REALNETWORKS INC
Form 10-Q
August 08, 2007

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

FORM 10-Q

(Mark One)

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

For the Quarterly Period Ended June 30, 2007

OR

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

For the transition period from to

Commission file number 0-23137

RealNetworks, Inc.

(Exact name of registrant as specified in its charter)

Washington	**91-1628146**
(State of incorporation)	*(I.R.S. Employer Identification Number)*
2601 Elliott Avenue, Suite 1000 **Seattle, Washington**	**98121**
(Address of principal executive offices)	*(Zip Code)*

(206) 674-2700

(Registrant s telephone number, including area code)

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 þ No o

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

Large accelerated filer þ Accelerated filer o Non-accelerated filer o

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

The number of shares of the registrant s Common Stock outstanding as of July 31, 2007 was 149,993,875.

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PART I. FINANCIAL INFORMATION

Item 1. Financial Statements

REALNETWORKS, INC. AND SUBSIDIARIES
UNAUDITED CONDENSED CONSOLIDATED BALANCE SHEETS
(In thousands, except per share data)

	June 30, 2007	December 31, 2006
ASSETS		
Current assets:		
Cash and cash equivalents	$ 219,548	$ 525,232
Short-term investments	394,215	153,688
Trade accounts receivable, net of allowances for doubtful accounts and sales returns	79,354	65,751
Deferred costs, current portion	5,089	1,643
Deferred tax assets, net, current portion	927	891
Prepaid expenses and other current assets	21,720	21,990
Total current assets	720,853	769,195
Equipment, software, and leasehold improvements:		
Equipment and software	94,038	83,587
Leasehold improvements	30,343	29,665
Total equipment, software, and leasehold improvements, at cost	124,381	113,252
Less accumulated depreciation and amortization	72,829	65,509
Net equipment, software, and leasehold improvements	51,552	47,743
Restricted cash equivalents	15,500	17,300
Equity investments	12,511	22,649
Other assets	5,412	5,148
Deferred tax assets, net, non-current portion	30,687	27,150
Other intangible assets, net	104,760	105,109
Goodwill	325,009	309,122
Total assets	$ 1,266,284	$ 1,303,416
LIABILITIES AND SHAREHOLDERS EQUITY		
Current liabilities:		
Accounts payable	$ 50,231	$ 52,097
Accrued and other liabilities	108,013	104,328
Deferred revenue, current portion	37,233	24,137
Accrued loss on excess office facilities, current portion	4,132	4,508
Total current liabilities	199,609	185,070
Deferred revenue, non-current portion	2,757	3,440

Accrued loss on excess office facilities, non-current portion	8,574	9,993
Deferred rent	4,446	4,331
Deferred tax liabilities, net, non-current portion	24,580	27,076
Convertible debt	100,000	100,000
Other long-term liabilities	6,912	3,740
Total liabilities	346,878	333,650
Shareholders equity:		
Preferred stock, $0.001 par value, no shares issued and outstanding		
Series A: authorized 200 shares		
Undesignated series: authorized 59,800 shares		
Common stock, $0.001 par value authorized 1,000,000 shares; issued and outstanding 152,028 shares in 2007 and 163,278 shares in 2006	152	162
Additional paid-in capital	706,848	791,108
Accumulated other comprehensive income	16,107	23,485
Retained earnings	196,299	155,011
Total shareholders equity	919,406	969,766
Total liabilities and shareholders equity	$ 1,266,284	$ 1,303,416

See accompanying notes to unaudited condensed consolidated financial statements.

REALNETWORKS, INC. AND SUBSIDIARIES
UNAUDITED CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS
AND COMPREHENSIVE (LOSS) INCOME
(In thousands, except per share data)

	Three Months ended June 30,		Six Months ended June 30,	
	2007	**2006**	**2007**	**2006**
Net revenue (A)	$ 136,171	$ 89,409	$ 265,643	$ 176,011
Cost of revenue (B)	49,199	26,646	95,142	53,399
Gross profit	86,972	62,763	170,501	122,612
Operating expenses:				
Research and development	25,005	18,684	48,484	36,783
Sales and marketing	50,081	37,961	99,781	74,044
General and administrative	17,063	14,317	34,417	27,543
Loss on excess office facilities				738
Subtotal operating expenses	92,149	70,962	182,682	139,108
Antitrust litigation benefit, net		(57,858)	(60,747)	(97,693)
Total operating expenses, net	92,149	13,104	121,935	41,415
Operating (loss) income	(5,177)	49,659	48,566	81,197
Other income (expenses):				
Interest and other, net	8,065	9,381	17,167	17,360
Gain on sale of equity investment	132	2,286	132	2,286
Equity in net loss of investments			(132)	
Other income, net	485	73	952	190
Other income, net	8,682	11,740	18,119	19,836
Income before income taxes	3,505	61,399	66,685	101,033
Income taxes	(2,178)	(22,521)	(25,397)	(37,272)
Net income	$ 1,327	$ 38,878	$ 41,288	$ 63,761
Basic net income per share	$ 0.01	$ 0.24	$ 0.26	$ 0.40

Diluted net income per share	$ 0.01	$ 0.22	$ 0.24	$ 0.36
Shares used to compute basic net income per share	153,880	159,938	157,929	160,410
Shares used to compute diluted net income per share	169,033	177,337	173,822	177,127
Comprehensive income:				
Net income	$ 1,327	$ 38,878	$ 41,288	$ 63,761
Unrealized holding losses on short-term and equity investments, net of income taxes	(2,663)	(5,094)	(5,719)	(12,915)
Foreign currency translation gains (losses)	1,268	1,005	(1,659)	1,372
Comprehensive (loss) income	$ (68)	$ 34,789	$ 33,910	$ 52,218
(A) Components of net revenue:				
License fees	$ 22,212	$ 22,850	$ 44,049	$ 45,486
Service revenue	113,959	66,559	221,594	130,525
	$ 136,171	$ 89,409	$ 265,643	$ 176,011
(B) Components of cost of revenue:				
License fees	$ 7,882	$ 9,329	$ 16,174	$ 19,190
Service revenue	41,317	17,317	78,968	34,209
	$ 49,199	$ 26,646	$ 95,142	$ 53,399

See accompanying notes to unaudited condensed consolidated financial statements.

REALNETWORKS, INC. AND SUBSIDIARIES
UNAUDITED CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS
(in thousands)

	Six Months Ended June 30,	
	2007	**2006**
Cash flows from operating activities:		
Net income	$ 41,288	$ 63,761
Adjustments to reconcile net income to net cash (used in) provided by operating activities:		
Depreciation and amortization	20,905	8,219
Stock-based compensation	11,307	7,311
Loss on disposal of equipment, software, and leasehold improvements	163	76
Equity in net loss of investments	132	
Gain on sale of equity investment	(132)	(2,286)
Excess tax benefit from stock option exercises	(596)	
Accrued loss on excess office facilities	(1,795)	(1,742)
Unrealized gain on trading securities	(2,102)	
Deferred income taxes	(6,069)	35,246
Purchases of trading securities	(270,000)	
Other	51	48
Net change in certain operating assets and liabilities, net of acquisitions	552	(50,651)
Net cash (used in) provided by operating activities	(206,296)	59,982
Cash flows from investing activities:		
Purchases of equipment, software, and leasehold improvements	(11,525)	(5,381)
Purchases of short-term investments	(38,768)	(102,853)
Proceeds from sales and maturities of short-term investments	70,343	86,422
Purchases of other intangibles assets	(2,060)	
Proceeds from sale of equity investments	1,615	2,286
Purchases of equity investments		(450)
Decrease in restricted cash equivalents	1,800	
Cash used in acquisitions, net of cash acquired	(25,351)	(7,086)
Net cash used in investing activities	(3,946)	(27,062)
Cash flows from financing activities:		
Net proceeds from sale of common stock under employee stock purchase plan and exercise of stock options	12,277	34,522
Excess tax benefit from stock options exercises	596	
Repurchase of common stock	(107,905)	(96,972)

Net cash used in financing activities	(95,032)	(62,450)
Effect of exchange rate changes on cash and cash equivalents	(410)	739
Net decrease in cash and cash equivalents	(305,684)	(28,791)
Cash and cash equivalents, beginning of period	525,232	651,971
Cash and cash equivalents, end of period	$ 219,548	$ 623,180
Supplemental disclosure of cash flow information:		
Cash paid for income taxes	$ 13,160	$ 12,042
Supplemental disclosure of non-cash investing and financing activities:		
Accrued acquisition costs	$ 368	$
Accrued acquisition consideration	$	$ 2,054

See accompanying notes to unaudited condensed consolidated financial statements.

REALNETWORKS, INC. AND SUBSIDIARIES
NOTES TO UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS
Three and Six Months Ended June 30, 2007 and 2006

Note 1. Summary of Significant Accounting Policies

Description of Business. RealNetworks, Inc. and subsidiaries (RealNetworks or Company) is a leading global provider of network-delivered digital media products and services. The Company also develops and markets software products and services that enable the creation, distribution and consumption of digital media, including audio and video.

Inherent in the Company s business are various risks and uncertainties, including limited history of certain of its product and service offerings and its limited history of offering premium subscription services on the Internet. The Company s success will depend on the acceptance of the Company s technology, products, and services and the ability to generate related revenue.

Basis of Presentation. The unaudited condensed consolidated financial statements include the accounts of the Company and its wholly-owned and majority-owned subsidiaries. All significant intercompany balances and transactions have been eliminated in consolidation. The Company acquired 99.7% of WiderThan Co., Ltd. (WiderThan) during the three months ended December 31, 2006. The Company acquired substantially all of the remaining 0.3% of WiderThan during the three months ended June 30, 2007. The accompanying unaudited condensed consolidated financial statements include 100% of the financial results of WiderThan from the date of acquisition. The minority interest in the earnings of WiderThan for the three and six months ended June 30, 2007 was nominal. The minority interest liability as of June 30, 2007 and December 31, 2006 was nominal.

The unaudited condensed consolidated financial statements reflect all adjustments, consisting only of normal, recurring adjustments that, in the opinion of the Company s management, are necessary for a fair presentation of the results of operations for the periods presented. Operating results for the three and six months ended June 30, 2007 are not necessarily indicative of the results that may be expected for any subsequent quarter or for the year ending December 31, 2007. Certain information and disclosures normally included in financial statements prepared in conformity with accounting principles generally accepted in the United States of America have been condensed or omitted pursuant to the rules and regulations of the Securities and Exchange Commission (SEC).

These unaudited condensed consolidated financial statements should be read in conjunction with the audited consolidated financial statements and related notes included in the Company s Annual Report on Form 10-K for the year ended December 31, 2006.

Revenue Recognition. The Company recognizes revenue in accordance with the following authoritative literature: AICPA Statement of Position (SOP) No. 97-2, *Software Revenue Recognition;* SOP No. 98-9, *Software Revenue Recognition with Respect to Certain Arrangements*; SOP No. 81-1, *Accounting for Performance of Construction-Type and Certain Production-Type Contracts*; SEC Staff Accounting Bulletin (SAB) No. 104, *Revenue Recognition in Financial Statements*; Financial Accounting Standards Board s (FASB) Emerging Issues Task Force (EITF) Issue No. 99-19, *Reporting Revenue Gross as a Principal versus Net as an Agent;* and EITF Issue No. 00-21, *Revenue Arrangements with Multiple Deliverables*. Generally the Company recognizes revenue when there is persuasive evidence of an arrangement, the fee is fixed or determinable, the product or services have been delivered and collectibility of the resulting receivable is reasonably assured.

Consumer subscription products are paid in advance, typically for monthly, quarterly or annual periods. Subscription revenue is recognized ratably over the related subscription period. Revenue from sales of downloaded individual tracks, albums and games are recognized at the time the music or game is made available, digitally, to the end user.

The Company recognizes revenue under the residual method for multiple element software arrangements when vendor specific objective evidence (VSOE) exists for all of the undelivered elements of the arrangement, but does not exist for one or more of the delivered elements in the arrangement, under SOP No. 97-2. Under the residual method, at the outset of the arrangement with a customer, the Company defers revenue for the fair value of the arrangement s undelivered elements such as post contract support (PCS), and recognizes revenue for the remainder of the arrangement fee attributable to the elements initially delivered, such as software licenses. VSOE for PCS is established on standard products for which no installation or customization is required based upon amount charged when PCS is sold separately. For multiple element software arrangements involving significant production, modification, or customization of the software, which are accounted for in accordance with the provisions of SOP No. 81-1, VSOE for PCS is established if customers have an optional renewal rate specified in the arrangement and the rate is substantive.

REALNETWORKS, INC. AND SUBSIDIARIES
NOTES TO UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

The Company has arrangements whereby customers pay one price for multiple products and services and in some cases, involve a combination of products and services. For arrangements with multiple deliverables, revenue is recognized upon the delivery of the individual deliverables in accordance with EITF Issue No. 00-21. In the event that there is no objective and reliable evidence of fair value of the delivered items, the revenue recognized upon delivery is the total arrangement consideration less the fair value of the undelivered items. The Company applies significant judgment in establishing the fair value of multiple elements within revenue arrangements.

The Company recognizes revenue on a gross or net basis in accordance with EITF Issue No. 99-19. In most arrangements, the Company contracts directly with end user customers, is the primary obligor and carries all collectibility risk. In such arrangements the Company reports revenue on a gross basis. In some cases, the Company utilizes third-party distributors to sell products or services directly to end user customers and carries no collectibility risk. In such instances the Company reports revenue on a net basis.

Revenue generated from advertising on the Company s websites and from advertising included in its products is recognized as revenue as the delivery of the advertising occurs.

Accounting for Taxes Collected From Customers. The Company collects various types of taxes from its customers, assessed by governmental authorities, that is imposed on and concurrent with revenue-producing transactions. Such taxes are not included in net revenue of the Company.

Reclassifications. Certain reclassifications have been made to the 2007 year-to-date information to conform to the presentation for the three months ended June 30, 2007.

Note 2. Recent Accounting Pronouncements

In June 2006, the FASB issued Financial Interpretation (FIN) No. 48, *Accounting for Uncertainty in Income Taxes an interpretation of FASB Statement No. 109.* FIN No. 48 clarifies the accounting for uncertainty in income taxes recognized in an enterprise s financial statements in accordance with SFAS No. 109, *Accounting for Income Taxes*, and prescribes a recognition threshold and measurement process for financial statement recognition and measurement of tax positions taken or expected to be taken in tax returns. FIN No. 48 also provides guidance on derecognition, classification, interest and penalties, accounting in interim periods, disclosure and transition. On January 1, 2007, date of adoption of FIN No. 48, the Company had $7.5 million of unrecognized tax benefits, of which $7.2 million would affect the effective tax rate if recognized. Although the implementation of FIN No. 48 did not impact the amount of liability for unrecognized tax benefits, the Company reclassified $5.3 million of liability for unrecognized tax benefits from current income taxes payable to other long-term liabilities to conform with the balance sheet presentation requirements of FIN No. 48.

In accordance with FIN No. 48, the Company recognizes potential accrued interest and penalties related to unrecognized tax benefits as a component of income tax expense. As of January 1, 2007, the Company had approximately $300,000 of accrued interest and penalties related to uncertain tax positions, which is included as a component of the $5.3 million of unrecognized tax benefit noted above. To the extent interest and penalties are not assessed with respect to uncertain tax positions, amounts accrued will be reduced and reflected as a reduction of the overall income tax provision. The Company does not anticipate that total unrecognized tax benefits will significantly change within the next twelve months.

The Company files numerous consolidated and separate income tax returns in the United States Federal, state, local, and foreign jurisdictions. With few exceptions, the Company is no longer subject to United States Federal, state, local, or foreign income tax examinations for years before 1993.

In September 2006, the FASB issued Statement of Financial Accounting Standards (SFAS) No. 157, *Fair Value Measurements*, which defines fair value, establishes a framework for measuring fair value in generally accepted accounting principles, and expands disclosures about fair value measurements. SFAS No. 157 does not require any new fair value measurements, but provides guidance on how to measure fair value by providing a fair value hierarchy used to classify the source of the information. SFAS No. 157 is effective for fiscal years beginning after November 15, 2007 and interim periods within those fiscal years. The Company is currently assessing the impact of SFAS No. 157 on its consolidated financial statements.

In February 2007, the FASB issued SFAS No. 159 *The Fair Value Option for Financial Assets and Financial Liabilities*, which provides companies with an option to report selected financial assets and liabilities at fair value. The objective of SFAS No. 159 is to reduce both the complexity in accounting for financial instruments and the volatility in earnings caused by measuring related assets

REALNETWORKS, INC. AND SUBSIDIARIES
NOTES TO UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

and liabilities differently. SFAS No. 159 is effective for fiscal years beginning after November 15, 2007. The Company is currently assessing the impact of SFAS No. 159 on its consolidated financial statements.

Note 3. Stock-Based Compensation

The Company accounts for stock-based compensation in accordance with SFAS No. 123R revised 2004, *Share-Based Payment*. Under the fair value provisions of the statement, stock-based compensation cost is measured at the grant date based on the fair value of the award and is recognized as expense over the requisite service period, which is the vesting period. The Company uses the Black-Scholes option-pricing model to determine the fair-value of stock-based awards under SFAS No. 123R. The Company recognizes compensation cost related to stock options granted prior to the adoption of SFAS No. 123R on an accelerated basis over the applicable vesting period using the methodology described in FIN No. 28, *Accounting for Stock Appreciation Rights and Other Variable Stock Option or Award Plans*. The Company recognizes compensation cost related to options granted subsequent to the adoption of SFAS No. 123R on a straight-line basis over the applicable vesting period.

The expected term of the options represents the estimated period of time until exercise and is based on historical experience of similar awards, including the contractual terms, vesting schedules, and expectations of future employee behavior. Expected stock price volatility is based on a combination of historical volatility of the Company s stock for the related expected term and the implied volatility of its traded options. The risk-free interest rate is based on the implied yield available on U.S. Treasury zero-coupon issues with a term equivalent to the expected term of the stock options. The Company has not paid dividends in the past.

The fair value of options granted was determined using the Black-Scholes model and the following weighted average assumptions:

	Three Months Ended June 30,		Six Months Ended June 30,	
	2007	**2006**	**2007**	**2006**
Expected dividend yield	0%	0%	0%	0%
Risk-free interest rate	4.73%	4.99%	4.72%	4.79%
Expected life (years)	4.1	4.3	4.1	4.3
Volatility	42%	49.1%	42%	48.4%

Recognized stock-based compensation expense is as follows (in thousands):

	Three Months Ended June 30,		Six Months Ended June 30,	
	2007	**2006**	**2007**	**2006**
Cost of service revenue	$ 154	$ 41	$ 313	$ 91
Research and development	1,641	1,318	3,413	2,687
Sales and marketing	2,203	1,434	4,590	2,793
General and administrative	1,624	880	2,991	1,740
Total stock-based compensation expense	$ 5,622	$ 3,673	$ 11,307	$ 7,311

No stock-based compensation was capitalized as part of the cost of an asset during the six months ended June 30, 2007 and 2006. As of June 30, 2007, $43.4 million of total unrecognized compensation cost, net of estimated forfeitures, related to stock options is expected to be recognized over a weighted-average period of 2.8 years.

