206	113	62	9
Income tax expenses applicable to Non-PRC operations				
Current income tax expenses	—	21	17	2
Subtotal income tax expenses applicable to Non-PRC operations	—	21	17	2
Total income tax expenses	206	134	79	11

The reconciliations of the income tax expenses for the years ended December 31, 2020, 2021 and 2022 were as follows:

	For the year ended December 31,			
	2020	2021	2022	
	RMB	RMB	RMB	US\$
Loss before income tax expense	(91,835)	(313,762)	(329,252)	(47,737)
PRC statutory tax rate	25%	25%	25%	25%
Income tax benefits at PRC statutory tax rate of 25%	(22,959)	(78,440)	(82,313)	(11,934)
Effect of different tax rates in different jurisdictions	14,347	31,370	32,886	4,768
Non-deductible expenses	1,195	5,455	6,758	980
Additional deduction for qualified R&D expenses	(13,646)	(24,197)	(20,731)	(3,006)
Effect on adoption of preferential tax rate	(12)	22	3	—
Changes in tax rate in measurement of deferred tax	3,345	—	—	—
Statutory expense	(1,855)	2,636	2,151	312
Others	133	134	79	11
Change in valuation allowance	19,658	63,154	61,246	8,880
Income tax expenses	206	134	79	11
Effect of preferential tax rate inside the PRC on basic and dilutive loss per share	—	—	—	—

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17. Income Taxes (Continued)

PRC (Continued)

The significant components of the Group's deferred tax assets (liabilities) were as follows:

	As of December 31,			
	2020	2021	2022	
	RMB	RMB	RMB	US\$
Non-current deferred tax assets				
Tax losses	103,721	151,160	203,259	29,470
Allowance for doubtful accounts	3,047	17,376	29,288	4,246
Lease liabilities	—	—	18,858	2,734
Welfare payables	4,308	5,807	7,362	1,067
Inventory provision	7,360	7,172	2,472	359
Accrued expenses and other liabilities	1,354	1,329	1,573	228
Intangible assets	—	43	23	3
Unrealized loss on long-term investment	—	69	20	3
Unrealized profit arising from elimination of inter-company transactions	466	474	206	30
Deferred government subsidies	35	15	—	—
Total deferred tax assets	120,291	183,445	263,061	38,140
Less: valuation allowance	(120,291)	(183,445)	(244,691)	(35,477)
Deferred tax assets, net of valuation allowance	—	—	18,370	2,663
Non-current deferred tax liabilities				
Right-of-use assets	—	—	(18,370)	(2,663)
Unrealized gain on long-term investment	(292)	(292)	(292)	(42)
Total deferred tax liabilities	(292)	(292)	(18,662)	(2,705)
Deferred tax assets (liabilities), net of valuation allowance	(292)	(292)	(292)	(42)

Full valuation allowances have been provided where, based on all available evidence, management determined that deferred tax assets are not more likely than not to be realizable in future tax years. Movement of valuation allowance is as follow:

	As of December 31,			
	2020	2021	2022	
	RMB	RMB	RMB	US\$
Valuation allowance				
Balance at beginning of the year	100,633	120,291	183,445	26,597
Additions	19,658	63,154	61,246	8,880
Balance at end of the year	120,291	183,445	244,691	35,477

The Group operates through several subsidiaries and the VIEs. Valuation allowance is considered for each of the entities on an individual basis.

Realization of the net deferred tax assets is dependent on factors including future reversals of existing taxable temporary differences and adequate future taxable income, exclusive of reversing deductible temporary differences and tax loss or credit carry forwards. As of December 31, 2021 and 2022, valuation allowances were provided against deferred tax assets in entities which were in a three-year cumulative loss position and not forecasting profits in the near future.

As of December 31, 2021 and 2022, the Group had deductible tax losses of RMB 584,961 and RMB786,444 (US\$114,024) are derived from entities in the PRC. The tax losses in PRC can be carried forward for five years to offset future taxable profit, and the period was extended to ten years for entities qualified as HNTE in 2018 and thereafter. The tax losses of entities in the PRC began to expire from December 31, 2022 to 2031, if not utilized.

As of December 31, 2021 and 2022, the Group had deductible tax losses of RMB 31,434 and RMB29,411 (US\$4,264) derived from entities in Hong Kong that will not expire if not utilized.

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17. Income Taxes (Continued)

Unrecognized Tax Benefit

As of December 31, 2021 and 2022, the Group had unrecognized tax benefit of RMB 5,480 and RMB5,480 (US\$795), respectively. The unrecognized tax benefit was mainly related to the withholding tax accrued for the facilitating service in the acquisition of land use right from Guangzhou government by EHang HK on behalf of a third-party buyer in 2017 and under-reported statutory profits before tax. The Group does not anticipate that the amount of existing unrecognized tax benefits will significantly change within the next 12 months; however, an estimate of the range of the possible change cannot be made at this moment. As of December 31, 2021 and 2022, unrecognized tax benefits of RMB5,480 and RMB5,480 (US\$795), respectively, if ultimately recognized, will impact the effective tax rate.

A reconciliation of the beginning and ending amount of unrecognized tax benefit was as follows:

	For the year ended December 31,			
	2020	2021	2022	
	RMB	RMB	RMB	US\$
Balance at the beginning of the year	(5,494)	(12,987)	(5,480)	(795)
Additions based on tax positions related to the current year	(7,673)	—	—	—
Reductions for tax positions of prior years	180	7,507	—	—
Balance at the end of the year	<u>(12,987)</u>	<u>(5,480)</u>	<u>(5,480)</u>	<u>(795)</u>

The Group did not record any significant interest and penalties related to an uncertain tax position for the years ended December 31, 2020, 2021 and 2022. Accumulated interest expenses and penalties recorded in unrecognized tax benefit were nil, nil and nil as of December 31, 2020, 2021 and 2022, respectively.

The material jurisdictions in which the Group is subject to potential examination is China. In general, the PRC tax authorities have up to five years to review a company's tax filings. As of December 31, 2022, the tax years ended December 31, 2017 through year ended as of the reporting dates for WFOE, the VIEs remain open to examination by the PRC tax authorities.

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18. Related Party Transactions

The principal related parties with which the Group had transactions during the year presented are as follows:

<u>Name of Entity or Individual</u>	<u>Relationship with the Company</u>
Mr. Huazhi Hu	Principal Shareholder of the Company, Chairman of the Board and Chief Executive Officer
Guangzhou Yitong Zhihang Technology Co., Ltd.	A company over which the Group has significant influence

(1) Transaction with related parties:

For the year ended December 31, 2022, there is no transaction with related parties. For the year ended December 31, 2021, the revenue from an equity investee over which the Group has significant influence amounted to RMB1,504.

(2) Amount due from a related party:

As of December 31, 2022, there are no amount due from related parties. As of December 31, 2021, amount due from a related party amounting to RMB1,360 represented the receivables for the sales of autonomous aerial vehicles to an equity investee over which the Group has significant influence.

(3) Guarantee received for borrowings:

As of December 31, 2021, RMB 10,000 short-term bank loans and RMB 20,000 long-term bank loans were guaranteed by the Group's founder and director, Mr. Huazhi Hu.

As of December 31, 2022, RMB 49,794 (US\$7,219) short-term bank loans and RMB 17,000 (US\$2,465) long-term bank loans were guaranteed by the Group's founder and director, Mr. Huazhi Hu.

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19. Shareholders' Equity

Ordinary Shares

On January 16, 2020, the Company issued 170,062 Class A ordinary shares pursuant to the underwriters' exercise of their over-allotment option to purchase additional ADSs.