Note 4. Business Combinations

Business Combinations During 2007

Sony NetServices GmbH

On May 15, 2007, the Company acquired all of the outstanding securities of Sony NetServices GmbH (SNS) in exchange for $12.8 million in cash payments, including $902,000 in direct acquisition related costs consisting primarily of professional fees.

SNS is located in Salzburg, Austria and is a provider of end-to-end white label digital music services to mobile operators in Europe. The Company believes that combining SNS assets and technology with its existing business will enhance the Company s

REALNETWORKS, INC. AND SUBSIDIARIES
NOTES TO UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

digital music offerings in the European market. The results of SNS operations are included in the Company s condensed consolidated financial statements starting from the date of acquisition.

A summary of the preliminary purchase price is as follows (in thousands):

Cash paid at acquisition	$ 11,924
Estimated direct acquisition costs	902
Total	$ 12,826

The aggregate purchase consideration has been allocated to the assets and liabilities acquired, including identifiable intangible assets, based on their respective estimated fair values as summarized below. The respective estimated fair values were determined by a third-party appraisal as of the date of acquisition and resulted in excess purchase consideration over the net tangible and identifiable intangible assets acquired of $9.3 million. Goodwill in the amount of $9.3 million is not deductible for tax purposes.

A summary of the preliminary allocation of the purchase price is as follows (in thousands):

Current assets	$ 5,110
Property and equipment	2,351
Intangible assets subject to amortization:	
Technology	1,760
Customer relationships	1,610
Goodwill	9,341
Total assets acquired	20,172
Current liabilities	(7,346)
Net assets acquired	$ 12,826

Technology has weighted average estimated useful life of seven years. Customer relationships have weighted average estimated useful lives of nine years. All of the intangible assets are being amortized over their estimated useful lives on a straight line basis.

Pro forma results are not presented as they are not material to the Company s overall unaudited condensed consolidated financial statements.

Exomi Oy

On June 8, 2007, the Company acquired all of the outstanding securities of Exomi Oy (Exomi) in exchange for $11.2 million in cash payments, including $468,000 in direct acquisition related costs consisting primarily of professional fees. The Company may be obligated to pay an additional 3.6 million ($4.9 million at June 30, 2007) over a three-year period, dependent on whether certain performance criteria are achieved. Such amounts are not included in the initial aggregate purchase price and, to the extent earned, will be recorded as goodwill when the performance criteria are achieved. No such payments were accrued during the period ended June 30, 2007.

Exomi is located in Helsinki, Finland and is a provider of short message service (SMS) messaging and gateway products and services with customers primarily in Europe and Latin America. The Company believes that combining

Exomi s assets and network with the Company s products and services will enhance its presence in the European and Latin American markets. The results of Exomi s operations are included in the Company s condensed consolidated financial statements starting from the date of acquisition.

A summary of the purchase price is as follows (in thousands):

Cash paid at acquisition	$ 10,745
Estimated direct acquisition costs	468
Total	$ 11,213

The aggregate purchase consideration has been allocated to the assets and liabilities acquired, including identifiable intangible assets, based on their respective estimated fair values as summarized below. The respective estimated fair values were determined by a third-party appraisal as of the date of acquisition and resulted in excess purchase consideration over the net tangible and identifiable intangible assets acquired of $2.9 million. Goodwill in the amount of $2.9 million is not deductible for tax purposes.

REALNETWORKS, INC. AND SUBSIDIARIES
NOTES TO UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

A summary of the preliminary allocation of the purchase price is as follows (in thousands):

Current assets	$ 5,409
Property and equipment	265
Other long-term assets	109
Intangible assets subject to amortization:	
Customer relationships	3,270
Technology	2,545
Tradenames and trademarks	287
Non-compete agreements	80
Goodwill	2,852
Total assets acquired	14,817
Current liabilities	(1,761)
Net deferred tax liabilities	(1,472)
Other long-term liabilities	(371)
Total liabilities acquired	(3,604)
Net assets acquired	$ 11,213

Customer relationships have weighted average estimated useful lives of eight years. Technology and tradenames and trademarks have weighted average estimated useful lives of four years. Non-compete agreements have weighted average estimated useful life of one year. All of the intangible assets are being amortized over their estimated useful lives on a straight line basis.

Pro forma results are not presented as they are not material to the Company s overall unaudited condensed consolidated financial statements.

Business Combinations During 2006

WiderThan Co. Ltd.

The Company acquired 99.7% of the outstanding common shares and American Depository Shares of WiderThan Co. Ltd. (WiderThan) during the three months ended December 31, 2006 for a total purchase price of $342.7 million. The results of WiderThan operations are included in the Company s unaudited condensed consolidated financial statements starting from the closing date of October 31, 2006. The Company acquired substantially all of the remaining 0.3% of the outstanding common shares and American Depository Shares of WiderThan during the three months ended June 30, 2007.

Zylom Media Group B.V.

On January 31, 2006, the Company acquired all of the outstanding securities of Zylom Media Group B.V. (Zylom) in exchange for $8.2 million in cash payments, including $293,000 in direct acquisition related costs consisting primarily of professional fees. The Company is also obligated to pay an additional $2.0 million, through individual payments of $1.0 million on the first and second anniversaries of the acquisition date. The first payment of $1.0 million was made during the six months ended June 30, 2007.

Additionally, the Company may be obligated to pay up to $10.9 million over a three-year period, dependent on whether certain performance criteria are achieved. Such amounts are not included in the initial aggregate purchase price and, to the extent earned, will be recorded as goodwill when the performance criteria are achieved. During the six months ended June 30, 2007, the Company accrued and paid $4.4 million towards such payments based on achievement of certain performance criteria.

Zylom is located in Eindhoven, The Netherlands and is a distributor, developer, and publisher of PC-based games in Europe. The Company believes that combining Zylom s assets and distribution network with the Company s downloadable PC-based games assets and distribution platform will enhance the Company s presence in the European games market. The results of Zylom s operations are included in the Company s condensed consolidated financial statements starting from the date of acquisition.

REALNETWORKS, INC. AND SUBSIDIARIES
NOTES TO UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

A summary of the purchase price is as follows (in thousands):

Cash paid at acquisition	$ 7,922
Additional payments related to initial purchase price	2,000
Additional payments for achievement of performance criteria	4,364
Direct acquisition costs	293
Total	$ 14,579

The aggregate purchase consideration has been allocated to the assets and liabilities acquired, including identifiable intangible assets, based on their respective estimated fair values as summarized below. The respective estimated fair values were determined by a third-party appraisal as of the date of acquisition and resulted in excess purchase consideration over the net tangible and identifiable intangible assets acquired of $12.5 million. Goodwill in the amount of $12.5 million is not deductible for tax purposes.

A summary of the allocation of the purchase price is as follows (in thousands):

Current assets	$ 1,830
Property and equipment	166
Intangible assets subject to amortization:	
Distributor and customer relationships	1,290
Technology and games	570
Tradenames and trademarks	560
Non-compete agreements	180
Goodwill	12,532
Total assets acquired	17,128
Current liabilities	(1,781)
Net deferred tax liabilities	(768)
Total liabilities acquired	(2,549)
Net assets acquired	$ 14,579

Distributor and customer relationships have weighted average estimated useful lives of five years. Technology, games, tradenames, and trademarks have weighted average estimated useful lives of three years. Non-compete agreements have weighted average estimated useful life of four years. All of the intangible assets are being amortized over their estimated useful lives on a straight line basis.

Pro forma results are not presented as they are not material to the Company s overall unaudited condensed consolidated financial statements.

REALNETWORKS, INC. AND SUBSIDIARIES
NOTES TO UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

Note 5. Cash, Cash Equivalents, Trading Securities, Short-Term Investments, and Restricted Cash Equivalents

Cash, cash equivalents, trading securities, short-term investments, and restricted cash equivalents as of June 30, 2007 consist of the following (in thousands):

	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Estimated Fair Value
Cash and cash equivalents:				
Cash	$ 137,275	$	$	$ 137,275
Money market mutual funds	54,930			54,930
Corporate notes and bonds	27,338	5		27,343
Total cash and cash equivalents	219,543	5		219,548
Trading securities:				
Money market mutual fund	270,000	2,102		272,102
Available-for-sale investments:				
Corporate notes and bonds	53,215	15	(140)	53,090
U.S. Government agency securities	69,027	23	(27)	69,023
Total available-for-sale investments	122,242	38	(167)	122,113
Total short-term investments	392,242	2,140	(167)	394,215
Total cash, cash equivalents, trading securities, and short-term investments	$ 611,785	$ 2,145	$ (167)	$ 613,763
Restricted cash equivalents	$ 15,500	$	$	$ 15,500

Cash, cash equivalents, short-term investments, and restricted cash equivalents as of December 31, 2006 consist of the following (in thousands):

	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Estimated Fair Value
Cash and cash equivalents:				
Cash	$ 108,415	$	$	$ 108,415
Money market mutual funds	231,634			231,634

Corporate notes and bonds	182,184			182,184
U.S. Government agency securities	2,999			2,999
Total cash and cash equivalents	525,232			525,232
Short-term investments:				
U.S. Government agency securities	153,520	188	(20)	153,688
Total short-term investments	153,520	188	(20)	153,688
Total cash, cash equivalents, and short-term investments	$ 678,752	$ 188	$ (20)	$ 678,920
Restricted cash equivalents	$ 17,300	$	$	$ 17,300

At June 30, 2007 and December 31, 2006, restricted cash equivalents represent cash equivalents pledged as collateral against two letters of credit for a total of $15.5 million and $17.3 million, respectively, in connection with two lease agreements.

Realized gains or losses on sales of available-for-sale securities for the three and six months ended June 30, 2007 and 2006 were not significant.

Unrealized gain on trading securities for the six months ended June 30, 2007 of $2.1 million is included in interest and other, net in the unaudited condensed consolidated statements of operations and comprehensive (loss) income. Unrealized gain on trading securities at June 30, 2007, was $2.1 million. The Company did not have any investments in trading securities during 2006.

REALNETWORKS, INC. AND SUBSIDIARIES
NOTES TO UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

Changes in estimated fair values of short-term investments are primarily related to changes in interest rates and are considered to be temporary in nature.

The contractual maturities of available-for-sale investments at June 30, 2007 are as follows (in thousands):

	Amortized Cost	Estimated Fair Value
Within one year	$ 83,207	$ 83,204
Between one year and five years	39,035	38,909
Total available-for-sale investments	$ 122,242	$ 122,113

Note 6. Allowance for Doubtful Accounts Receivable and Sales Returns

Activity in the allowance for doubtful accounts receivable and sales returns is as follows (in thousands):

	Allowance For	
	Doubtful Accounts Receivable	Sales Returns
Balances, December 31, 2006	$ 1,101	$ 1,389
Additions charged to expenses/revenue	75	2,688
Amounts written off	(117)	(2,700)
Balances, June 30, 2007	$ 1,059	$ 1,377

As of June 30, 2007 and December 31, 2006 one international customer accounted for 22% and 25%, respectively, of trade accounts receivable. The same international customer accounted for 13% and 12% of total revenue during the three and six months ended June 30, 2007, respectively. No one customer accounted for more than 10% of total revenue during the three and six months ended June 30, 2006.

Note 7. Equity Investments

As of June 30, 2007 and December 31, 2006, the carrying value of equity investments in publicly traded companies consists primarily of approximately 10.6% of outstanding shares of J-Stream Inc. (J-Stream), a Japanese media services company. These equity investments are accounted for as available-for-sale and the increase over the cost basis, net of income taxes, is reflected as a component of accumulated other comprehensive income.

Summary of equity investments is as follows (in thousands):

	June 30, 2007		December 31, 2006	
	Cost	Carrying Value	Cost	Carrying Value
Publicly traded investments	$ 913	$ 11,586	$ 913	$ 20,235
Privately held investments	1,551	925	1,879	2,414
Total equity investments	$ 2,464	$ 12,511	$ 2,792	$ 22,649

Note 8. Other Intangible Assets

Other intangible assets at June 30, 2007 consist of the following (in thousands):

	Gross Amount	Accumulated Amortization	Net
Customer relationships	$ 77,540	$ 8,901	$ 68,639
Developed technology	41,085	13,974	27,111
Patents, trademarks and tradenames	7,402	3,252	4,150
Service contracts and other	6,821	1,961	4,860
Total other intangible assets	$ 132,848	$ 28,088	$ 104,760

REALNETWORKS, INC. AND SUBSIDIARIES
NOTES TO UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

Other intangible assets at December 31, 2006 consist of the following (in thousands):

	Gross Amount	Accumulated Amortization	Net
Customer relationships	$ 73,061	$ 3,386	$ 69,675
Developed technology	36,891	9,981	26,910
Patents, trademarks and tradenames	7,114	2,226	4,888
Service contracts and other	4,680	1,044	3,636
Total other intangible assets	$ 121,746	$ 16,637	$ 105,109

Amortization expense related to other intangible assets during the three and six months ended June 30, 2007 was $5.7 million and $11.3 million, respectively. Amortization expense related to other intangible assets during the three and six months ended June 30, 2006 was $482,000 and $1.2 million, respectively.

As of June 30, 2007, estimated future amortization of other intangible assets is as follows (in thousands):

2007 (remaining six months)	$ 11,663
2008	22,656
2009	20,853
2010	16,939
2011	11,128
Thereafter	21,521
Total	$ 104,760

Note 9. Goodwill

Changes in goodwill are as follows (in thousands):

Balance, December 31, 2006	$ 309,122
Increases for payments due to Zylom	4,364
Adjustments to purchase price for WiderThan	(1,296)
Purchase of additional shares of WiderThan	1,160
Increase due to acquisitions	12,193
Effects of foreign currency translation	(534)
Balance, June 30, 2007	$ 325,009

Note 10. Accrued and Other Liabilities

Accrued and other liabilities consist of (in thousands):

	June 30, 2007	December 31, 2006
Royalties and other fulfillment costs	$ 32,127	$ 29,968

Employee compensation, commissions and benefits	21,379	25,244
Income taxes payable	12,811	8,455
Sales, VAT and other taxes payable	10,787	13,364
Legal fees and contingent legal fees	4,187	4,075
Accrued charitable donations	79	2,048
Other	26,643	21,174
Total	$ 108,013	$ 104,328

Note 11. Loss on Excess Office Facilities

In October 2000, the Company entered into a 10-year lease agreement for additional office space located near its corporate headquarters in Seattle, Washington. Due to a subsequent decline in the market for office space in Seattle and the Company s re-assessment of its facilities requirements in 2001, the Company accrued for estimated future losses on excess office facilities. The Company has accrued additional estimates of future losses on this facility since 2001 based on changes in market conditions, securing tenants at rates lower than those used in the original estimate, and certain other factors.

REALNETWORKS, INC. AND SUBSIDIARIES
NOTES TO UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

During the three months ended March 31, 2006 the Company recorded $738,000 of additional loss due to building operating expenses that are not expected to be recovered under the terms of the existing sublease arrangements. The Company did not identify any factors which caused it to revise its estimates during the period ended June 30, 2007. The estimated loss as of June 30, 2007 consists of $8.8 million of sublease income under existing sublease arrangements.

A summary of activity for accrued loss on excess office facilities is as follows (in thousands):

Accrued loss on excess office facilities, December 31, 2006	$ 14,501
Less amounts paid on accrued loss on excess office facilities, net of sublease income	(1,795)
Accrued loss on excess office facilities, June 30, 2007	12,706
Less current portion	4,132
Accrued loss on excess office facilities, non-current portion	$ 8,574

Note 12. Repurchase of Common Stock

In April 2006, the Company s Board of Directors authorized a share repurchase program of up to an aggregate of $100.0 million of the Company s outstanding common stock. During the three months ended March 31, 2007, the Company purchased 9.8 million shares at an average cost of $7.99 per share for an aggregate value of $78.5 million. No amounts remained authorized for repurchase under the repurchase program as of March 31, 2007.

In May 2007, the Board of Directors of the Company authorized a new share repurchase program for the repurchase of up to an aggregate of $100.0 million of the Company s outstanding common stock. During the three months ended June 30, 2007, the Company purchased 3.5 million shares at an average cost of $8.31 per share for an aggregate value of $29.4 million. As of June 30, 2007, $70.6 million remained authorized for repurchase under the May 2007 repurchase program.

Note 13. Earnings Per Share

Basic net income per share is computed by dividing net income by the weighted average number of common shares outstanding during the period. Diluted net income per share is computed by dividing net income by the weighted average number of common and dilutive potential common shares outstanding during the period. Share count used to compute basic and diluted net income per share is calculated as follows (in thousands):

	Three Months Ended June 30,		Six Months Ended June 30,	
	2007	2006	2007	2006
Weighted average common shares outstanding used to compute basic net income per share	153,880	159,938	157,929	160,410
Dilutive potential common shares:				
Stock options and restricted stock	4,403	6,649	5,143	5,967
Convertible debt	10,750	10,750	10,750	10,750
Shares used to compute diluted net income per share	169,033	177,337	173,822	177,127

During the three and six months ended June 30, 2007, 19.5 million and 17.4 million, respectively, shares of common stock potentially issuable from stock options are excluded from the calculation of diluted net income per share because of their antidilutive effect. During the three and six months ended June 30, 2006, 3.2 million and

3.9 million, respectively, shares of common stock potentially issuable from stock options are excluded from the calculation of diluted net income per share because of their antidilutive effect.

Note 14. Commitments and Contingencies

Borrowing Arrangements. The Company s subsidiary, WiderThan, has entered into three lines of credit with three Korean domestic banks with an aggregate maximum available limit of $4.3 million at interest rates ranging primarily from 1.3% to 1.63% over the rate earned on the underlying deposits. WiderThan has entered into a separate line of credit with a Korean domestic bank with maximum available limit of $1.1 million bearing interest at 6.0%. During the six months ended June 30, 2007 the Company did not draw on these lines of credit and there were no balances outstanding as of June 30, 2007 and December 31, 2006.

REALNETWORKS, INC. AND SUBSIDIARIES
NOTES TO UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

The Company s subsidiary, WiderThan India Pvt. Ltd., has entered into two separate lines of credit with a Korean bank in India with maximum available limit of $122,000 bearing interest at 10.25%. At June 30, 2007 the Company had $122,000 outstanding under these arrangements which is included in accrued and other liabilities in the accompanying unaudited condensed consolidated balance sheets.

The Company s subsidiary, WiderThan, uses corporate charge cards issued by a Korean domestic bank with an aggregate line of credit of up to $5.4 million. The charged amounts are generally payable in the following month depending on the billing cycle and are included in accounts payable in the accompanying unaudited condensed consolidated balance sheets. In general, the term of the arrangement is one year, with automatic renewal in April of each year. The arrangement may be terminated in writing by mutual agreement between the bank and the Company. The Company is not subject to any financial or other restrictive covenants under the terms of this arrangement.