For the year ended December 31, 2020, 430,108 Class B ordinary shares were converted to Class A ordinary shares.

On January 29, 2021, the Company issued 1,230,769 Class A ordinary shares to a European asset management company to complete its private placement.

On July 29, 2021, the company issued and transferred 2,500,000 Class A ordinary shares to The Bank of New York Mellon, its depositary bank to be issued to employees upon the vesting of restricted share units under the Plans. For the year ended December 31, 2021, 3,002,130 Class A ordinary shares were issued pursuant to the vesting of restricted share units, among which 1,914,630 Class A ordinary shares were settled with shares held by the depositary bank. Therefore, as of December 31, 2021, 585,370 Class A ordinary shares remain available for future issuance. These shares are legally issued but not outstanding for the purpose of accounting and thus are excluded from the basic net loss per share calculation.

For the year ended December 31, 2021, 4,855,995 Class B ordinary shares were converted to Class A ordinary shares.

On October 26, 2022, the company issued and transferred 876,380 Class A ordinary shares to The Bank of New York Mellon, its depositary bank to be issued to employees upon the vesting of restricted share units under 2015 the Plans. For the year ended December 31, 2022, 2,595,750 Class A ordinary shares were issued pursuant to the vesting of restricted share units, among which 590,750 Class A ordinary shares were settled with shares held by the depositary bank. Therefore, as of December 31, 2022, 871,000 Class A ordinary shares remain available for future issuance. These shares are legally issued but not outstanding for the purpose of accounting and thus are excluded from the basic net loss per share calculation.

For the year ended December 31, 2022, 1,110,000 Class B ordinary shares were converted to Class A ordinary shares.

As of December 31, 2022, there were 77,309,937 Class A and 39,026,560 Class B ordinary shares outstanding.

Additional Paid-in Capital

In January 2022, the Company withheld the individual income tax of RMB 11,230 for employees' vested share-based awards and made the cash payment to tax authorities. Concurrently, the company withheld and received equivalent ADSs shares with fair value of RMB11,230 on that day from the employees for clearance of the individual income tax. The amount was debited to additional paid-in capital.

As detailed in Note 13, Warrants arising from Private Placement were accounted for as additional paid-in capital.

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19. Shareholders' Equity (Continued)

Accumulated Other Comprehensive Income (loss)

	Foreign currency translation adjustment RMB	Unrealized (realized) gains on available- for-sales investments RMB	Total RMB
Balance as of January 1, 2020	10,195	—	10,195
Other comprehensive (loss) income	(9,974)	1,729	(8,245)
Balance as of December 31, 2020	221	1,729	1,950
Other comprehensive loss	(6,107)	(1,729)	(7,836)
Balance as of December 31, 2021	(5,886)	—	(5,886)
Other comprehensive income	20,896	—	20,896
Balance as of December 31, 2022	15,010	—	15,010
Balance as of December 31, 2022 (US\$)	2,176	—	2,176

20. Loss Per Share

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

	2020		For the year ended December 31, 2021				2022	
	Class A	Class B	Class A	Class B	Class A		Class B	
	RMB	RMB	RMB	RMB	RMB	US\$	RMB	US\$
<i>Numerator:</i>								
Net loss attributable to EHang Holdings Limited	(51,294)	(36,325)	(193,772)	(120,187)	(214,390)	(31,083)	(113,831)	(16,504)
Net loss attributable to EHang Holdings Limited's ordinary shareholders	(51,294)	(36,325)	(193,772)	(120,187)	(214,390)	(31,083)	(113,831)	(16,504)
<i>Denominator (in thousands of shares):</i>								
Weighted-average number of ordinary shares outstanding – basic and diluted (in thousands of shares)	64,143	45,420	69,733	43,252	74,917	74,917	39,778	39,778
Loss per share – basic and diluted	(0.80)	(0.80)	(2.78)	(2.78)	(2.86)	(0.41)	(2.86)	(0.41)

The Company had potential dilutive securities such as unvested RSUs and options granted, and Underlying Shares to be issued under the Private Placement. As the Group incurred losses for the years ended December 31, 2020, 2021 and 2022, these potential ordinary shares were anti-dilutive and excluded from the calculation of diluted net loss per share of the Company. The weighted-average numbers of non-vested RSUs excluded from the calculation of diluted net loss per share of the Company were 989,728, 5,492,295 and 3,782,562 as of December 31, 2020, 2021 and 2022, respectively.

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21. Restricted Net Assets

The Company's ability to pay dividends is primarily dependent on the Company receiving distributions of funds from its subsidiary and the VIEs. Relevant PRC statutory laws and regulations permit payments of dividends by the Company's PRC subsidiaries, the VIEs only out of their retained earnings, if any, as determined in accordance with PRC accounting standards and regulations. The results of operations reflected in the consolidated financial statements prepared in accordance with U.S. GAAP differ from those reflected in the statutory financial statements of the Company's subsidiaries and VIEs.

In accordance with the PRC Regulations on Enterprises with Foreign Investment and the articles of association of the Company's PRC subsidiaries, a foreign-invested enterprise established in the PRC is required to provide certain statutory reserves, namely general reserve fund, the enterprise expansion fund and staff welfare and bonus fund which are appropriated from net profit as reported in the enterprise's PRC statutory accounts. A foreign-invested enterprise is required to allocate at least 10% of its annual after-tax profit to the general reserve fund until such reserve has reached 50% of its respective registered capital based on the enterprise's PRC statutory accounts. Appropriations to the enterprise expansion fund and staff welfare and bonus fund are at the discretion of the board of directors for all foreign-invested enterprises. The aforementioned reserves can only be used for specific purposes and are not distributable as cash dividends. The WFOE was established as a foreign-invested enterprise and, therefore, is subject to the above mandated restrictions on distributable profits. For the years ended December 31, 2020, 2021 and 2022, WFOE did not have after-tax profit and therefore no statutory reserves have been allocated.

Additionally, in accordance with the Company Law of the PRC, a domestic enterprise is required to provide statutory surplus fund at least 10% of its annual after-tax profits until such statutory surplus fund has reached 50% of its registered capital based on the enterprise's PRC statutory financial statements. A domestic enterprise is also required to provide discretionary surplus fund, at the discretion of the board of directors, from the net profits reported in the enterprise's PRC statutory financial statements. The aforementioned reserve funds can only be used for specific purposes and are not distributable as cash dividends.

Foreign exchange and other regulations in the PRC may further restrict the Group's VIEs from transferring funds to the Company in the form of dividends, loans and advances. Amounts restricted include paid-in capital and statutory reserves of the Group's PRC subsidiaries and the equity of the VIEs, as determined pursuant to PRC generally accepted accounting principles. As of December 31, 2022, restricted net assets of the Company's PRC subsidiaries and the VIEs was RMB122,546 (US\$17,767). Therefore in accordance with Rules 5-04 and 12-04 of Regulation S-X, the condensed parent company only financial statements as of December 31, 2021 and 2022 and for the years ended December 31, 2020, 2021 and 2022 are disclosed in Note 22.

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22. Company Financial Statements (Parent Company Only)

The Company performed a test on the restricted net assets of its consolidated subsidiaries and VIEs in accordance with Securities and Exchange Commission Regulation S-X Rule 4-08 (e) (3), "General Notes to Financial Statements" and concluded that it was applicable for the Company to disclose the financial information for the Company only.

The footnote disclosures contain supplemental information relating to the operations of the Company.