The Company s subsidiary, WiderThan, has a letter of credit of up to $5.0 million with a Korean domestic bank for importing goods, with one-year maturity (renewable every April), and bears interest at 2.5% over the London Inter-Bank Offer Rate (LIBOR). Borrowings under this letter of credit are collateralized by import documents and goods being imported under such documentation. To the extent that the Company has any outstanding balance, the Company is subject to standard covenants and notice requirements under the terms of this facility, such as covenants to consult with the lender prior to engaging in certain events, which include, among others, mergers and acquisitions or sale of material assets or to furnish certain financial and other information. The Company is not, however, subject to any financial covenant requirements or other restrictive covenants that restrict the Company s ability to utilize this facility or to obtain financing elsewhere. During the six months ended June 30, 2007 the Company did not draw on the letter of credit and there was no balance outstanding as of June 30, 2007 and December 31, 2006.

The Company s subsidiary, WiderThan, has purchased guarantees amounting to $390,000 from Seoul Guarantee Insurance which guarantees payments for one year under certain supply contracts the Company has with a customer in Korea.

Litigation. In August 2005, a lawsuit was filed against the Company in the U.S. District Court for the District of Maryland by Ho Keung Tse, an individual residing in Hong Kong. The suit alleges that certain of the Company s products and services infringe the plaintiff s patent relating to the distribution of digital files, including sound tracks, music, video and executable software in a manner which restricts unauthorized use. The plaintiff seeks to enjoin the Company from the allegedly infringing activity and to recover treble damages for the alleged infringement. The Company s co-defendants were granted a motion to transfer the lawsuit from the District of Maryland to the Northern District of California in 2006. The Company disputes the plaintiff s allegations in the action and intends to vigorously defend itself.

In June 2005, an association representing certain music producers in the Republic of Korea sent the Company s WiderThan subsidiary a notice demanding payment of fees for the Company s use in its carrier application services since July 2004 of songs over which the association claims it holds certain rights. The Company used, and paid fees for, these songs under licensing agreements with independent music label companies and such agreements contain representations that these music label companies are the rightful, legal owner of the songs. Nevertheless, the association is claiming that it is the rightful owner. The Company is currently investigating the merit of the association s claims and the scope of any potential liability. Under the Company s licensing agreements, the independent music label companies are required to indemnify the Company for any losses resulting from their breach of representations. Should the Company become liable to the association in this matter, the Company intends to exercise its indemnity rights under its licensing agreements with the independent music label companies.

In June 2003, a lawsuit was filed against the Company and Listen.com, Inc. (Listen) in federal district court for the Northern District of Illinois by Friskit, Inc. (Friskit), alleging that certain features of the Company s and Listen s products and services willfully infringe certain patents relating to allowing users to search for streaming media files, to create custom playlists, and to listen to the streaming media file sequentially and continuously. Friskit sought to enjoin the Company from the alleged infringing activity and to recover treble damages from the alleged infringement. The court granted the Company s motion for summary judgment on July 26, 2007 and invalidated all claims on grounds of obviousness. Friskit has a 30-day period to appeal the court s ruling.

In December 2003, the Company filed suit against Microsoft Corporation (Microsoft) in the U.S. District Court for the Northern District of California, pursuant to U.S. and California antitrust laws, alleging that Microsoft has illegally used its monopoly power to restrict competition, limit consumer choice, and attempt to monopolize the field of digital media. On October 11, 2005, the Company and Microsoft entered into a settlement agreement pursuant to which the Company agreed to settle all antitrust disputes worldwide with Microsoft, including the U.S. litigation. Upon settlement of the legal disputes, the Company and Microsoft entered into two commercial agreements that provide for collaboration in digital music and casual games. The combined contractual payments related to the settlement agreement and the two commercial agreements to be made by Microsoft to the Company over the terms of the

REALNETWORKS, INC. AND SUBSIDIARIES
NOTES TO UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

agreements are $761.0 million. The Company had received such payments in full as of March 31, 2007. The Company recorded a gain of $60.7 million during the three months ended March 31, 2007 that is included in antitrust litigation benefit, net in the unaudited condensed consolidated statement of operations and comprehensive income. No such gain was recorded during the three months ended June 30, 2007. Gain of $57.9 million and $97.7 million, was recorded during the three and six ended June 30, 2006, respectively, that is included in antitrust litigation benefit, net in the unaudited condensed consolidated statement of operations and comprehensive income.

In April 2007, the Copyright Royalty Board (CRB) issued a decision setting new royalty rates for the use of sound recordings in Internet radio from 2006 through 2010. As part of the new rates, the CRB established a new minimum fee applicable to commercial webcasters, including the Company. The CRB determined that webcasters must pay a minimum fee of $500 per channel. The decision is not clear regarding how the minimum fee would apply to radio services like those delivered by the Company which enable users to customize the channel or which use an algorithm to help ensure that the channel reflects the relevant genre or artists. Currently, the CRB decision is being appealed to the United States Court of Appeals. Depending upon how the minimum fee provision is interpreted, if the CRB s minimum fee decision is upheld on appeal the Company could incur additional liability for minimum fees relating to its provision of Internet radio. At this time, the amount of this potential liability is not determinable. Prior to the April 2007 CRB decision, webcasting services were subject to a $2,500 per webcaster yearly minimum fee.

From time to time the Company is, and expects to continue to be, subject to legal proceedings and claims in the ordinary course of its business, including employment claims, contract-related claims, and claims of alleged infringement of third-party patents, trademarks and other intellectual property rights. These claims, including those described above, even if not meritorious, could force the Company to spend significant financial and managerial resources. The Company is not aware of any legal proceedings or claims that the Company believes will have, individually or taken together, a material adverse effect on the Company s business, prospects, financial condition or results of operations. However, the Company may incur substantial expenses in defending against third-party claims and certain pending claims are moving closer to trial. The Company expects that its potential costs of defending these claims may increase as the disputes move into the trial phase of the proceedings. In the event of a determination adverse to the Company, the Company may incur substantial monetary liability, and/or be required to change its business practices. Either of these could have a material adverse effect on the Company s financial position and results of operations.

Note 15. Segment Information

The Company operates in two business segments: Consumer Products and Services and Technology Products and Solutions, for which the Company receives revenue from its customers. The Company s Chief Operating Decision Maker is considered to be the Company s CEO Staff (CEOS), which is comprised of the Company s Chief Executive Officer, Chief Financial Officer, President, and Senior Vice Presidents. The CEOS reviews financial information presented on both a consolidated basis and on a business segment basis, accompanied by disaggregated information about products and services and geographical regions for purposes of making decisions and assessing financial performance. The CEOS reviews discrete financial information regarding profitability of the Company s Consumer Products and Services and Technology Products and Solutions segments and, therefore, the Company reports these as operating segments as defined by SFAS No. 131, *Disclosure About Segments of an Enterprise and Related Information.*

The Company s customers consist primarily of end users located in the U.S., Republic of Korea, and various foreign countries. Revenue by geographic region is as follows (in thousands):

	Three Months Ended June 30,		**Six Months Ended June 30,**	
	2007	**2006**	**2007**	**2006**
United States	$ 88,035	$ 66,542	$ 172,589	$ 132,242
Europe	20,522	15,925	38,232	29,830

Republic of Korea	18,885		37,284	
Rest of the World	8,729	6,942	17,538	13,939
Total net revenue	$ 136,171	$ 89,409	$ 265,643	$ 176,011

The Company s segments are defined as follows:

Consumer Products and Services segment primarily includes revenue from: digital media subscription services such as Rhapsody, RadioPass, GamePass and SuperPass; sales and distribution of third-party software and services; sales of digital content such as music and game downloads; sales of premium versions of RealPlayer and related products; and advertising. These products and services are

REALNETWORKS, INC. AND SUBSIDIARIES
NOTES TO UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

sold and provided primarily through the Internet and the Company charges customers credit cards at the time of sale. Billing periods for subscription services typically occur monthly, quarterly or annually, depending on the service purchased.

Technology Products and Solutions segment includes revenue from: sales of ringback tone, music-on-demand, video-on-demand, messaging, and information services; sales of media delivery system software, including Helix system software and related authoring and publishing tools, both directly to customers and indirectly through original equipment manufacturer (OEM) channels; support and maintenance services sold to customers who purchase software products; broadcast hosting services; and consulting and professional services that are offered to customers. These products and services are primarily sold to corporate customers.

Revenue by segment is as follows (in thousands):

	Three Months Ended June 30,		Six Months Ended June 30,	
	2007	2006	2007	2006
Consumer products and services	$ 87,115	$ 77,442	$ 172,155	$ 152,253
Technology products and solutions	49,056	11,967	93,488	23,758
Total net revenue	$ 136,171	$ 89,409	$ 265,643	$ 176,011

Consumer Products and Services revenue is comprised of the following (in thousands):

	Three Months Ended June 30,		Six Months Ended June 30,	
	2007	2006	2007	2006
Music	$ 36,801	$ 30,118	$ 70,928	$ 59,036
Media Software and services	25,419	26,127	52,430	53,404
Games	24,895	21,197	48,797	39,813
Total consumer products and service revenue	$ 87,115	$ 77,442	$ 172,155	$ 152,253

Long-lived assets, consisting of equipment, software, leasehold improvements, other intangible assets, and goodwill by geographic region are as follows (in thousands):

	June 30, 2007	December 31, 2006
United States	$ 175,030	$ 172,846
Republic of Korea	247,996	256,032
Europe	50,840	26,807
Rest of the World	7,455	6,289
Total long-lived assets	$ 481,321	$ 461,974

Net assets by geographic location are as follows (in thousands):

	June 30, 2007	December 31, 2006
United States	$ 516,961	$ 621,532
Republic of Korea	340,577	314,106
Europe	53,697	26,298
Rest of the World	8,171	7,830
Total net assets	$ 919,406	$ 969,766

REALNETWORKS, INC. AND SUBSIDIARIES
NOTES TO UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

Goodwill is assigned to the Company s segments as follows (in thousands):

	June 30, 2007	December 31, 2006
Consumer products and services	$ 137,568	$ 131,997
Technology products and solutions	187,441	177,125
Total goodwill	$ 325,009	$ 309,122

Operating expenses of both Consumer Products and Services and Technology Products and Solutions include costs directly attributable to those segments and an allocation of general and administrative and other corporate overhead costs. General and administrative and other corporate overhead costs are allocated to the segments and are generally based on the relative headcount of each segment. The accounting policies used to derive segment results are generally the same as those described in Note 1.

Reconciliation of segment operating income (loss) to income (loss) before income taxes for the three months ended June 30, 2007 is as follows (in thousands):

	Consumer Products and Services	Technology Products and Solutions	Reconciling Amounts	Consolidated
Net revenue	$ 87,115	$ 49,056	$	$ 136,171
Cost of revenue	28,898	20,301		49,199
Gross profit	58,217	28,755		86,972
Other operating expenses	54,425	37,724		92,149
Operating income (loss)	3,792	(8,969)		(5,177)
Total non-operating income, net			8,682	8,682
Income (loss) before income taxes	$ 3,792	$ (8,969)	$ 8,682	$ 3,505

Reconciliation of segment operating income (loss) to income (loss) before income taxes for the three months ended June 30, 2006 is as follows (in thousands):

	Consumer Products and Services	Technology Products and Solutions	Reconciling Amounts	Consolidated
Net revenue	$ 77,442	$ 11,967	$	$ 89,409
Cost of revenue	24,415	2,231		26,646

Gross profit	53,027	9,736		62,763
Antitrust litigation benefit, net			(57,858)	(57,858)
Other operating expenses	56,463	14,499		70,962
Operating income (loss)	(3,436)	(4,763)	57,858	49,659
Total non-operating income, net			11,740	11,740
Income (loss) before income taxes	$ (3,436)	$ (4,763)	$ 69,598	$ 61,399

Reconciliation of segment operating income (loss) to income (loss) before income taxes for the six months ended June 30, 2007 is as follows (in thousands):

	Consumer Products and Services	Technology Products and Solutions	Reconciling Amounts	Consolidated
Net revenue	$ 172,155	$ 93,488	$	$ 265,643
Cost of revenue	56,712	38,430		95,142
Gross profit	115,443	55,058		170,501
Antitrust litigation benefit, net			(60,747)	(60,747)
Other operating expenses	109,584	73,098		182,682
Operating income (loss)	5,859	(18,040)	60,747	48,566
Total non-operating income, net			18,119	18,119
Income (loss) before income taxes	$ 5,859	$ (18,040)	$ 78,866	$ 66,685

REALNETWORKS, INC. AND SUBSIDIARIES
NOTES TO UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

Reconciliation of segment operating income (loss) to income (loss) before income taxes for the six months ended June 30, 2006 is as follows (in thousands):

	Consumer Products and Services	Technology Products and Solutions	Reconciling Amounts	Consolidated
Net revenue	$ 152,253	$ 23,758	$	$ 176,011
Cost of revenue	49,166	4,233		53,399
Gross profit	103,087	19,525		122,612
Loss on excess office facilities			738	738
Antitrust litigation benefit, net			(97,693)	(97,693)
Other operating expenses	110,342	28,028		138,370
Operating income (loss)	(7,255)	(8,503)	96,955	81,197
Total non-operating income, net			19,836	19,836
Income (loss) before income taxes	$ (7,255)	$ (8,503)	$ 116,791	$ 101,033

Item 2. Management s Discussion and Analysis of Financial Condition and Results of Operations

This Quarterly Report on Form 10-Q and the documents incorporated herein by reference contain forward-looking statements that have been made pursuant to the provisions of the Private Securities Litigation Reform Act of 1995. These forward-looking statements are based on current expectations, estimates, and projections about RealNetworks industry, products, management s beliefs, and certain assumptions made by management. Words such as anticipates, expects, intends, plans, believes, seeks, estimates, and similar expressions are intended to identify forward-lo statements. Forward-looking statements include statements with respect to:

future revenues, income taxes, net income per diluted share, acquisition costs and related amortization, and other measures of results of operations;

the effects of acquiring WiderThan, Sony NetServices GmbH (SNS), and Exomi Oy (Exomi), including our position as a technology services provider for leading wireless carriers;

plans, strategies and expected opportunities for growth, increased profitability and innovation in 2007 and future years;

the expected growth and profitability of our Technology Products and Solutions business;

the financial performance and growth of our Games business, including future international growth;

the migration of our Media Software and Services businesses from general purpose subscription businesses toward premium services and free-to-consumer services, the popularity of the RealPlayer and our expected introduction of new products and innovations in our Media Software and Services business;

our ability to grow our Music business, including opportunities for us to become the platform of choice for the Consumer Electronics industry, the integration of our Rhapsody DNA into the digital devices of an expanding list of partners and our plans to introduce additional innovations;

the effect of future interoperability on our Music business, the significance of growth opportunities in the digital music market and our expectations for short-term progress and long-term success in our Music business;

our financial position, planned capital expenditures, and the availability of capital resources;

our expectations regarding acquisition activity in 2007 and our focus on the integration of completed acquisitions;

future competition; and

the degree of seasonality in our revenue.

These statements are not guarantees of future performance and actual actions or results may differ materially. These statements are subject to certain risks, uncertainties and assumptions that are difficult to predict, including those noted in the documents incorporated herein by reference. Particular attention should also be paid to the cautionary language in section Item 1 of Part II entitled Legal Proceedings and Item 1A of Part II entitled Risk Factors. RealNetworks undertakes no obligation to update publicly any forward-looking statements as a result of new information, future events or otherwise, unless required by law. Readers should, however, carefully review the risk factors included in other reports or documents filed by RealNetworks from time to time with the Securities and Exchange Commission, particularly the Quarterly Reports on Form 10-Q and any Current Reports on Form 8-K.

Overview

We are a leading creator of digital media services and software. Consumers use our services and software, such as Rhapsody, RealArcade, and RealPlayer to find, play, purchase, and manage free and premium digital content, including music, games, and video. Broadcasters, cable and wireless communication companies, media companies and enterprises, such as Verizon Wireless and AT&T in the U.S. and SK Telecom in the Republic of Korea (South Korea), use our digital media applications and services to create, secure and deliver digital media to PCs, mobile phones, portable music players and other consumer electronics devices and to provide entertainment services to their subscribers.

Our strategy is to continue to leverage our Internet and mobile media technology, business partnerships and worldwide user base to increase our sales of digital media products, services and advertising in order to build a sustainable and profitable global business. We intend to continue our strategy of expanding our products and services beyond the PC to mobile devices and to create compelling digital media and entertainment experiences on a variety of devices. We also intend to use our strong cash position to continue to seek acquisition opportunities to further our strategic initiatives and to enhance our competitive position.

In recent years, we have focused our efforts on growing our consumer businesses through both internal initiatives and strategic acquisitions of businesses and technologies. We have also increased our focus on free-to-consumer products and services, such as our Rhapsody.com website and our introduction of downloadable games containing in-game advertising. These products and services generate advertising revenue and are also designed to increase the exposure of our paid digital music and games products and services to consumers. As a result, revenue in our Consumer Products and Services segment grew 12% from the second quarter of 2006.

Revenue in 2007 from our Technology Products and Solutions segment grew significantly compared to 2006, increasing by 310%. This increase was driven primarily by our acquisitions of WiderThan in October 2006 and SNS during the second quarter of 2007. WiderThan is a leader in delivering integrated digital entertainment solutions to communications service providers worldwide. WiderThan s applications, content, and services enable wireless carriers to provide a broad range of mobile entertainment to their subscribers, including ringback tones, music-on-demand, mobile games, ringtones, messaging, and information services. We expect revenue in our Technology Products and Solutions segment to grow as a percentage of total revenue and in absolute dollars during 2007 as it will include a full year of the results of operations of WiderThan. We also believe that WiderThan s technology platform and history of wireless innovation will assist our strategy of moving our content and services beyond the PC to multiple platforms.

On May 15, 2007, we acquired all of the outstanding securities of SNS for $12.8 million in cash payments, including $902,000 in direct acquisition related costs. SNS is located in Salzburg, Austria and is a provider of end-to-end white label digital music services to mobile operators in Europe. We believe that combining SNS assets and technology with our existing business will enhance our digital music offerings in the European market.

On June 8, 2007, we acquired all of the outstanding securities of Exomi in exchange for $11.2 million in cash payments, including $468,000 in direct acquisition related costs. We may be obligated to pay an additional 3.6 million ($4.9 million at June 30, 2007) over a three-year period, dependent on whether certain performance criteria are achieved. Exomi is located in Helsinki, Finland and is a provider of short message service (SMS) messaging and gateway products and services with customers primarily in Europe and Latin America. We believe that combining Exomi s assets and network with our products and services will enhance our presence in the Latin American market.

We manage our business, and correspondingly report revenue, based on two operating segments: Consumer Products and Services and Technology Products and Solutions.