The Company did not have significant capital and other commitments, or guarantees as of December 31, 2022

Condensed Balance Sheets

	As of December 31,		
	2021 RMB	2022 RMB	2022 US\$ Note 2(e)
ASSETS			
Current assets			
Cash and cash equivalents	72,998	362	52
Amounts due from a subsidiary	—	13,697	1,986
Total current assets	72,998	14,059	2,038
Non-current assets			
Investments in subsidiaries	290,462	213,579	30,966
Total non-current assets	290,462	213,579	30,966
Total assets	363,460	227,638	33,004
Liabilities			
Current liabilities			
Accruals and other liabilities	3,744	27,432	3,977
Amounts due to the subsidiaries the VIEs	—	11,230	1,628
Total current liabilities	3,744	38,662	5,605
Non-current liabilities			
Net interests of the VIEs	27,115	64,718	9,383
Total non-current liabilities	27,115	64,718	9,383
Total liabilities	30,859	103,380	14,988
Shareholders' equity:			
Class A Ordinary shares	50	51	8
Class B Ordinary shares	25	24	3
Additional paid-in capital	1,459,374	1,558,356	225,940
Statutory reserves	1,191	1,191	173
Accumulated deficit	(1,122,153)	(1,450,374)	(210,284)
Accumulated other comprehensive (loss) income	(5,886)	15,010	2,176
Total shareholders' equity	332,601	124,258	18,016
Total liabilities and shareholders' equity	363,460	227,638	33,004

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22. Company Financial Statements (Parent Company Only) (Continued)

Condensed Statements of Comprehensive Loss

	For the Year Ended December 31,			
	2020 RMB	2021 RMB	2022 RMB	2022 US\$ Note 2(e)
Operating expenses:				
General and administrative expenses	(1,144)	(5,668)	(13,630)	(1,976)
Total operating expenses	(1,144)	(5,668)	(13,630)	(1,976)
Loss from operations	(1,144)	(5,668)	(13,630)	(1,976)
Interest income	463	14	1	—
Share of losses from subsidiaries	(117,678)	(299,575)	(253,575)	(36,765)
Income (losses) from the VIEs	30,740	(8,730)	(37,603)	(5,452)
Other expenses	—	—	(23,414)	(3,394)
Net loss attributable to the Company's ordinary shareholders	(87,619)	(313,959)	(328,221)	(47,587)
Other comprehensive (loss) income				
Foreign currency translation adjustment, net of nil tax	(9,974)	(6,107)	20,896	3,030
Unrealized gains on available-for-sale debt securities	1,729	(1,729)	—	—
Other comprehensive (loss) income, net of tax	(8,245)	(7,836)	20,896	3,030
Comprehensive loss attributable to the Company's ordinary shareholder	(95,864)	(321,795)	(307,325)	(44,557)

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22. Company Financial Statements (Parent Company Only) (continued)

Condensed Statements of Cash Flows

	For the Year Ended December 31,			
	2020	2021	2022	2022
	RMB	RMB	RMB	US\$
				Note (e)
Cash flows from operating activities	(681)	(4,874)	(13,738)	(1,992)
Cash flows from investing activities				
Capital contribution to Group companies	(66,599)	(190,026)	(58,898)	(8,539)
Other investing activities	(484)	150	—	—
Net cash used in investing activities	(67,083)	(189,876)	(58,898)	(8,539)
Cash flows from financing activities				
Other financing activities	(7,343)	256,947	—	—
Net cash (used in) provided by financing activities	(7,343)	256,947	—	—
Net (decrease) increase in cash and cash equivalents	(75,107)	62,197	(72,636)	(10,531)
Cash and cash equivalents at beginning of the year	85,908	10,801	72,998	10,583
Cash and cash equivalents at end of the year	10,801	72,998	362	52

Basis of presentation

Condensed financial information is used for the presentation of the Company, or the parent company.

The parent company records its investment in its subsidiary, the VIEs under the equity method of accounting as prescribed in ASC 323, *Investments-Equity Method and Joint Ventures*. Such investments are presented on the Condensed Balance Sheets as “Investments in subsidiaries and VIEs”, and their respective loss as “Share of losses from subsidiaries and VIEs” on the Condensed Statements of Comprehensive Loss.