Consumer Products and Services segment primarily includes revenue from: digital media subscription services such as Rhapsody, RadioPass, GamePass and SuperPass; sales and distribution of third-party software and services; sales of digital content such as music and game downloads; sales of premium versions of our RealPlayer and related products; and advertising. This segment primarily includes sales of these products directly to consumers and also includes sales of these products through distribution partners such as broadband service providers and retailers.

Technology Products and Solutions segment includes revenue from: sales of ringback tone, music-on-demand, video-on-demand, messaging, and information services; sales of our media delivery system software, including Helix system software and related authoring and publishing tools, both directly to customers and indirectly through original equipment manufacturer (OEM) channels; support and maintenance services that we sell to customers who purchase our software products; broadcast hosting services; and consulting and professional services we offer to our customers.

Critical Accounting Policies and Estimates

The preparation of our financial statements requires us to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenue and expenses during the reported period. Our critical accounting policies and estimates are as follows:

Revenue recognition;

Estimating music publishing rights and music royalty accruals;

Recoverability of deferred costs;

Estimating allowances for doubtful accounts and sales returns;

Estimating losses on excess office facilities;

Determining whether declines in the fair value of investments are other-than-temporary and estimating fair market value of investments in privately held companies;

- Valuation of other intangible assets;
- Valuation of goodwill;
- Stock-based compensation; and
- Accounting for income taxes.

Revenue Recognition. We recognize revenue in accordance with the following authoritative literature: AICPA Statement of Position (SOP) No. 97-2, *Software Revenue Recognition;* SOP No. 98-9, *Software Revenue Recognition with Respect to Certain Arrangements*; SOP No. 81-1, *Accounting for Performance of Construction-Type and Certain Production-Type Contracts*; Securities and Exchange Commission (SEC) Staff Accounting Bulletin (SAB) No. 104, *Revenue Recognition in Financial Statements*; Financial

Accounting Standards Board s Emerging Issues Task Force (EITF) Issue No. 00-21, *Revenue Arrangements with Multiple Deliverables;* and EITF Issue No. 99-19, *Reporting Revenue Gross as a Principal versus Net as an Agent.* Generally we recognize revenue when there is persuasive evidence of an arrangement, the fee is fixed or determinable, the product or services have been delivered and collectibility of the resulting receivable is reasonably assured.

Consumer subscription products are paid in advance, typically for monthly, quarterly or annual periods. Subscription revenue is recognized ratably over the related subscription period. Revenue from sales of downloaded individual tracks, albums and games are recognized at the time the music or game is made available, digitally, to the end user.

We recognize revenue under the residual method for multiple element software arrangements when VSOE exists for all of the undelivered elements of the arrangement, but does not exist for one or more of the delivered elements in the arrangement, under SOP No. 97-2. Under the residual method, at the outset of the arrangement with a customer, we defer revenue for the fair value of the arrangement s undelivered elements such as Post Contract Support (PCS), and recognize revenue for the remainder of the arrangement fee attributable to the elements initially delivered, such as software licenses. VSOE for PCS is established on standard products for which no installation or customization is required based upon amount charged when PCS is sold separately. For multiple element software arrangements involving significant production, modification, or customization of the software, which are accounted for in accordance with the provisions of SOP No. 81-1, VSOE for PCS is established if customers have an optional renewal rate specified in the arrangement and the rate is substantive.

We have arrangements whereby customers pay one price for multiple products and services and in some cases, involve a combination of products and services. For arrangements with multiple deliverables, revenue is recognized upon the delivery of the individual deliverables in accordance with EITF Issue No. 00-21. In the event that there is no objective and reliable evidence of fair value of the delivered items, the revenue recognized upon delivery is the total arrangement consideration less the fair value of the undelivered items. We apply significant judgment in establishing the fair value of multiple elements within revenue arrangements.

We recognize revenue on a gross or net basis, in accordance with EITF Issue No. 99-19. In most arrangements, we contract directly with end user customers, are the primary obligor and carry all collectibility risk. In such arrangements we report revenue on a gross basis. In some cases, we utilize third-party distributors to sell products or services directly to end user customers and carry no collectibility risk. In such instances we report revenue on a net basis.

Revenue generated from advertising appearing on our websites and from advertising included in our products is recognized as revenue as the delivery of the advertising occurs.

Music Publishing Rights and Music Royalty Accruals. We must make estimates of amounts owed related to our music publishing rights and music royalties for our domestic and international music services. Material differences may result in the amount and timing of our expense for any period if management made different judgments or utilized different estimates. Under copyright law, we may be required to pay licensing fees for digital sound recordings and compositions we deliver. Copyright law generally does not specify the rate and terms of the licenses, which are determined by voluntary negotiations among the parties or, for certain compulsory licenses where voluntary negotiations are unsuccessful, by arbitration. There are certain geographies and agencies for which we have not yet completed negotiations with regard to the royalty rate to be applied to the current or historic sales of our digital music offerings. Our estimates are based on contracted or statutory rates, when established, or management s best estimates based on facts and circumstances regarding the specific music services and agreements in similar geographies or with similar agencies. While we base our estimates on historical experience and on various other assumptions that management believes to be reasonable under the circumstances, actual results may differ materially from these estimates under different assumptions or conditions.

Recoverability of Deferred Costs. We defer costs on projects for service revenue and system sales. Deferred costs consist primarily of direct and incremental costs to customize and install systems, as defined in individual customer contracts, including costs to acquire hardware and software from third parties and payroll costs for our employees and other third parties.

We recognize such costs in accordance with our revenue recognition policy by contract. For revenue recognized under the completed contract method, costs are deferred until the products are delivered, or upon completion of services or, where applicable, customer acceptance. For revenue recognized under the percentage of completion method, costs are recognized as products are delivered or services are provided in accordance with the percentage of completion calculation. For revenue recognized ratably over the term of the contract, costs are recognized ratably over the term of the contract, commencing on the date of revenue recognition. At each balance sheet date, we review deferred costs, to ensure they are ultimately recoverable. Any anticipated losses on uncompleted contracts are recognized when evidence indicates the estimated total cost of a contract exceeds its estimated total revenue.

Allowances for Doubtful Accounts and Sales Returns. We must make estimates of the uncollectibility of our accounts receivable. We specifically analyze the age of accounts receivable and historical bad debts, customer credit-worthiness and current economic trends when evaluating the adequacy of the allowance for doubtful accounts. Similarly, we must make estimates of potential future product returns related to current period revenue. We analyze historical returns, current economic trends, and changes in customer demand and acceptance of our products when evaluating the adequacy of the sales returns allowance. Significant judgments and estimates must be made and used in connection with establishing allowances for doubtful accounts and sales returns in any accounting period. Material differences may result in the amount and timing of our revenue for any period if we were to make different judgments or utilize different estimates.

Accrued Loss on Excess Office Facilities. We made significant estimates in determining the appropriate amount of accrued loss on excess office facilities. If we made different estimates, our loss on excess office facilities could be significantly different from that recorded, which could have a material impact on our operating results. Our original estimate has been revised in previous periods in response to changes in market conditions for commercial real estate in the area where the excess office facilities are located, or to reflect negotiated changes in sublease rates charged to occupying tenants. The significant factors we consider when making our estimates are discussed in the section entitled Loss on Excess Office Facilities.

Impairment of Investments. We periodically evaluate whether any declines in the fair value of our investments are other-than-temporary. Significant judgments and estimates must be made to assess whether an other-than-temporary decline in fair value of investments has occurred and to estimate the fair value of investments in privately held companies. Material differences may result in the amount and timing of any impairment charge if we were to make different judgments or utilize different estimates.

Valuation of Other Intangible Assets. Other intangible assets consist primarily of fair value of customer agreements and contracts, developed technology, trademarks, patents, and tradenames acquired in business combinations. Other intangible assets are amortized on a straight line basis over their useful lives and are subject to periodic review for impairment. The initial recording and periodic review processes require extensive use of estimates and assumptions, including estimates of undiscounted future cash flows expected to be generated by the acquired assets. Should conditions be different than management s current assessment, material write-downs of intangible assets may be required. We periodically review the estimated remaining useful lives of other intangible assets. A reduction in the estimated remaining useful life could result in accelerated amortization expense in future periods.

Valuation of Goodwill. We assess the impairment of goodwill on an annual basis, in our fourth quarter, or whenever events or changes in circumstances indicate that the fair value of the reporting unit to which goodwill relates is less than the carrying value. Factors we consider important which could trigger an impairment review include the following:

poor economic performance relative to historical or projected future operating results;

significant negative industry, economic or company specific trends;

changes in the manner of our use of the assets or the plans for our business; and

loss of key personnel.

If we were to determine that the fair value of a reporting unit was less than its carrying value, including goodwill, based upon the annual test or the existence of one or more of the above indicators of impairment, we would measure impairment based on a comparison of the implied fair value of reporting unit goodwill with the carrying amount of goodwill. The implied fair value of goodwill is determined by allocating the fair value of a reporting unit to its assets (recognized and unrecognized) and liabilities in a manner similar to a purchase price allocation. The residual fair value after this allocation is the implied fair value of the goodwill of the reporting unit. To the extent the carrying amount of reporting unit goodwill is greater than the implied fair value of reporting unit goodwill, we would record an impairment charge for the difference. Judgment is required in determining our reporting units and assessing fair value of the reporting units. There were no impairments related to goodwill in any of the periods presented.

Stock-Based Compensation. We account for stock-based compensation in accordance with Statement of Financial Accounting Standards (SFAS) No. 123R, *Share-Based Payment*. Under the provisions of SFAS No. 123R, which we adopted as of January 1, 2006, stock-based compensation cost is estimated at the grant date based on the award s fair-value as calculated by the Black-Scholes option-pricing model and is recognized as expense over the requisite service period, which is the vesting period. The Black-Scholes model requires various highly judgmental assumptions including volatility and expected option life. If any of the assumptions used in the Black-Scholes model change significantly, stock-based compensation expense may differ materially in the future from the amounts recorded in our consolidated statement of operations. We are required to estimate forfeitures at the time of grant and revise those estimates in subsequent periods if actual forfeitures differ from those estimates. We use historical data to estimate pre-vesting option forfeitures and record stock-based compensation expense only for those awards that are expected to vest.

Accounting for Income Taxes. We use the asset and liability method of accounting for income taxes. Under this method, income tax expense is recognized for the amount of taxes payable or refundable for the current year. In addition, deferred tax assets and liabilities are recognized for the expected future tax consequences of temporary differences between the financial reporting and tax bases of assets and liabilities, and for operating losses and tax credit carryforwards. Deferred tax assets and liabilities and operating loss and tax credit carryforwards are measured using enacted tax rates expected to apply to taxable income in the years in which those temporary differences and operating loss and tax credit carryforwards are expected to be recovered or settled. We must make assumptions, judgments and estimates to determine current provision for income taxes, deferred tax assets and liabilities and any valuation allowance to be recorded against deferred tax assets. Our judgments, assumptions, and estimates relative to the current provision for income tax take into account current tax laws, our interpretation of current tax laws and possible outcomes of future audits conducted by foreign and domestic tax authorities. Changes in tax law or our interpretation of tax laws and future tax audits could significantly impact the amounts provided for income taxes in our consolidated financial statements.

We must periodically assess the likelihood that our deferred tax assets will be recovered from future taxable income, and to the extent that recovery is not likely, a valuation allowance must be established. The establishment of a valuation allowance and increases to such an allowance result in either increases to income tax expense or reduction of income tax benefit in the statement of operations. Factors we consider in making such an assessment include, but are not limited to: past performance and our expectation of future taxable income, macro-economic conditions and issues facing our industry, existing contracts, our ability to project future results and any appreciation of our investments and other assets.

We have not provided for U.S. deferred income taxes or withholding taxes on non-U.S. subsidiaries undistributed earnings. These earnings are intended to be permanently reinvested in operations outside of the U.S. If these amounts were distributed to the U.S., in the form of dividends or otherwise, we could be subject to additional U.S. income taxes. It is not practicable to determine the U.S. federal income tax liability or benefit on such earnings due to the availability of foreign tax credits and the complexity of the computation, if such earnings were not deemed to be permanently reinvested.

In June 2006, the FASB issued Financial Interpretation (FIN) No. 48, *Accounting for Uncertainty in Income Taxes an interpretation of FASB Statement No. 109.* FIN No. 48 clarifies the accounting for uncertainty in income taxes recognized in an enterprise s financial statements in accordance with SFAS No. 109, *Accounting for Income Taxes*, and prescribes a recognition threshold and measurement process for financial statement recognition and measurement of tax positions taken or expected to be taken in tax returns. FIN No. 48 also provides guidance on derecognition, classification, interest and penalties, accounting in interim periods, disclosure and transition. On January 1, 2007, date of adoption of FIN No. 48, we had $7.5 million of unrecognized tax benefits, of which $7.2 million would affect the effective tax rate if recognized. Although the implementation of FIN No. 48 did not impact the amount of liability for unrecognized tax benefits, we reclassified $5.3 million of liability for unrecognized tax benefits from current income taxes payable to other long-term liabilities to conform with the balance sheet presentation requirements of FIN No. 48.

In accordance with FIN No. 48, we recognize potential accrued interest and penalties related to unrecognized tax benefits as a component of income tax expense. As of January 1, 2007, we had approximately $300,000 of accrued interest and penalties related to uncertain tax positions, which is included as a component of the $5.3 million of unrecognized tax benefit noted above. To the extent interest and penalties are not assessed with respect to uncertain tax positions, amounts accrued will be reduced and reflected as a reduction of the overall income tax provision. As of June 30, 2007, we do not anticipate that total unrecognized tax benefits will significantly change within the next twelve months.

We file numerous consolidated and separate income tax returns in the United States Federal, state, local, and foreign jurisdictions. With few exceptions, we are no longer subject to United States Federal, state, local, or foreign income tax examinations for years before 1993.

Revenue by Segment

Revenue by segment is as follows (dollars in thousands):

	Three Months Ended June 30,			Six Months Ended June 30,		
	2007	Change	2006	2007	Change	2006
Consumer products and services	$ 87,115	12%	$ 77,442	$ 172,155	13%	$ 152,253
Technology products and solutions	49,056	310	11,967	93,488	294	23,758
Total net revenue	$ 136,171	52%	$ 89,409	$ 265,643	51%	$ 176,011

Revenue by segment as a percentage of total net revenue is as follows:

	Three Months Ended June 30,		Six Months Ended June 30,	
	2007	2006	2007	2006
Consumer products and services	64%	87%	65%	87%
Technology products and solutions	36	13	35	13
Total net revenue	100%	100%	100%	100%

Consumer Products and Services. Consumer Products and Services primarily includes revenue from: digital media subscription services such as Rhapsody, RadioPass, GamePass, FunPass and SuperPass and stand-alone subscriptions; sales and distribution of third-party software and services; sales of digital content such as music and game downloads; sales of premium versions of our RealPlayer and related products; and advertising. These products and services are sold and provided primarily through the Internet and we charge customers credit cards at the time of sale. Billings for subscription services typically occur monthly, quarterly or annually, depending on the service purchased.

Consumer Products and Services revenue increased 12% and 13%, respectively, during the three and six months ended June 30, 2007 compared to the three and six months ended June 30, 2006, due primarily to increased sales of our Music and Games products. Additional factors contributing to the change in revenue are discussed below in the sections included within Consumer Products and Services revenue. We believe the growth in our Music and Games is due in part to the continued shift in our marketing and promotional efforts to these services as well as product improvements and increasing consumer acceptance and adoption of digital media products and services. We cannot predict with accuracy how these product offerings will perform in the future, at what rate digital media products and services will grow, if at all, or the nature or potential impact of anticipated competition.

Technology Products and Solutions. Technology Products and Solutions revenue is derived from products and services that enable wireless carriers, cable companies, and other media and communications companies to distribute digital media content to PCs, mobile phones, and other non-PC devices. Technology Products and Solutions that we sell as application services consist of ringback tones, music-on-demand, video-on-demand, and inter-carrier messaging, and are primarily sold to wireless carriers. Technology Products and Solutions that we sell as software consist of Helix system software and related authoring and publishing tools, digital rights management technology, messaging gateways, and support and maintenance services that we sell to customers who purchase these products. We also offer broadcast hosting and consulting services to our customers. These products and services are primarily sold to corporate, government and educational customers. We do not require collateral from our customers, but we often require payment before or at the time products and services are delivered. Many of our customers are given standard commercial credit terms, and for these customers we do not require payment before products and services are delivered.

Technology Products and Solutions revenue increased 310% and 294%, respectively, during the three and six months ended June 30, 2007 compared to the three and six months ended June 30, 2006, due primarily to our acquisitions of WiderThan (acquired in October 2006) and SNS (acquired in May 2007). For the remainder of 2007, we expect Technology Products and Solutions revenue to continue to increase in absolute dollars and as a percentage of total revenue as compared to the same period in 2006 because future quarters in 2007 will include revenue from these acquisitions and from our acquisition of Exomi completed in June 2007. We also believe that sales of certain of our business software products will continue to be substantially affected by Microsoft s continuing practice of bundling its competing Windows Media Player and server software for free with its Windows operating system products. No assurance can be given when, or if, we will experience increased sales of our Technology Products and Solutions to customers in these markets.

Consumer Products and Services Revenue

A further analysis of our Consumer Products and Services revenue is as follows (dollars in thousands):

	Three Months Ended June 30,			Six Months Ended June 30,		
	2007	Change	2006	2007	Change	2006
Music	$ 36,801	22%	$ 30,118	$ 70,928	20%	$ 59,036
Media software and services	25,419	(3)	26,127	52,430	(2)	53,404
Games	24,895	17	21,197	48,797	23	39,813
Total consumer products and services revenue	$ 87,115	12%	$ 77,442	$ 172,155	13%	$ 152,253

Music. Music revenue primarily includes revenue from: our Rhapsody and RadioPass subscription services; sales of digital music content through our Rhapsody service and our RealPlayer music store; and advertising from our music websites. Music revenue increased 22% during the quarter ended June 30, 2007 compared to the quarter ended June 30, 2006, due primarily to growth in subscription revenue from our subscription-based music products and advertising, which together accounted for all of this increase.

Music revenue increased 20% during the six months ended June 30, 2007 compared to the six months ended June 30, 2006, due primarily to growth in subscription revenue from our subscription-based music products and advertising, which together accounted for this increase. We believe the continued growth of our Music revenue is due primarily to the broader acceptance of paid online music services and the increased focus of our marketing efforts on our music offerings.

Media Software and Services. Media Software and Services revenue primarily includes revenue from: our SuperPass and stand-alone premium video subscription services; RealPlayer Plus and related products; sales and distribution of third-party software products; and all advertising other than that related directly to our Music and Games businesses. Media Software and Services revenue decreased 3% and 2%, respectively, during the quarter and six months ended June 30, 2007 compared to the quarter and six months ended June 30, 2006. The decreases were due primarily to a shift in our marketing and promotional efforts towards our Music and Games subscription services, which we believe represent a greater growth opportunity for us.