The subsidiaries did not pay any dividends to the Company for the periods presented. The Company does not have significant commitments or long-term obligations as of the period end other than those presented.

The parent company's condensed financial statements should be read in conjunction with the Company's consolidated financial statements.

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23. Fair Value Measurements

There are no assets measured or disclosed at fair value on a recurring basis as of December 31, 2022. Assets measured or disclosed at fair value on a recurring basis as of December 31, 2021 are summarized below:

	Fair Value Measurements as of December 31, 2021 using			
	Quoted Price in Active Market for Identical Assets	Significant Other Observable Inputs	Unobservable Inputs	Total
	(Level 1)	(Level 2)	(Level 3)	fair value
	RMB	RMB	RMB	RMB
<i>Fair value measurement</i>				
Short-term investments				
Trading debt investments	—	65,108	—	65,108
Total asset measured at fair value	—	65,108	—	65,108

The Group values its trading debt investments using the redemption prices provided by the issuing financial institutions that are not market observable inputs, and accordingly the Group classifies the valuation techniques that use these inputs as Level 2. These products have original maturities of one year or less; therefore, the carrying values approximate their fair values.

The Group invested in available-for-sale debt investments with a one-year term in a closed-end segregated portfolio fund in 2020 and redeemed it in 2021. The investment objective of the fund is to achieve capital appreciation by primarily investing in shares of target companies to be listed in internationally recognizable stock exchanges in their respective initial public offerings. The fund may hold or invest 100% of its assets in temporary investments such as cash or cash equivalents at the discretion of the management of the fund. The investments cannot be sold or transferred, pledged, mortgaged, encumbered or otherwise disposed of without the prior written consent of the management of the fund.

There were no other assets or liabilities measured at a recurring or non-recurring basis as of December 31, 2021 and 2022. The Group measures certain financial and non-financial assets, including long-term investments and long-lived assets, at fair value on a nonrecurring basis when impairment charges are recognized.

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24. Commitments and Contingencies

(a) Capital Commitments

The Group and a third-party investor entered into an investment agreement to establish an investee with a certain payment schedule (Note 10). The following table sets forth our contractual obligations as of December 31, 2022.

	RMB	US\$
2023	1,750	254
2024	1,750	254
Total	3,500	508

(b) Contingencies

The Group is subject to legal and regulatory actions that arise from time to time. The assessment as to whether a loss is probable or reasonably possible, and as to whether such loss or a range of such loss is estimable, often involves significant judgment about future events, and the outcome of litigation is inherently uncertain. Save as disclosed in Note 11(a) and below, the Group is currently not in any legal or administrative proceedings that may have a material adverse impact on the financial position, results of operations or cash flows of the Group.

(i) Shareholder securities litigation

Between February 17 and 26, 2021, three federal securities class action lawsuits (captioned *Amberber v. EHang Holdings Limited, et al.*, Case No. 1:21-cv-01392-GBD (S.D.N.Y., filed Feb. 17, 2021), *Chaumont v. EHang Holdings Limited, et al.*, Case No. 1:21-cv-01526-GBD (S.D.N.Y., filed Feb. 19, 2021), and *Klein v. EHang Holdings Limited, et al.*, Case No. 2:21-cv-01811-JFW-PVC (C.D. Cal., filed Feb. 26, 2021)) were filed by purported holders of the Company ADSs in federal court. The complaints asserted claims under Sections 10(b) and 20(a) of the Securities Exchange Act of 1934, as amended, and generally allege that the company and certain of the Group’s officers made false and misleading statements regarding the status of its urban air mobility business, its international and domestic regulatory approvals, its relationships with major customers, and its manufacturing facilities. The complaints name as defendants the Company and certain of its officers. In addition to costs and attorneys’ fees, the complaints seek compensatory and punitive damages. The Group vigorously defended against them. These lawsuits were consolidated into a single class action lawsuit under the caption *In re EHang Holdings Ltd. Securities Litigation 1.21-CV-01392-GBD-GWG* (S.D.N.Y., filed Feb. 19, 2021), and a lead plaintiff and lead counsel were selected in February 2022. The lead plaintiff filed an amended complaint on April 25, 2022, making similar allegations as those in the previous complaints. Defendants filed a motion to dismiss the amended complaint in June 2022. The lead plaintiff filed an opposition to the defendants’ motion to dismiss in August 2022. The defendants filed a reply in support of their motion to dismiss in September 2022. In October 2022, the Court held oral argument on defendants’ motion to dismiss. The Court granted the defendants’ motion to dismiss the amended complaint on December 15, 2022, and entered final judgment dismissing the action in its entirety with prejudice on January 24, 2023. Lead plaintiff did not appeal the final judgment and on February 23, 2023, lead plaintiff’s deadline to appeal expired.