Games. Games revenue primarily includes revenue from: the sale of individual games through our RealArcade service and our Games related websites including GameHouse, Mr. Goodliving, Zylom (acquired in January 2006), and Atrativa (acquired in November 2006); our GamePass and FunPass subscription service; and advertising through RealArcade and our Games related websites. Games revenue increased 17% and 23%, respectively, during the quarter and six months ended June 30, 2007 compared to the quarter and six months ended June 30, 2006, due primarily to increased advertising and subscription revenue generated through our RealArcade service and our websites, including Zylom and GameHouse. Advertising and subscription revenue accounted for 83% and 89%, respectively, of this revenue increase; no other single factor contributed materially to the change during the periods. We believe the increased focus of our marketing efforts on our Games business, the addition of new game titles to our RealArcade, GamePass, and FunPass offerings, and our focus on in-game advertising, will contribute to continued growth in our Games business.

Geographic Revenue

Revenue by geographic region is as follows (dollars in thousands):

	Three Months Ended June 30,			Six Months Ended June 30,		
	2007	Change	2006	2007	Change	2006
United States	$ 88,035	32%	$ 66,542	$ 172,589	31%	$ 132,242
Europe	20,522	29	15,925	38,232	28	29,830
Republic of Korea	18,885	n/a		37,284	n/a	
Rest of the world	8,729	26	6,942	17,538	26	13,939
Total net revenue	$ 136,171	52%	$ 89,409	$ 265,643	51%	$ 176,011

Revenue in the U.S. increased 32% and 31%, respectively, during the quarter and six months ended June 30, 2007 compared to the quarter and six months ended June 30, 2006, due primarily to our acquisition of WiderThan and the growth of our Music and Games businesses. See Consumer Products and Services Revenue *Music* and *Games* above for further discussion of these changes. Revenue in Europe increased 29% and 28%, respectively, during the quarter and six months ended June 30, 2007 compared to the quarter and six months ended June 30, 2006, due primarily to the continued growth of our Games business and the acquisition of SNS and Zylom. Revenue in the Republic of Korea resulted directly from our acquisition of WiderThan.

Revenue

License fees and Service revenue in accordance with SEC regulations, is as follows (dollars in thousands):

	Three Months Ended June 30,			Six Months Ended June 30,		
	2007	Change	2006	2007	Change	2006
License fees	$ 22,212	(3)%	$ 22,850	$ 44,049	(3)%	$ 45,486

Service revenue	113,959	71	66,559	221,594	70	130,525
Total net revenue	$ 136,171	52%	$ 89,409	$ 265,643	51%	$ 176,011

License fees and Service revenue as a percentage of total revenue is as follows:

	Three Months Ended June 30,		Six Months Ended June 30,	
	2007	2006	2007	2006
License fees	16%	26%	17%	26%
Service revenue	84	74	83	74
Total net revenue	100%	100%	100%	100%

License Fees. License fees primarily include revenue from: sales of content such as game downloads and digital music tracks; sales of our media delivery system software; sales of premium versions of our RealPlayer Plus and related products; sales of messaging gateways to mobile carriers; and sales of third-party products. License fees include revenue from both our Consumer Products and Services and Technology Products and Solutions segments. A decrease in online sales of individual tracks through our Rhapsody music subscription service and our RealPlayer Music Store accounted for nearly all of the 3% decrease in license fees during each of the quarter and six months ended June 30, 2007 compared to the quarter and six months ended June 30, 2006.

Service Revenue. Service revenue primarily includes revenue from: digital media subscription services such as SuperPass, Rhapsody, RadioPass, GamePass, FunPass and stand-alone subscriptions; sales of application services sold to wireless carriers to deliver ringback tones, music-on-demand, video-on-demand, messaging, and information services to wireless carriers customers; support and maintenance services that we sell to customers who purchase our software products; broadcast hosting and consulting services that we offer to our customers; distribution of third-party software; and advertising. Service revenue includes revenue from both our Consumer Products and Services and Technology Products and Solutions segments. Service revenue increased 71% and 70%, respectively, during the quarter and six months ended June 30, 2007 compared to the quarter and six months ended June 30, 2006. Sales of application services to wireless carriers, including ringback tones, music-on-demand, inter-carrier messaging, and video-on-demand services, primarily obtained from our acquisition of WiderThan, accounted for 82% and 79%, respectively, of the increases in service revenue; no other single factor contributed materially to the change during the periods.

Deferred Revenue

Deferred revenue is comprised of unrecognized revenue and prepayments related to application services, unearned subscription services, support contracts, prepayments under OEM arrangements and other prepayments for which the earnings process has not been completed. Total deferred revenue at June 30, 2007 was $40.0 million compared to $27.6 million at December 31, 2006. Substantially all of the increase in deferred revenue was due to prepayments from wireless carriers for applications to deliver ringback tone, music-on-demand, and video-on-demand services.

Cost of Revenue by Segment

Cost of revenue by segment is as follows (dollars in thousands):

	Three Months Ended June 30,			Six Months Ended June 30,		
	2007	Change	2006	2007	Change	2006
Consumer products and services	$ 28,898	18%	$ 24,415	$ 56,712	15%	$ 49,166
Technology products and solutions	20,301	810	2,231	38,430	808	4,233
Total cost of revenue	$ 49,199	85%	$ 26,646	$ 95,142	78%	$ 53,399

Cost of revenue as a percentage of segment revenue is as follows:

	Three Months Ended June 30,		Six Months Ended June 30,	
	2007	2006	2007	2006
Consumer products and services	33%	32%	33%	32%
Technology products and solutions	41	19	41	18
Total cost of revenue	36	30	36	30

Cost of Consumer Products and Services. Cost of Consumer Products and Services revenue consist primarily of cost of content and delivery of the content included in our digital media subscription service offerings; royalties paid on sales of games, music and other third-party products; amounts paid for licensed technology; costs of product media, duplication, manuals and packaging materials; hardware devices and accessories; and fees paid to third-party vendors for order fulfillment and support services. Cost of Consumer Products and Services increased 18% and 15%, respectively, during the quarter and six months ended June 30, 2007 compared to the quarter and six months ended June 30, 2006. Increase in content and licensing costs related to increase in the number of Music and Games products and services sold resulted in 83% and 92%, respectively, of these increases. No other single factor contributed materially to the change.

Cost of Technology Products and Solutions. Cost of Technology Products and Solutions revenue includes amounts paid for licensed technology, costs of product media, duplication, manuals, packaging materials, fees paid to third-party vendors for order fulfillment, cost of personnel providing support and consulting services, and expenses incurred in providing our streaming media hosting services. Increased personnel, support, and related costs for the acquired operations of WiderThan accounted for substantially all of the 810% and 808%, respectively, increase in cost of Technology Products and Solutions revenue during the quarter and six months ended June 30, 2007 compared to the quarter and six months ended June 30, 2006.

Cost of Revenue

Cost of revenue is as follows (dollars in thousands):

	Three Months Ended June 30,			Six Months Ended June 30,		
	2007	Change	2006	2007	Change	2006
License fees	$ 7,882	(16)%	$ 9,329	$ 16,174	(16)%	$ 19,190
Service revenue	41,317	139	17,317	78,968	131	34,209
Total cost of revenue	$ 49,199	85%	$ 26,646	$ 95,142	78%	$ 53,399

Cost of revenue as a percentage of related revenue is as follows:

	Three Months Ended June 30,		Six Months Ended June 30,	
	2007	2006	2007	2006
License fees	35%	41%	37%	42%
Service revenue	36	26	36	26
Total cost of revenue	36	30	36	30

Cost of License Fees. Cost of license fees includes royalties paid on sales of games, music and other third-party products, amounts paid for licensed technology, amortization of acquired technology, costs of product media, duplication, manuals, packaging materials, and fees paid to third-party vendors for order fulfillment. Cost of license fees decreased 16% in each of the quarter and six months ended June 30, 2007 compared to the quarter and six months ended June 30, 2006 due primarily to the decrease in online sales of individual songs through our Rhapsody subscription service and our RealPlayer Music Store as well as lower amortization of acquired technology related to assets that became fully amortized during the periods. Decreases in these costs accounted for 59% and 51% of the decline in the respective periods; no other single factor contributed materially to the change.

Cost of Service Revenue. Cost of service revenue includes the cost of content and delivery of the content included in our digital media subscription and mobile service offerings, cost of in-house and contract personnel providing support, amortization of acquired technology, and consulting services, royalties, and expenses incurred in providing our streaming media hosting services. Content costs are expensed over the period the content is available to our subscription services customers. Cost of service revenue increased 139% and 131%, respectively, during the quarter and six months ended June 30, 2007 compared to the quarter and six months ended June 30, 2006, due primarily to the acquisition of WiderThan. Costs related to the development and delivery of application services sold to wireless carriers accounted for 73% and 75%, respectively, of the increase in cost of service revenue; no other single factor contributed materially to the change during the periods.

Operating Expenses

Research and Development

Research and development expenses consist primarily of salaries and related personnel costs, expense associated with stock-based compensation, and consulting fees associated with product development. To date, all research and development costs have been expensed as incurred because technological feasibility for software products is generally not established until substantially all development is complete. Research and developments costs and changes are as follows (dollars in thousands):

	Three Months Ended June 30,			Six Months Ended June 30,		
	2007	Change	2006	2007	Change	2006
Research and development	$25,005	34%	$18,684	$48,484	32%	$36,783
As a percentage of total net revenue	18%		21%	18%		21%

Research and development expenses, including non-cash stock-based compensation, increased 34% during the quarter ended June 30, 2007 compared to the quarter ended June 30, 2006, due primarily to an overall increase in personnel and related costs, which include costs related to WiderThan (acquired in October 2007) and SNS (acquired in May 2007). Personnel and related costs accounted for 65% of the total increase in research and development costs; no other single factor contributed materially to the increase during the period. The decrease in research and development expenses as a percentage of total net revenue is due primarily to a higher growth in total net revenue.

Research and development expenses increased 32% during the six months ended June 30, 2007 compared to the six months ended June 30, 2006, due primarily to an overall increase in personnel and related costs, which include costs related to WiderThan (acquired in October 2007) and SNS (acquired in May 2007). These personnel and related costs accounted for 66% of the total increase in research and development costs; no other single factor contributed materially to the increase during the period. The decrease in research and development expenses as a percentage of total net revenue is due primarily to a higher growth in total net revenue.

Sales and Marketing

Sales and marketing expenses consist primarily of salaries and related personnel costs, sales commissions, amortization of certain intangible assets capitalized in our acquisitions, credit card fees, subscriber acquisition costs, consulting fees, trade show expenses, advertising costs and costs of marketing collateral. Sales and marketing costs and changes are as follows (dollars in thousands):

	Three Months Ended June 30,			Six Months Ended June 30,		
	2007	Change	2006	2007	Change	2006
Sales and marketing	$50,081	32%	$37,961	$99,781	35%	$74,044
As a percentage of total net revenue	37%		42%	38%		42%

Sales and marketing expenses, including non-cash stock-based compensation, increased 32% during the quarter ended June 30, 2007 compared to the quarter ended June 30, 2006. Personnel and related costs accounted for 47% of the total increase in sales and marketing expenses including costs related to WiderThan (acquired in October 2007) and SNS (acquired in May 2007). An additional 27% of the increase in sales and marketing expenses was due to an increase in amortization of other intangible assets capitalized in our acquisition of WiderThan and SNS. No other single factor contributed materially to the increase during the period. The decrease in sales and marketing expenses as a percentage of total net revenue is due to a higher growth in total net revenue.

Sales and marketing expenses, including non-cash stock-based compensation, increased 35% during the six months ended June 30, 2007 compared to the six months ended June 30, 2006. Personnel and related costs accounted for 48% of the total increase in sales and marketing expenses including costs related to WiderThan (acquired in October 2007) and SNS (acquired in May 2007). An additional 25% of the increase in sales and marketing expenses was due to an increase in amortization of other intangible assets capitalized in our acquisition of WiderThan and SNS. No other single factor contributed materially to the increase during the period. The decrease in sales and marketing expenses as a percentage of total net revenue is due to a higher growth in total net revenue.

General and Administrative

General and administrative expenses consist primarily of salaries and related personnel costs, fees for professional and temporary services and contractor costs, stock-based compensation, and other general corporate costs. General and administrative costs and changes are as follows (dollars in thousands):

	Three Months Ended June 30,			Six Months Ended June 30,		
	2007	Change	2006	2007	Change	2006
General and administrative	$17,063	19%	$14,317	$34,417	25%	$27,543
As a percentage of total net revenue	13%		16%	13%		16%

General and administrative expenses, including non-cash stock-based compensation, increased 19% during the quarter ended June 30, 2007 compared to the quarter ended June 30, 2006. Personnel and related costs, including costs related to WiderThan (acquired in October 2007) and SNS (acquired in May 2007) and consulting and professional services accounted for substantially all of the increase in general and administrative expenses during the period. The decrease in general and administrative expenses as a percentage of total net revenue is due to a higher growth in total net revenue.

General and administrative expenses, including non-cash stock-based compensation, increased 25% during the six months ended June 30, 2007 compared to the six months ended June 30, 2006. Personnel and related costs, including costs related to WiderThan (acquired in October 2007) and SNS (acquired in May 2007) and consulting and professional services accounted for substantially all of the increase in general and administrative expenses during the period. The decrease in general and administrative expenses as a percentage of total net revenue is due to a higher growth in total net revenue.

Loss on Excess Office Facilities

In October 2000, we entered into a 10-year lease agreement for additional office space located near our corporate headquarters in Seattle, Washington. Due to a subsequent decline in the market for office space in Seattle and our re-assessment of our facilities requirements in 2001, we accrued for estimated future losses on excess office facilities. Additionally, we accrued for estimated future losses on this facility in 2002 and 2003 based on changes in market conditions and securing tenants at rates lower than those used in the original estimate.

During the quarter ended March 31, 2006, we increased our loss estimate by $738,000 to account for building operating expenses that are not expected to be recovered under the terms of the existing sublease agreements. No such charge was recorded during the six months ended June 30, 2007.

The total accrued loss of $12.7 million at June 30, 2007 is shown net of expected future sublease income of $8.8 million, which was committed under sublease contracts at the time of the estimate. We regularly evaluate the market for office space in the cities where we have operations. If the market for such space declines further in future periods, we may have to revise our estimates further, which may result in additional losses on excess office facilities.

Antitrust Litigation Benefit, Net

On October 11, 2005, we entered into a settlement agreement with Microsoft pursuant to which we agreed to settle all antitrust disputes worldwide with Microsoft, including the U.S. litigation. Antitrust litigation benefit, net consist of settlement income, legal fees, personnel costs, communications, equipment, technology and other professional services costs incurred directly attributable to our antitrust case against Microsoft, as well as our participation in various international antitrust proceedings against Microsoft, including the European Union. No antitrust litigation benefit, net was recorded during the quarter ended June 30, 2007. Antitrust litigation benefit, net of $60.7 million was recorded during the quarter ended March 31, 2007 when we received the final payment under the settlement. Antitrust litigation benefit, net of $57.9 million and $97.7 million was recorded during the quarter and six months ended June 30, 2006, respectively.

Other Income, Net

Other income, net consists primarily of: interest income on our cash, cash equivalents, trading securities, and short-term investments, which are net of interest expense from amortization of offering costs related to our convertible debt and equity in net loss of investments. Other income, net and quarter-over-quarter changes are as follows (dollars in thousands):

	Three Months Ended June 30,			Six Months Ended June 30,		
	2007	Change	2006	2007	Change	2006
Interest and other, net	$ 8,065	(14)%	$ 9,381	$ 17,167	(1)%	$ 17,360
Gain on sale of equity investments	132	(94)	2,286	132	(94)	2,286
Equity in net loss of investments		n/a		(132)	n/a	
Other income, net	485	564	73	952	401	190
Other income, net	$ 8,682	(26)%	$ 11,740	$ 18,119	(9)%	$ 19,836

Other income, net decreased during 2007 due primarily to a decrease in interest income due to a decrease in our average investment balance. The decline in the average investment balance is due to the use of cash for acquisition and stock buy-backs. The decline in 2007 was also due to the decrease in gain on sale of equity investments partially offset by the decrease in equity in net loss of investments.

As of March 31, 2007, the carrying value of equity investments in publicly traded companies consists primarily of approximately 10.6% of the outstanding shares of J-Stream Inc., a Japanese media services company. The market value of these shares has increased from the original cost of $913,000, resulting in a carrying value of $11.6 million and $20.2 million as of June 30, 2007 and December 31, 2006, respectively. These equity investments are accounted for as available-for-sale and the increase over the cost basis, net of income taxes, is reflected as a component of accumulated other comprehensive income. Although the carrying value of our J-Stream investment was $11.6 million at June 30, 2007, there can be no assurance that any gain can be realized through the disposition of these shares because the market for these shares is relatively limited and the share price is volatile.

Income Taxes

During the quarters ended June 30, 2007 and 2006, we recognized income tax expense of $2.2 million and $22.5 million, respectively, related to U.S. and foreign income taxes. During the six months ended June 30, 2007 and 2006, we recognized income tax expense of $25.4 million and $37.3 million, respectively, related to U.S. and foreign income taxes. The decrease in income tax expense is a result of the change in income before income tax primarily related to the decline in settlement income from Microsoft. The increase in tax expense as a percentage of pre-tax income during the three months ended June 30, 2007 was the result of our lower net income combined with non-deductibility of losses in certain foreign jurisdictions.

In June 2006, the FASB issued Financial Interpretation (FIN) No. 48, *Accounting for Uncertainty in Income Taxes an interpretation of FASB Statement No. 109.* FIN No. 48 clarifies the accounting for uncertainty in income taxes recognized in an enterprise s financial statements in accordance with SFAS No. 109, *Accounting for Income Taxes*, and prescribes a recognition threshold and measurement process for financial statement recognition and measurement of tax positions taken or expected to be taken in tax returns. FIN No. 48 also provides guidance on derecognition, classification, interest and penalties, accounting in interim periods, disclosure and transition. On January 1, 2007, date of adoption of FIN No. 48, we had $7.5 million of unrecognized tax benefits, of which $7.2 million would affect the effective tax rate if recognized. Although the implementation of FIN No. 48 did not impact the amount of liability for unrecognized tax benefits, we reclassified $5.3 million of liability for unrecognized tax benefits from current income taxes payable to other long-term liabilities to conform with the balance sheet presentation requirements of FIN No. 48.

In accordance with FIN No. 48, we recognize potential accrued interest and penalties related to unrecognized tax benefits as a component of income tax expense. As of January 1, 2007, we had approximately $300,000 of accrued interest and penalties related to uncertain tax positions, which is included as a component of the $5.3 million of unrecognized tax benefit noted above. To the extent interest and penalties are not assessed with respect to uncertain tax positions, amounts accrued will be reduced and reflected as a reduction of the overall income tax provision. We do not anticipate that total unrecognized tax benefits will significantly change within the next twelve months.

We file numerous consolidated and separate income tax returns in the United States Federal, state, local, and foreign jurisdictions. With few exceptions, we are no longer subject to United States Federal, state, local, or foreign income tax examinations for years before 1993.

During the quarter ended March 31, 2007, WiderThan Americas, Inc. (WTA) became a directly wholly-owned subsidiary of RealNetworks, Inc. WTA was previously a wholly-owned subsidiary of WiderThan Co., Ltd. The restructuring decreased our deferred tax liabilities and goodwill by $1.8 million.

New Accounting Pronouncements

In September 2006, the FASB issued SFAS No. 157, *Fair Value Measurements*, which defines fair value, establishes a framework for measuring fair value in generally accepted accounting principles, and expands disclosures about fair value measurements. SFAS No. 157 does not require any new fair value measurements, but provides guidance on how to measure fair value by providing a fair value hierarchy used to classify the source of the information. SFAS No. 157 is effective for fiscal years beginning after November 15, 2007 and interim periods within those fiscal years. We are currently assessing the impact of SFAS No. 157 on our consolidated financial statements.

In February 2007, the FASB issued SFAS No. 159 *The Fair Value Option for Financial Assets and Financial Liabilities*, which provides companies with an option to report selected financial assets and liabilities at fair value. The objective of SFAS No. 159 is to reduce both the complexity in accounting for financial instruments and the volatility in earnings caused by measuring related assets and liabilities differently. SFAS No. 159 is effective for fiscal years beginning after November 15, 2007. We are currently assessing the impact of SFAS No. 159 on our consolidated financial statements.

Liquidity and Capital Resources

The following summarizes working capital, cash, cash equivalents, trading securities, short-term investments, and restricted cash (in thousands):

	June 30, 2007	December 31, 2006
Working capital	$521,244	$584,125
Cash, cash equivalents, trading securities, and short-term investments	613,763	678,920
Restricted cash	15,500	17,300

Working capital decreased primarily due to the use of $107.9 million for the repurchase of our common stock offset by cash generated from operations. Restricted cash declined by $1.8 million due to a change in the contractual terms of the related letter of credit.

The following summarizes cash flows (in thousands):

	June 30, 2007	June 30, 2006
Cash (used in) provided by operating activities	$(206,296)	$ 59,982
Cash used in investing activities	(3,946)	(27,062)
Cash used in financing activities	(95,032)	(62,450)

Net use of cash in operating activities in 2007 was primarily for the purchase of trading securities of $270.0 million, increase in accounts receivable and deferred costs of $12.7 million, and decrease in accounts payable of $6.6 million offset by net income, including antitrust litigation benefit, net of $60.7 million, and an increase in deferred revenue of $11.9 million and accrued and other liabilities of $3.0 million. Trading securities were purchased to generate capital gains to offset capital loss carryforwards. Operating activities provided cash in 2006 primarily from net income, including antitrust litigation benefit, net of $97.7 million, offset by an increase in accrued and other liabilities of $44.9 million.

In 2007, investing activities used cash primarily for purchases of equipment, software, and leasehold improvements of $11.5 million as well as the additional purchase price for the achievement of performance criteria paid to the selling shareholders of Zylom and the acquisitions of SNS and Exomi of an aggregate of $25.4 million. In 2006, investing activities used cash primarily for purchases of equipment, software, and leasehold improvements of $5.4 million as well as the acquisition of Zylom of $7.1 million. Sales and maturities net of purchases of short-term investments provided cash of $31.6 million during 2007. Purchases net of proceeds from sales and maturities of short-term investments used cash of $16.4 million during 2006.

Financing activities used cash for the repurchase of our common stock of $107.9 million and $97.0 million during 2007 and 2006, respectively. The use of cash was partially offset by cash received from sale of common stock under employee stock purchase plan and exercise of stock options of $12.3 million and $34.5 million during 2007 and 2006, respectively.

In April 2006, the Company s Board of Directors authorized a share repurchase program of up to an aggregate of $100.0 million of the Company s outstanding common stock. During the quarter ended March 31, 2007, we purchased 9.8 million shares at an average cost of $7.99 per share for an aggregate value of $78.5 million. No amounts remained authorized for repurchase under the repurchase program as of March 31, 2007.

In May 2007, our Board of Directors authorized a new share repurchase program for the repurchase of up to an aggregate of $100.0 million of our outstanding common stock. The May 2007 program replaces the April 2006 program. During the quarter ended June 30, 2007, we purchased 3.5 million shares at an average cost of $8.31 per share for an aggregate value of $29.4 million. As of June 30, 2007, $70.6 million remained authorized for repurchase under the May 2007 repurchase program.

We currently have no planned significant capital expenditures for 2007 other than those in the ordinary course of business. In the future, we may seek to raise additional funds through public or private equity financing, or through other sources such as credit facilities. The sale of additional equity securities could result in dilution to our shareholders. In addition, in the future, we may enter into cash or stock acquisition transactions or other strategic transactions that could reduce cash available to fund our operations or result in dilution to shareholders.

Our contractual obligations include convertible debt, office leases, and contractual payments due to content and other service providers. As of June 30, 2007, we have $7.5 million of uncertain tax positions in accordance with FIN No. 48. We believe that our current cash, cash equivalents, and short-term investments will be sufficient to meet our anticipated cash needs for working capital and capital expenditures for at least the next 12 months.

We do not hold derivative financial instruments or equity securities in our short-term investment portfolio. Our cash equivalents and short-term investments consist of high quality securities, as specified in our investment policy guidelines. The policy limits the amount of credit exposure to any one non-U.S. Government or non-U.S. Agency issue or issuer to a maximum of 5% of the total portfolio. These securities are subject to interest rate risk and will decrease in value if interest rates increase. Because we have historically had the ability to hold our fixed income investments until maturity, we do not expect our operating results or cash flows to be significantly affected by a sudden change in market interest rates in our securities portfolio.

We conduct our operations in ten primary functional currencies: the U.S. dollar, the Korean won, the Japanese yen, the British pound, the Euro, the Mexican peso, the Brazilian real, the Australian dollar, the Hong Kong dollar, and the Singapore dollar. Historically, neither fluctuations in foreign exchange rates nor changes in foreign economic conditions have had a significant impact on our financial condition or results of operations. We currently do not hedge the majority of our foreign currency exposures and are therefore subject to the risk of exchange rate fluctuations. We invoice our international customers primarily in U.S. dollars, except in Korea, Japan, Germany, France, the United Kingdom and Australia, where we invoice our customers primarily in won, yen, euros, pounds, and Australian dollars, respectively. We are exposed to foreign exchange rate fluctuations as the financial results of foreign subsidiaries are translated into U.S. dollars in consolidation. Our exposure to foreign exchange rate fluctuations also arises from intercompany payables and receivables to and from our foreign subsidiaries. Foreign exchange rate fluctuations did not have a material impact on our financial results during the six months ended June 30, 2007 and 2006.

Off-Balance Sheet Agreements

Our only significant off-balance sheet arrangements relate to operating lease obligations for office facility leases and other contractual obligations related primarily to minimum contractual payments due to content and other service providers.

Item 3. Quantitative and Qualitative Disclosures About Market Risk

The following discussion about our market risk involves forward-looking statements. Actual results could differ materially from those projected in the forward-looking statements.

Interest Rate Risk. Our exposure to interest rate risk from changes in market interest rates relates primarily to our short-term investment portfolio. We do not hold derivative financial instruments or equity investments in our short-term investment portfolio. Our short-term investments consist of trading and available-for-sale high quality debt securities as specified in our investment policy. Investments in both fixed and floating rate instruments carry a degree of interest rate risk. The fair value of fixed rate securities may be adversely impacted due to a rise in interest rates, while floating rate securities may produce less income than expected if interest rates fall. Additionally, a declining rate environment creates reinvestment risk because as securities mature the proceeds are reinvested at a lower rate, generating less interest income. Due in part to these factors, our future interest income may be adversely impacted due to changes in interest rates. In addition, we may incur losses in principal if we are forced to sell securities that have declined in market value due to changes in interest rates. Because we have historically had the ability to hold our short-term investments until maturity and the substantial majority of our short-term investments mature within one year of purchase, we would not expect our operating results or cash flows to be significantly impacted by a sudden change in market interest rates. There have been no material changes in our investment methodology regarding our cash equivalents and short-term investments since December 31, 2006. Based on our cash, cash equivalents, short-term investments, and restricted cash equivalents at June 30, 2007, a hypothetical 10% increase/decrease in interest rates would increase/decrease our annual interest income and cash flows by approximately $1.7 million during the remainder of 2007.

Investment Risk. As of June 30, 2007, we had investments in voting capital stock of both publicly traded and privately-held technology companies for business and strategic purposes. Our investments in publicly traded companies are accounted for as available-for-sale, carried at current market value and are classified as long-term as they are strategic in nature. We periodically evaluate whether any declines in fair value of our investments are other-than-temporary based on a review of qualitative and quantitative factors. For investments with publicly quoted market prices, these factors include the time period and extent by which its accounting basis exceeds its quoted market price. We consider additional factors to determine whether declines in fair value are other-than-temporary, such as the investee s financial condition, results of operations, and operating trends. The evaluation also considers publicly available information regarding the investee companies. For investments in private companies with no quoted market price, we consider similar qualitative and quantitative factors as well as the implied value from any recent rounds of financing completed by the investee. No impairment charge was recorded during any of the periods presented.

Foreign Currency Risk. We conduct business internationally in several currencies. As such, we are exposed to adverse movements in foreign currency exchange rates.

Our exposure to foreign exchange rate fluctuations arise in part from: (1) translation of the financial results of foreign subsidiaries into U.S. dollars in consolidation; (2) the re-measurement of non-functional currency assets, liabilities and intercompany balances into U.S. dollars for financial reporting purposes; and (3) non-U.S. dollar denominated sales to foreign customers. A portion of these risks is managed through the use of financial derivatives, but fluctuations could impact our results of operations and financial position.

Generally, our practice is to manage foreign currency risk for the majority of material short-term intercompany balances through the use of foreign currency forward contracts. These contracts require us to exchange currencies at rates agreed upon at the contract s inception. Because the impact of movements in currency exchange rates on forward contracts offsets the related impact on the short-term intercompany balances, these financial instruments help alleviate the risk that might otherwise result from certain changes in currency exchange rates. We do not designate our foreign exchange forward contracts related to short-term intercompany accounts as hedges and, accordingly, we adjust these instruments to fair value through results of operations. However, we may periodically hedge a portion of our foreign exchange exposures associated with material firmly committed transactions, long-term investments, highly predictable anticipated exposures and net investments in foreign subsidiaries.

Our foreign currency risk management program reduces, but does not entirely eliminate, the impact of currency exchange rate movements.

Historically, neither fluctuations in foreign exchange rates nor changes in foreign economic conditions have had a significant impact on our financial condition or results of operations. Foreign exchange rate fluctuations did not have a material impact on our financial results during the six months ended June 30, 2007 and 2006.

Item 4. Controls and Procedures

(a) *Evaluation of Disclosure Controls and Procedures.* Based on an evaluation as of the end of the period covered by this report, the Company s principal executive officer and principal financial officer have concluded that the Company s disclosure controls and procedures (as defined in Rules 13a-15(e) and 15d-15(e) under the Securities Exchange Act of 1934, as amended (the Exchange Act)) were effective to ensure that information required to be disclosed by the Company in reports that it files or submits under the Exchange Act (1) is recorded, processed, summarized and reported within the time periods specified in Securities and Exchange Commission rules and forms, and (2) is accumulated and communicated to the Company s management, including its principal executive officer and principal financial officer, as appropriate to allow timely decisions regarding required disclosure.

(b) *Changes in Internal Controls.* There have not been any changes in the Company s internal control over financial reporting (as such term is defined in Rule 13a-15(f) and 15d-15(f) under the Exchange Act) during the fiscal quarter ended June 30, 2007 that have materially affected, or are reasonably likely to materially affect, the Company s internal control over financial reporting.

PART II. OTHER INFORMATION

Item 1. Legal Proceedings

In August 2005, a lawsuit was filed against the Company in the U.S. District Court for the District of Maryland by Ho Keung Tse, an individual residing in Hong Kong. The suit alleges that certain of the Company s products and services infringe the plaintiff s patent relating to the distribution of digital files, including sound tracks, music, video and executable software in a manner which restricts unauthorized use. The plaintiff seeks to enjoin the Company from the allegedly infringing activity and to recover treble damages for the alleged infringement. The Company s co-defendants were granted a motion to transfer the lawsuit from the District of Maryland to the Northern District of California in 2006. The Company disputes the plaintiff s allegations in the action and intends to vigorously defend itself.

In June 2003, a lawsuit was filed against the Company and Listen.com, Inc. (Listen) in federal district court for the Northern District of Illinois by Friskit, Inc. (Friskit), alleging that certain features of the Company s and Listen s products and services willfully infringe certain patents relating to allowing users to search for streaming media files, to create custom playlists, and to listen to the streaming media file sequentially and continuously. Friskit sought to enjoin the Company from the alleged infringing activity and to recover treble damages from the alleged infringement. The court granted the Company s motion for summary judgment on July 26, 2007 and invalidated all claims on grounds of obviousness. Friskit has a 30-day period to appeal the court s ruling.

From time to time the Company is, and expects to continue to be, subject to legal proceedings and claims in the ordinary course of its business, including employment claims, contract-related claims, and claims of alleged infringement of third-party patents, trademarks and other intellectual property rights. These claims, including those described above, even if not meritorious, could force the Company to spend significant financial and managerial resources. The Company is not aware of any legal proceedings or claims that the Company believes will have, individually or taken together, a material adverse effect on the Company s business, prospects, financial condition or results of operations. However, the Company may incur substantial expenses in defending against third-party claims and certain pending claims are moving closer to trial. The Company expects that its potential costs of defending these claims may increase as the disputes move into the trial phase of the proceedings. In the event of a determination adverse to the Company, the Company may incur substantial monetary liability, and/or be required to change its business practices. Either of these could have a material adverse effect on the Company s financial position and results of operations.

Item 1A. Risk Factors

You should carefully consider the risks described below together with all of the other information included in this annual report on Form 10-Q. The risks and uncertainties described below are not the only ones facing our company. If any of the following risks actually occurs, our business, financial condition or operating results could be harmed. In such case, the trading price of our common stock could decline, and investors in our common stock could lose all or part of their investment.

Risks Related to Our Consumer Products and Services Business

Future growth of our online consumer businesses may not keep pace with recently realized growth rates; any slowdown in growth would negatively impact our overall operating results.

Our Consumer Products and Services revenue for subscriptions and services provided have grown substantially in the past two years. A slowdown in the growth of our consumer businesses would have a negative impact on our total revenue and consolidated operating results. Moreover, these consumer businesses compete in new and rapidly evolving markets and face substantial competitive threats. Our prospects for future growth in these businesses must be considered in light of the risks, expenses and difficulties frequently encountered in new and fiercely competitive markets.

We are experiencing greater fluctuations in revenue due to seasonality than at any time in our past, and we expect this trend to continue.

We are increasingly experiencing seasonality in our business, particularly with respect to the fourth quarter of our fiscal year. Our consumer businesses, which include advertising revenue, make up a large percentage of our revenue, and the fourth quarter has traditionally been the seasonally strongest quarter for internet advertising. In addition, as we have begun partnering more closely with device manufacturers for our consumer music services, we expect sales of these devices to follow typical consumer buying patterns with a majority of consumer electronics being sold in the fourth quarter. Finally, WiderThan s historical business has seen a concentration of system sales, deployments, and consulting revenue in the fourth quarter. These factors may result in increasing seasonality in our business and we cannot predict with accuracy how these factors will impact our quarterly financial results.

The success of our subscription services businesses depends upon our ability to increase subscription revenue.

Our operating results could be adversely impacted by the loss of subscription revenue. Internet subscription businesses are a relatively new media delivery model and we cannot predict with accuracy our long-term ability to maintain or increase subscription revenue. Subscribers may cancel their subscriptions to our services for many reasons, including a perception that they do not use the services sufficiently or that the service does not provide enough value, a lack of attractive or exclusive content generally or as compared to competitive service offerings (including Internet piracy), or because customer service issues are not satisfactorily resolved. In recent periods, we have seen an increase in the number of gross customer cancellations of our subscription services due in part to an increasingly large subscriber base. As our subscription business evolves, we have increased our focus on free-to-consumer products and services. In addition, certain subscription based products and services with mobile carriers and broadband service providers are sold on a flat-fee or revenue-share basis. It is not clear what the long-term impact of this evolution will have on our subscription revenue.

Our digital content subscription business, and our online music services in particular, depend on our continuing ability to license compelling content on commercially reasonable terms.

We must continue to obtain compelling digital media content for our video, music, and games services in order to maintain and increase usage, subscription service revenue, and overall customer satisfaction for these products. In some cases, we pay substantial fees to obtain premium content. For instance, we pay substantial royalty fees to music labels to license content. Moreover, our online music service offerings depend on music licenses from the major music labels and publishers, and the failure of any such parties to renew these licenses under terms that are acceptable to us would harm our ability to offer successful music subscription services and therefore our operating results. If we cannot obtain premium digital content for any of our digital content subscription services on commercially reasonable terms, or at all, our business will be harmed.

RealPlayer 11 may not achieve consumer or market acceptance and may be subject to legal challenge.

We recently launched a new version of our media delivery software, RealPlayer 11. Consumers can use RealPlayer 11 to record and download videos from websites on the Internet with a single click on a Download this Video button that appears in the consumer s web browser when a video is playing. Consumers can also simultaneously download and record multiple videos in a number of popular formats and can save the videos to CDs with the free version of RealPlayer 11 and to DVDs with a premium version that can be purchased through our websites. We cannot predict the rate of adoption or level of usage of RealPlayer 11 or whether it will lead to increased sales of any of our consumer products or services.

There are other risks associated with the distribution of RealPlayer 11, including the risk that content owners may claim that the recording and downloading of their content with RealPlayer 11 infringes their intellectual property rights even though RealPlayer 11 automatically recognizes and will not download content protected by digital rights management. It is possible that content owners may allege infringement even though RealPlayer 11 has substantial non-infringing uses. Usage of downloaded content by consumers for other than personal use, including commercial use, may also lead to claims against us for infringement of copyright or other intellectual property rights of third parties. Although we believe RealPlayer 11 is legal, there is no assurance that a court would agree with our position. Responding to these potential claims may require us to enter into royalty and licensing agreements on unfavorable terms, require us to stop distributing or selling, or to redesign, RealPlayer 11, or to pay damages. If we are required to enter into such agreements or take such actions, our operating results may be adversely impacted.

Music publishing royalty rates for music subscription services are not yet fully established; a determination of high royalty rates could negatively impact our operating results.