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24. Commitments and Contingencies (Continued)

(ii) Former employee litigation

A former employee of the Company's former U.S. subsidiary, EHang, Inc., filed a civil lawsuit against the Company, EHang GZ and certain individual defendants, including Mr. Huazhi Hu, chairman and chief executive officer of the Company, in the United States District Court for the Northern District of California. The plaintiff alleged that he was entitled to receive restricted share units from the Company. Following a trial by jury in April 2022, the Court entered judgment for the Plaintiff and against the Company, EHang GZ and Mr. Huazhi Hu as follows: (i) Judgment is entered against the Company on claims for breach of contract, false promise and unpaid wages, and the Company is held jointly and severally liable for compensatory damages in the amount of US\$3,500 and is liable for punitive damages in the amount of US\$10,000; (ii) Judgment is entered against EHang GZ on claims for breach of contract, false promise and unpaid wages, and Ehang GZ is held jointly and severally liable for compensatory damages in the amount of US\$3,500; and (iii) Judgment is entered against Mr. Huazhi Hu on claims for false promise and unpaid wages, and Mr. Huazhi Hu is held jointly and severally liable for compensatory damages in the amount of US\$3,500 and is liable for punitive damages in the amount of US\$ 5,000. The Company then filed a motion for new trial challenging the finding of false promise, the amount of the compensatory damage award, and the amount of the punitive damage award. The judge granted the motion as to the false promise claim and set aside the verdict on that cause of action against The Company and Mr. Huazhi Hu, and because the false promise claim was the only claim that could give rise to punitive damages, the court set aside the punitive damage award and ordered a new trial on the false promise claim. The court denied the motion as to the compensatory damage award.

Following the motion for new trial, the parties have been engaged in settlement discussions. On April 25, 2023, the parties entered into a settlement agreement involving a total payment to the former employee of US\$3,375 in four equal quarterly installments within one year.

25. Subsequent Events

- (a) As detailed in Note 13, the Private Placement will be closed on the condition that the investor obtains the ODI approval. In March and April 2023, the investor obtained the ODI approval and the Company issued the Underlying shares to the Investor, repaid RMB69,861 to the investor and received the total consideration of US\$ 10,000.
- (b) The Group, via Ehang GZ, held 60% interest in EHang Egret GD, which in turn held 60% interest in Xi'an EHang Egret Media Technology Co. Ltd. ("EHang Egret Xi'an"). In March 2023, EHang GZ entered into an agreement to acquire 40% interest of EHang Egret GD from the non-controlling shareholder for a consideration of RMB4,000. Concurrently, EHang Egret GD entered into an agreement to dispose of 60% interest of EHang Egret Xi'an to the non-controlling shareholder at zero consideration. Upon the closing of the transactions, Ehang GZ will hold 100% interest of EHang Egret GD and will no longer have any interest in EHang Egret Xi'an. Management is in the process to assess the impact of the transaction.