Publishing royalty rates associated with music subscription services in the U.S. and abroad are not fully established. Public performance licenses are negotiated individually, and we have not yet agreed to rates with all of the performing rights societies for all of our music subscription service activities. We may be required to pay a rate that is higher than we expect, as the issue was recently submitted to a Rate Court by the American Society of Composers, Authors and Publishers (ASCAP) for judicial determination. We have license agreements with the Harry Fox Agency, an agency that represents music publishers, and with many independent music publishers to reproduce musical compositions as required in the creation and delivery of on-demand streams and tethered downloads, but these license agreements do not include final royalty rates. The license agreements anticipate industry-wide agreement on rates, or, if no industry-wide agreement can be reached, determination by a copyright royalty board (CRB), an administrative judicial proceeding supervised by the U.S. Copyright Office. If the rates agreed to or determined by a CRB or by Congress are higher than we expect, the increased expense could negatively impact our operating results. The publishing rates associated with our international music streaming services are also not yet determined and may be higher than our current estimates.

The April 2007 Copyright Royalty Board decision regarding Internet radio royalties and minimum payments could result in material expenses that would harm our operating results and our ability to provide popular radio services.

In April 2007, the Copyright Royalty Board (CRB) issued a decision setting new royalty rates for the use of sound recordings in Internet radio from 2006 through 2010. As part of the new rates, the CRB established a new minimum fee applicable to commercial webcasters, including us. The CRB determined that webcasters must pay a minimum fee of $500 per channel. The decision is not clear regarding how the minimum fee would apply to radio services like ours which enable users to customize the channel or which use an algorithm to help ensure that the channel reflects the relevant genre or artists. Currently, the CRB decision is being appealed to the United States Court of Appeals. Depending upon how the minimum fee provision is interpreted, if the CRB s minimum fee decision is upheld on appeal we could incur additional liability for minimum fees relating to its provision of Internet radio. At this time, the amount of this potential liability is not determinable. Prior to the April 2007 CRB decision, webcasting services were subject to a $2,500 per webcaster yearly minimum fee.

Our consumer businesses face substantial competitive challenges that may prevent us from being successful in those businesses.

Music. Our online music services face significant competition from traditional offline music distribution competitors and from other online digital music services, as well as online theft or piracy. Some of these competing online services have spent substantial amounts on marketing and have received significant media attention, including Apple s iTunes music download service, which it markets closely with its extremely popular iPod line of portable digital audio players and its recently introduced iPhone. Microsoft has also begun offering premium music services in conjunction with its Windows Media Player and also now markets a portable music player and related download software and music service called Zune. We also expect increasing competition from online retailers such as Amazon.com. Our current music service offerings may not be able to compete effectively in this highly competitive market. Our online music services also face significant competition from free peer-to-peer services which allow consumers to directly access a wide variety of free content without securing licenses from content providers. Enforcement efforts have not effectively shut down these services and there can be no assurance that these services will ever be shut down. The ongoing presence of these free services substantially impairs the marketability of legitimate services like ours.

Media Software and Services. Our media software and services (primarily our SuperPass subscription service) face competition from existing competitive alternatives and other free emerging services and technologies, such as user generated content services like YouTube and alternative streaming media playback technologies including Microsoft Windows Media Player and Adobe Flash. Content owners are increasingly marketing their content on their own websites rather than licensing to other distributors such as us. We face competition in these markets from traditional media outlets such as television, radio, CDs, DVDs, videocassettes and others. We also face competition from emerging Internet media sources and established companies entering into the Internet media content market, including Time Warner s AOL subsidiary, Microsoft, Apple, Adobe, Yahoo! and broadband ISPs. We expect this competition to become more intense as the market and business models for Internet video content mature and more competitors enter these new markets. Competing services may be able to obtain better or more favorable access to compelling video content than us, may develop better offerings than us and may be able to leverage other assets to promote their offerings successfully.

Games. Our RealArcade, GameHouse, and Zylom branded services compete with other online distributors of downloadable casual PC games. Some of these distributors have high volume distribution channels and greater financial resources than we do, including Yahoo! Games, MSN Gamezone, Pogo.com, and Shockwave. We expect competition to intensify in this market from these and other competitors and no assurance can be made that we will be able to continue to grow our revenue. Our GameHouse, Zylom, and Mr. Goodliving content development studios compete with other developers and publishers of downloadable PC and mobile games. Our development studios compete primarily with other developers of downloadable and mobile casual PC games and must continue to develop popular and high-quality game titles to maintain our competitive position and help maintain the growth of our games business.

We may not be successful in maintaining and growing our distribution of digital media products.

We cannot predict whether consumers will continue to download and use our digital media products consistent with past usage, especially in light of the fact that Microsoft bundles its competing Windows Media Player with its Windows operating system. Our inability to maintain continued high volume distribution of our digital media products could hold back the growth and development of related revenue streams from these market segments, including the distribution of third-party products, and therefore could harm our business and our prospects.

The success of our music services depend, in part, on interoperability with our customer s music playback hardware.

In order for our digital music services to continue to grow we must design services that interoperate effectively with a variety of hardware products, including portable digital audio players, mobile handsets, home stereos and PCs. We depend on significant cooperation with manufacturers of these products and with software manufacturers that create the operating systems for such hardware devices to achieve our objectives. To date, Apple has not agreed to design its popular iPod line of portable digital audio players or its new iPhone to function with our music services. If we cannot successfully design our service to interoperate with the music playback devices that our customers own, our business will be harmed.

Risks Related to Our Technology Products and Solutions Business

Our recent acquisitions could expose us to new risks, disrupt our business and adversely impact our results of operations.

In November 2006, we announced the final results of our tender offer for WiderThan Co., Ltd. (WiderThan) pursuant to which we acquired 99.7% of the outstanding common shares and American Depository Shares of WiderThan. We acquired the remaining 0.3% of WiderThan during the three months ended June 30, 2007. We also acquired SNS and Exomi in May 2007 and June 2007, respectively. The integration of these acquisitions, particularly WiderThan, is continuing and may divert the attention of management and other key personnel from other core business operations, which could adversely impact our financial performance in the near term. Moreover, the integration of WiderThan s operations into the Company will require expansions to our system of internal controls over financial reporting. Any failure to successfully operate and integrate WiderThan could have an adverse effect on our results of operations.

Our businesses may be adversely affected by developments affecting the South Korean economy amid increased tensions with North Korea.

With the acquisition of WiderThan, we generate a material portion of our revenue from operations in the Republic of Korea (South Korea). On a consolidated basis, during each of the three and six months ended June 30, 2007 we derived 14% of our revenue from our operations in South Korea and expect that we will generate a significant portion of our revenue from South Korea in the remainder of 2007. Operating in this market subjects us to risks that were not previously relevant to us, including risks associated with the general state of the economy in South Korea and the potential instability of the Democratic People s Republic of Korea (North Korea).

Relations between South Korea and North Korea have been tense throughout Korea s modern history. The level of tension between the two Koreas has fluctuated and may increase or change abruptly as a result of current and future events, including ongoing contacts at the highest levels of the governments of South Korea and North Korea. Any further increase in tensions, which may occur, for example, if high-level contacts break down or military hostilities occur, could have a material adverse effect on our business, financial condition, and results of operations.

Our traditional system software business has been negatively impacted by the effects of our competitors and our settlement agreement with Microsoft may not improve sales of our system software products.

We believe that our traditional system software sales have been negatively impacted primarily by the competitive effects of Microsoft, which markets and often bundles its competing technology with its market leading operating systems and server software. In December 2003, we filed suit against Microsoft in U.S. District Court to redress what we believed were illegal, anticompetitive practices by Microsoft. In October 2005, we entered into a settlement agreement with Microsoft regarding these claims and we also entered into two commercial agreements related to our digital music and casual games businesses. Although the settlement agreement contained a substantial cash payment to us and a series of technology agreements between the two companies, Microsoft will continue to be an aggressive competitor with our traditional systems software business. We cannot be sure whether the portions of the settlement agreement designed to limit Microsoft s ability to leverage its market power will be effective and we cannot predict when, or if, we will experience increased demand for our system software products.

A majority of the revenue that we generate in South Korea is dependent upon our relationship with SK Telecom, the largest wireless carrier in Korea; any deterioration of this relationship could materially harm our business.

We offer our mobile entertainment services to consumers in South Korea through SK Telecom, the largest wireless carrier in South Korea. In the near term, we expect that we will continue to generate a material portion of our total revenue through SK Telecom. If SK Telecom fails to market or distribute our applications or terminates its business contracts with us, or if our relationship with SK Telecom deteriorates in any significant way, we may be unable to replace the affected business arrangements with acceptable alternatives, which could have a material negative impact on our revenue and operating results. Also, if we are unable to continue our service development in conjunction with SK Telecom, our ability to develop, test, and introduce new services will be materially harmed.

Contracts with our carrier customers subject us to significant risks that could negatively impact our revenue from application services.

With our acquisitions of WiderThan, SNS, and Exomi, we now derive a material portion of our revenue from carrier application services. Many of our carrier application services contracts provide for revenue sharing arrangements but we have little control over the pricing decisions of our carrier customers. Furthermore, most of these contracts do not provide for guaranteed minimum payments or usage levels. Moreover, since most of our carrier customer contracts are non-exclusive, it is possible that our wireless carriers could purchase similar application services from third parties, and cease to use our services in the future. As a result, our revenue derived under these agreements may be substantially reduced depending on the pricing and usage decisions of our carrier customers.

In addition, none of our carrier application services contracts obligates our carrier customers to market or distribute any of our applications. As a result, revenue related to our application services are, to a large extent, dependent upon the marketing and promotion activities of our carrier customers. The loss of carrier customers or a reduction in marketing or promotion of our applications would likely result in the loss of future revenues from our carrier application services.

Finally, many of our carrier contracts are short term and allow for early termination by the carrier with or without cause. These contracts are therefore subject to renegotiation of pricing or other key terms that could be adverse to our interests, and leave us vulnerable to non-renewal by the carriers. If our carrier contracts are terminated, not renewed, or renegotiated in a manner less favorable to us, our application services revenue would be negatively impacted.

Our carrier customers could begin developing some or all of our carrier applications services on their own, which could result in the loss of future revenues.

Most of our carrier customers do not offer internally-developed application services that compete with ours. If, however our carrier customers begin developing these application services internally, we could be forced to lower our prices or increase the amount of service we provide in order to maintain our business with those carrier customers. This could result in the loss of future revenues from our carrier application services or the reduction of margins related to such revenues.

The mobile entertainment market is highly competitive.

The market for mobile entertainment services, including ringback tone and music-on-demand solutions, is highly competitive. Current and potential future competitors include major media companies, Internet portal companies, content aggregators, wireless software providers and other pure-play wireless entertainment publishers. In connection with music-on-demand in particular, we may in the future compete with companies such as Apple, Microsoft, Napster, and Yahoo! which currently provide music-on-demand services for online or other non-mobile platforms. In addition, the major music labels may demand more aggressive revenue sharing arrangements or seek an alternative business model less favorable to us. Increased competition has in the past resulted in pricing pressure, forcing us to lower the selling price of our services. If we are not as successful as our competitors in our target markets, our sales could decline, our margins could be negatively impacted and we could lose market share, any of which could materially harm our business.

Our Helix open source initiative is subject to risks associated with open source technology.

Although we have invested substantial resources in the development of the underlying technology within our Helix DNA Platform and the Helix Community process, the market and industry may not accept these technologies and, therefore, we may not derive royalty or support revenue from them. Moreover, the introduction of the Helix DNA

Platform open source and community source licensing schemes may adversely affect sales of our commercial system software products to mobile operators, broadband providers, corporations, government agencies, educational institutions and other business and non-business organizations.

Our patents may not improve our business prospects.

Our primary strategy with regard to patents is to use our patent portfolio to increase licensing and usage of our Helix products. We do not know whether our patents will ultimately be deemed enforceable, valid, or infringed. Accordingly, we cannot predict whether our patent strategy will be successful or will improve our financial results. Moreover, we may be forced to litigate to determine the validity and scope of our patents. Any such litigation could be costly and may not achieve the desired results.

Risks Related to Our Business in General

Our operating results are difficult to predict and may fluctuate, which may contribute to fluctuations in our stock price.

As a result of the rapidly changing markets in which we compete, our operating results may fluctuate from period-to-period. In past periods, our operating results have been affected by personnel reductions and related charges, charges relating to losses on excess office facilities, and impairment charges for certain of our equity investments. Our operating results may be adversely affected by similar or other charges or events in future periods, which could cause the trading price of our stock to decline. Certain of our expense decisions (for example, research and development and sales and marketing efforts) are based on predictions regarding business and the markets in which we compete. To the extent that these predictions prove inaccurate, our revenue may not be sufficient to offset these expenditures, and our operating results may be harmed. In addition, we recently acquired the operations of WiderThan. We have limited experience managing these assets which may make it more difficult for us to accurately predict our operating results.

Our settlement agreement with Microsoft may not improve our business prospects.

In October 2005, we entered into a settlement agreement with Microsoft regarding claims of monopolistic activity which we had made against them. In connection with the settlement, we also entered into two commercial agreements with Microsoft related to our digital music and casual games businesses. The settlement agreement consists of a series of substantial cash payments, all of which have been received by us, and a series of technology agreements between the two companies. We cannot be sure that we will be able to apply the proceeds of the settlement in a way that will improve our operating results or otherwise increase the value of our shareholders investments in our stock.

Our products and services must compete with the products and services of strong or dominant competitors.

Our software and services must compete with strong existing competitors and new competitors that may enter with competitive new products, services, and technologies. These market conditions have in the past resulted in, and could likely continue to result in the following consequences, any of which could adversely affect our business, our operating results and the trading price of our stock:

reduced prices, revenue and margins;

increased expenses in responding to competitors;

loss of current and potential customers, market share and market power;

lengthened sales cycles;

degradation of our stature and reputation in the market;

changes in our business and distribution and marketing strategies;

changes to our products, services, technology, licenses and business practices, and other disruption of our operations;

strained relationships with partners; and

pressure to prematurely release products or product enhancements.

Many of our current and potential competitors have longer operating histories, greater name recognition, more employees and significantly greater resources than we do. Our competitors across the breadth of our product lines include a number of large and powerful companies, such as Microsoft, Apple, and Yahoo!.

Failure to develop and introduce new products and services that achieve market acceptance could result in a loss of market opportunities and negatively affect our operating results.

The process of developing new, and enhancing existing, products and services is complex, costly and uncertain. Our business depends on providing products and services that are attractive to subscribers and consumers, which, in part, is subject to unpredictable and volatile factors beyond our control, including end-user preferences and competing products and services. Any failure by us to timely respond to or accurately anticipate consumers changing needs and emerging technological trends could significantly harm our current market share or result in the loss of market opportunities. In addition, we must make long-term investments, develop or obtain appropriate intellectual property and commit significant resources before knowing whether our predictions will accurately reflect consumer demand for our products and services. Therefore, our operating results could be negatively impacted.

Microsoft is one of our strongest competitors, and employs highly aggressive tactics against us.

Microsoft is one of our principal competitors in the development and distribution of digital media and media distribution technology. Microsoft s market power in related markets such as personal computer operating systems, office software suites and web browser software gives it unique advantages in the digital media markets. Despite the settlement of our antitrust litigation with Microsoft, we expect that Microsoft will continue to compete vigorously in the digital media markets in the future. Microsoft s dominant position in certain parts of the computer and software markets, and its aggressive activities have had, and in the future will likely continue to have, adverse effects on our business and operating results.

If our products are not able to support the most popular digital media formats, our business will be substantially impaired.

We may not be able to license technologies, like codecs or digital rights management technology, that obtain widespread consumer and developer use, which would harm consumer and developer acceptance of our products and services. In addition, our codecs and formats may not continue to be in demand or as desirable as other third-party codecs and formats, including codecs and formats created by Microsoft or industry standard formats created by MPEG.

We depend upon our executive officers and key personnel, but may be unable to attract and retain them, which could significantly harm our business and results of operations.

Our success depends on the continued employment of certain executive officers and key employees, particularly Robert Glaser, our founder, Chairman of the Board and Chief Executive Officer. The loss of the services of Mr. Glaser or other key executive officers or employees could harm our business.

Our success is also dependent upon our ability to identify, attract and retain highly skilled management, technical, and sales personnel, both in our domestic operations and as we expand internationally. Qualified individuals are in high demand and competition for such qualified personnel in our industry is intense, and we may incur significant costs to retain or attract them. There can be no assurance that we will be able to attract and retain the key personnel necessary to sustain our business or support future growth.

Our industry is experiencing consolidation that may cause us to lose key relationships and intensify competition.

The Internet and media distribution industries are undergoing substantial change, which has resulted in increasing consolidation and formation of strategic relationships. Acquisitions or other consolidating transactions could harm us in a number of ways, including the loss of customers if competitors or users of competing technologies consolidate with our current or potential customers, or our current competitors become stronger, or new competitors emerge from consolidations. Any of these events could put us at a competitive disadvantage, which could cause us to lose customers, revenue and market share. Consolidation in our industry, or in related industries such as broadband carriers, could force us to expend greater resources to meet new or additional competitive threats, which could also harm our operating results.

Industry consolidation could also cause the loss of strategic relationships if our strategic partners are acquired by or enter into relationships with a competitor. Because we rely on strategic relationships with third parties, including relationships providing for content acquisition and distribution of our products, the loss of current strategic relationships (due to industry consolidation or otherwise), the inability to find other strategic partners, our failure to effectively manage these relationships or the failure of our existing relationships to achieve meaningful positive results could harm our business.

Acquisitions involve costs and risks that could harm our business and impair our ability to realize potential benefits from acquisitions.

As part of our business strategy, we have acquired technologies and businesses in the past, including as recently as June 2007, and expect that we will continue to do so in the future. The failure to adequately manage the costs and address the financial, legal and operational risks raised by acquisitions of technology and businesses could harm our business and prevent us from realizing the benefits of the acquisitions.

Acquisition-related costs and financial risks related to completed and potential future acquisitions may harm our financial position, reported operating results, or stock price. Previous acquisitions have resulted in significant expenses, including amortization of purchased technology and amortization of acquired identifiable intangible assets, which are reflected in our operating expenses. New acquisitions and any potential future impairment of the value of purchased assets could have a significant negative impact on our future operating results.

Acquisitions also involve operational risks that could harm our existing operations or prevent realization of anticipated benefits from an acquisition. These operational risks include:

- difficulties and expenses in assimilating the operations, products, technology, information systems, and/or personnel of the acquired company;
- retaining key management or employees of the acquired company;
- entrance into unfamiliar markets, industry segments, or types of businesses;
- operating and integrating acquired businesses in remote locations;
- integrating and managing businesses based in countries in which we have little or no prior experience;
- diversion of management time and other resources from existing operations to integration activities for acquired businesses;
- impairment of relationships with employees, affiliates, advertisers or content providers of our business or acquired business; and
- assumption of known and unknown liabilities of the acquired company, including intellectual property claims.

Our strategic investments may not be successful and we may have to recognize expenses in our income statement in connection with these investments.

We have made, and in the future we may continue to make, strategic investments in other companies, including joint ventures. These investments often involve immature and unproven businesses and technologies and involve a high degree of risk. We could lose the entire amount of our investment. No assurance can be made that we will realize the anticipated benefits from any of our strategic investments.

We need to develop relationships and technical standards with manufacturers of non-PC media and communication devices to grow our business.

Access to the Internet through devices other than a personal computer (PC), such as personal digital assistants, cellular phones, television set-top devices, game consoles, Internet appliances and portable music and games devices has increased dramatically and is expected to continue to increase. If a substantial number of alternative device manufacturers do not license and incorporate our technology into their devices, we may fail to capitalize on the opportunity to deliver digital media to non-PC devices which could harm our business prospects. If we do not successfully make our products and technologies compatible with emerging standards and the most popular devices used to access digital media, we may miss market opportunities and our business and results will suffer.

Our business and operating results will suffer if our systems or networks fail, become unavailable, unsecured or perform poorly so that current or potential users do not have adequate access to our products, services and websites.

Our ability to provide our products and services to our customers and operate our business depends on the continued operation of our information systems and networks. A significant or repeated reduction in the performance, reliability or availability of our information systems and network infrastructure could harm our ability to conduct our business, and harm our reputation and ability to attract and retain users, customers, advertisers and content providers. We have on occasion experienced system errors and failures that caused interruption in availability of products or content or an increase in response time. Problems with our systems and networks could result from our failure to adequately maintain and enhance these systems and networks, natural disasters and similar events, power failures, HVAC failures, intentional actions to disrupt our systems and networks and many other causes. The vulnerability of a large portion of our computer and communications infrastructure is enhanced because much of it is located at a single leased facility in Seattle, Washington, an area that is at heightened risk of earthquake, flood, and volcanic events. Many of our services do not currently have fully redundant systems or a formal disaster recovery plan, and we may not have adequate business interruption insurance to compensate us for losses that may occur from a system outage.

Our network is subject to security risks that could harm our business and reputation and expose us to litigation or liability.

Online commerce and communications depend on the ability to transmit confidential information and licensed intellectual property securely over private and public networks. Any compromise of our ability to transmit and store such information and data securely, and any costs associated with preventing or eliminating such problems, could damage our business, hurt our ability to distribute products and services and collect revenue, threaten the proprietary or confidential nature of our technology, harm our reputation, and expose us to litigation or liability. We also may be required to expend significant capital or other resources to alleviate problems caused by such breaches or attacks. Any successful attack or breach of our security could hurt consumer demand for our products and services, expose us to consumer class action lawsuits, and harm our business.

The growth of our business is dependent in part on successfully implementing our international expansion strategy.

A key part of our strategy is to develop localized products and services in international markets through subsidiaries, branch offices and joint ventures, if we do not successfully implement this strategy, we may not recoup our international investments and we may fail to develop or maintain worldwide market share. In addition, our recent acquisitions of Exomi, SNS, WiderThan, Zylom, and Mr. Goodliving have increased our revenue from our international operations. Our international operations involve risks inherent in doing business on an international level, including difficulties in managing operations due to distance, language, and cultural differences, different or conflicting laws and regulations, taxes, and exchange rate fluctuations. Any of these factors could harm operating results and financial condition. Our foreign currency exchange risk management program reduces, but does not eliminate, the impact of currency exchange rate movements.

As part of our international expansion strategy, we intend to grow our business in The People s Republic of China (PRC). PRC government regulates our business in PRC through regulations and license requirements restricting (i) the scope of foreign investment in the Internet, retail and delivery sectors, (ii) Internet content and (iii) the sale of certain media products. In order to meet PRC local ownership and regulatory licensing requirements, our business in PRC is operated through a PRC subsidiary which acts in cooperation with PRC companies owned by nominee shareholders who are PRC nationals. Although we believe this structure complies with existing PRC laws, it involves unique risks. There are substantial uncertainties regarding the interpretation of PRC laws and regulations, and it is possible that PRC government will ultimately take a view contrary to ours. If any of our PRC entities were found to be in violation of existing or future PRC laws or regulations or if interpretations of those laws and regulations were to change, the business could be subject to fines and other financial penalties, have its licenses revoked or be forced to shut down entirely.

We may be unable to adequately protect our proprietary rights and may face risks associated with third-party claims relating to our intellectual property.

Our ability to compete partly depends on the superiority, uniqueness and value of our technology, including both internally developed technology, and technology licensed from third parties. To protect our proprietary rights, we rely on a combination of patent, trademark, copyright and trade secret laws, confidentiality agreements with our employees and third parties, and protective contractual provisions. As disputes regarding the ownership of technologies and rights associated with streaming media, digital distribution, and online businesses are common and likely to arise in the future, we may be forced to litigate to enforce or defend our intellectual property rights or to determine the validity and scope of other parties proprietary rights. Any such litigation would likely be costly, distract our management, and the existence and/or outcome of any such litigation could harm our business.

Despite our efforts to protect our proprietary rights, any of the following would likely reduce the value of our intellectual property:

our applications for patents and trademarks relating to our business may not be granted and, if granted, may be challenged or invalidated;

our efforts to protect our intellectual property rights may not be effective in preventing misappropriation of our technology;

our efforts may not prevent the development and design by others of products or technologies similar to, competitive with, or superior to those we develop; or

another party may obtain a blocking patent, thus requiring us to either obtain a license or design around the patent in order to continue to offer the contested feature or service in our products.

From time to time we receive claims and inquiries from third parties alleging that our technology may infringe the third parties proprietary rights, especially patents. Third parties have also asserted and most likely will continue to assert claims against us alleging infringement of copyrights, trademark rights, trade secret rights or other proprietary rights, or alleging unfair competition or violations of privacy rights. Currently we are investigating or litigating a variety of such pending claims, some of which are described in Part II of this report under the heading Legal Proceedings.

We may be subject to market risk and legal liability in connection with the data collection capabilities of our products and services.

Many of our products are interactive Internet applications that by their very nature require communication between a client and server to operate. To provide better consumer experiences and to operate effectively, our products send information to our servers. Many of the services we provide also require that a user provide certain information to us. We have an extensive privacy policy concerning the collection, use and disclosure of user data involved in interactions between our client and server products. Any failure by us to comply with our posted privacy policy and existing or new legislation regarding privacy issues could impact the market for our products and services, subject us to litigation, and harm our business.

We account for employee stock options using the fair value method, which may have a material adverse affect on our results of operations.

On January 1, 2006, we adopted the provisions of, and started accounting for stock-based compensation in accordance with, the Financial Accounting Standards Board s Statement of Financial Accounting Standard (SFAS) No. 123R revised 2004, *Share Based Payment*, which requires a company to recognize, as an expense, the fair value of stock options and other stock-based compensation. We are required to record an expense for our stock-based compensation plans using the fair value method as described in SFAS No. 123R, which results in the recognition of significant and ongoing accounting charges, for which we recorded an expense of $5.6 million and $3.7 million during the three months ended June 30, 2007 and 2006, respectively, and $11.3 million and $7.3 million during the six months ended June 30, 2007 and 2006, respectively, in our condensed consolidated statement of operations. Stock options are also a key part of the compensation packages that we offer our employees. If we are forced to curtail our broad-based option program due to these additional charges, it may become more difficult for us to attract and retain employees.

We may be subject to assessment of sales and other taxes for the sale of our products, license of technology or provision of services.

Currently we do not collect sales or other taxes on the sale of our products, license of technology, or provision of services in states and countries other than those in which we have offices or employees. Our business would be harmed if one or more states or any foreign country were to require us to collect sales or other taxes from past sales or income related to products, licenses of technology, or provision of services.

Effective July 1, 2003, we began collecting Value Added Tax, or VAT, on sales of electronically supplied services provided to European Union residents, including software products, games, data, publications, music, video and fee-based broadcasting services. There can be no assurance that the European Union will not make further modifications to the VAT collection scheme, the effects of which could require significant enhancements to our systems and increase the cost of selling our products and services into the European Union. The collection and remittance of VAT subjects us to additional currency fluctuation risks.

The Internet Tax Freedom Act, or ITFA, which Congress extended until November 2007, among other things, imposed a moratorium on discriminatory taxes on electronic commerce. The imposition by state and local governments of various taxes upon Internet commerce could create administrative burdens for us and could decrease our future sales.

We may be subject to additional income tax assessments.

We are subject to income taxes in the U.S. and numerous foreign jurisdictions. Significant judgment is required in determining our worldwide provision for income taxes, income taxes payable, and net deferred tax assets. In the ordinary course of business, there are many transactions and calculations where the ultimate tax determination is uncertain. Although we believe our tax estimates are reasonable, the final determination of tax audits and any related litigation could be materially different than that which is reflected in our historical financial statements. An audit or litigation can result in significant additional income taxes payable in the U.S. or foreign jurisdictions which could have a material adverse effect on our financial condition and results of operations.

We donate a portion of our net income to charity.

In periods where we achieve profitability, we intend to donate 5% of our annual net income to charitable organizations, which would reduce our net income for those periods.

Risks Related to the Securities Markets and Ownership of Our Common Stock

Our directors and executive officers beneficially own approximately one third of our stock, which gives them significant control over certain major decisions on which our shareholders may vote, may discourage an acquisition of us, and any significant sales of stock by our officers and directors could have a negative effect on our stock price.

Our executive officers, directors and affiliated persons beneficially own more than one third of our common stock. Robert Glaser, our Chief Executive Officer and Chairman of the Board, beneficially owns the majority of that stock. As a result, our executive officers, directors and affiliated persons will have significant influence to:

elect or defeat the election of our directors;

amend or prevent amendment of our articles of incorporation or bylaws;

effect or prevent a merger, sale of assets or other corporate transaction; and

control the outcome of any other matter submitted to the shareholders for vote.

Management s stock ownership may discourage a potential acquirer from making a tender offer or otherwise attempting to obtain control of RealNetworks, which in turn could reduce our stock price or prevent our shareholders from realizing a premium over our stock price.

Provisions of our charter documents, Shareholder Rights Plan, and Washington law could discourage our acquisition by a third-party.

Our articles of incorporation provide for a strategic transaction committee of the board of directors. Without the prior approval of this committee, and subject to certain limited exceptions, the board of directors does not have the authority to:

adopt a plan of merger;

authorize the sale, lease, exchange or mortgage of assets representing more than 50% of the book value of our assets prior to the transaction or on which our long-term business strategy is substantially dependent;

authorize our voluntary dissolution; or

take any action that has the effect of any of the above.

RealNetworks has also entered into an agreement providing Mr. Glaser with certain contractual rights relating to the enforcement of our charter documents and Mr. Glaser s roles and authority within RealNetworks.

We have adopted a shareholder rights plan that provides that shares of our common stock have associated preferred stock purchase rights. The exercise of these rights would make the acquisition of RealNetworks by a third-party more expensive to that party and has the effect of discouraging third parties from acquiring RealNetworks without the approval of our board of directors, which has the power to redeem these rights and prevent their exercise.

Washington law imposes restrictions on some transactions between a corporation and certain significant shareholders. The foregoing provisions of our charter documents, shareholder rights plan, our agreement with Mr. Glaser, our zero coupon convertible subordinated notes and Washington law, as well as our charter provisions that provide for a classified board of directors and the availability of blank check preferred stock, could have the effect of making it more difficult or more expensive for a third-party to acquire, or of discouraging a third-party from attempting to acquire, control of us. These provisions may therefore have the effect of limiting the price that investors might be willing to pay in the future for our common stock.

We are exposed to potential risks from legislation requiring companies to evaluate controls under Section 404 of the Sarbanes-Oxley Act of 2002.

We have evaluated our internal controls in order to allow management to report on, and our registered independent public accounting firm to attest to, our internal controls, as required by Section 404 of the Sarbanes-Oxley Act of 2002. We have performed the system and process evaluation and testing required in an effort to comply with the management certification and auditor attestation requirements of Section 404. The requirements and processes associated with Section 404 are still evolving and we cannot be certain that the measures we have taken will be sufficient to meet the Section 404 requirements as changes occur to the guidance and our reporting environment or that we will be able to implement and maintain adequate controls over financial reporting processes and reporting in the future. Moreover, we cannot be certain that the costs associated with such measures will not exceed our estimates, which could impact our overall level of profitability. Any failure to meet the Section 404 requirements or to implement required new or improved controls, or difficulties or unanticipated costs encountered in their implementation, could cause investors to lose confidence in our reported financial information or could harm our financial results, which could have a negative effect on the trading price of our stock.

Certain material weaknesses in internal controls of WiderThan were identified as of December 31, 2005; if we fail to remediate and maintain an effective system of internal controls at WiderThan we may be unable to accurately report our financial results or reduce our ability to prevent or detect fraud, and investor confidence may be affected.

In connection with the audit of WiderThan s 2005 financial statements, the management of WiderThan identified certain material weaknesses, as defined by the Public Company Accounting Oversight Board s Auditing Standard No. 2, as of December 31, 2005, as follows:

WiderThan did not retain accounting staff with sufficient depth and skill in the application of U.S. GAAP commensurate with the reporting requirements of a U.S. registrant;

WiderThan did not have effective controls over establishing and maintaining accounting policies related to revenue recognition; and

WiderThan did not maintain effective controls, including monitoring, over the financial close and reporting process. Specifically, WiderThan relied heavily on the use of spreadsheet programs during the financial close process and did not have adequately designed controls to ensure the completeness, accuracy, and restricted access to such spreadsheets.

In making its assessment of the effectiveness of internal control over financial reporting as of December 31, 2006 management excluded WiderThan, as permitted by the SEC, because it was acquired on October 31, 2006. We are in the process of integrating the finance operations of WiderThan into our finance department; however, there is no certainty that the identified material weaknesses will be remediated in a timely manner or controls will be implemented to prevent a material misstatement in the consolidated financial statements. Moreover, we cannot be certain that the costs associated with such measures will not exceed our estimates, which could impact our overall level of profitability. Any failure to remediate these material weaknesses could cause investors to lose confidence in our reported financial information or could harm our financial results.

Our stock price has been volatile in the past and may continue to be volatile.

The trading price of our common stock has been highly volatile. For example, during the 52-week period ended June 30, 2007, the price of our common stock ranged from $7.51 to $11.94 per share. Our stock price could be subject to wide fluctuations in response to factors such as actual or anticipated variations in quarterly operating results, changes in financial estimates, recommendations by securities analysts, changes in the competitive environment, as well as any of the other risk factors described above.

Financial forecasting of our operating results will be difficult because of the changing nature of our products and business, and our actual results may differ from forecasts.

As a result of the dynamic markets in which we compete, it is difficult to accurately forecast our operating results and metrics. Our inability or the inability of the financial community to accurately forecast our operating results could result in our reported net income (loss) in a given quarter to differ from expectations, which could cause a decline in the trading price of our common stock.

Item 2. Unregistered Sales of Equity Securities and Use of Proceeds

(a) During the quarter ended June 30, 2007, the Company issued and sold unregistered securities as follows:

(1) On June 29, 2007, the Company issued an aggregate of 2,997 shares of Common Stock to three non-employee directors as compensation for board service during the first quarter of 2007 pursuant to the RealNetworks, Inc. Amended and Restated 2005 Stock Incentive Plan. The aggregate value of the shares was $25,000. The shares were issued in reliance on Section 4(2) under the Securities Act of 1933, as amended, on the basis that the transactions did not involve a public offering.

(b) Not applicable

(c) Purchases of Equity Securities by the Issuer and Affiliated Purchasers

In May 2007, our Board of Directors authorized a new share repurchase program for the repurchase of up to an aggregate of $100.0 million of our outstanding common stock. Below is a summary of share repurchases during the quarter ended June 30, 2007.

All of the repurchases in the table below were made through the Board of Directors authorized share repurchase program. No purchases were made in April 2007.

For further information regarding our share repurchase plan see Note 12 of Notes to Unaudited Condensed Consolidated Financial Statements.

Period		Total Number of Shares Repurchased (in thousands)	Average Price Paid Per Share
5/1/2007	5/31/2007	1,448	$ 8.43
6/1/2007	6/30/2007	2,092	8.23
Total		3,540	$ 8.31

Item 3. Default Upon Senior Securities

None

Item 4. Submission of Matters to a Vote of Security Holders

An Annual Meeting of Shareholders (Annual Meeting) of the Company was held on June 25, 2007. The matters voted on at the Annual Meeting and votes cast on such matters were as follows:

The election of three Class 1 directors to serve until the 2010 Annual Meeting of Shareholders, or until such directors earlier retirement, resignation or removal, or the election of their successors.

Directors Elected	For	Withheld
Eric A. Benhamou	140,891,103	1,378,770
Edward Bleier	141,071,644	1,198,229
Kalpana Raina	141,080,707	1,189,166

The terms of the following directors continued after the Annual Meeting:

Jonathan D. Klein
James W. Breyer
Robert Glaser
Jeremy Jaech

The approval of amendments to the Company s 2005 Stock Incentive Plan, including the authorization of the issuance of a total of 15,000,000 shares of the Company s Common Stock.

	Votes
For	71,766,499
Against	46,682,724
Broker non-votes	23,508,109
Abstain	312,541

The approval of the Company s 2007 Employee Stock Purchase Plan.

	Votes
For	112,761,377
Against	5,704,017
Broker non-votes	23,508,109
Abstain	296,370

The ratification of the appointment of KPMG LLP as the Company s registered public accounting firm for the fiscal year ending December 31, 2007.

	Votes
For	139,587,956
Against	2,311,344
Broker non-votes	
Abstain	370,573

Item 5. Other Information

None

Item 6. Exhibits

Exhibits Required by Item 601 of Regulation S-K

Exhibit Number	Description
3.1	Amended and Restated Bylaws of RealNetworks, Inc. adopted April 24, 2007 (incorporated by reference from Exhibit 3.1 to RealNetworks Current Report on Form 8-K filed with the Securities and Exchange Commission on April 27, 2007)
10.1	RealNetworks, Inc. 2005 Stock Incentive Plan, as amended and restated on June 25, 2007 (incorporated by reference from Exhibit 10.1 to RealNetworks Current Report on Form 8-K filed with the Securities and Exchange Commission on June 29, 2007)
10.2	RealNetworks, Inc. 2007 Employee Stock Purchase Plan
31.1	Certification of Robert Glaser, Chairman and Chief Executive Officer of RealNetworks, Inc., 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
31.2	Certification of Michael Eggers, Senior Vice President, Chief Financial Officer and Treasurer of RealNetworks, Inc., 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
32.1	Certification of Robert Glaser, Chairman and Chief Executive Officer of RealNetworks, Inc., Pursuant to 18 U.S.C. Section 1350, as Adopted Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002
32.2	Certification of Michael Eggers, Senior Vice President, Chief Financial Officer and Treasurer of RealNetworks, Inc., Pursuant to 18 U.S.C. Section 1350, as Adopted Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002

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SIGNATURE

Pursuant to the requirements of the Securities Exchange Act of 1934, the Registrant has duly caused this Report to be signed on its behalf by the undersigned, thereunto duly authorized, on August 8, 2007.

REALNETWORKS, INC.

By: /s/ Michael Eggers

Michael Eggers
Title: Senior Vice President, Chief Financial Officer and Treasurer
(Principal Financial and Accounting Officer)

INDEX TO EXHIBITS

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