REALNETWORKS INC
Form 10-Q
August 11, 2008

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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, 2008

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, a non-accelerated filer, or a smaller reporting company. See definitions of large accelerated filer, accelerated filer and smaller reporting company in Rule 12b-2 of the Exchange Act. (Check one):

Large accelerated filer þ	Accelerated filer o	Non-accelerated filer o (Do not check if a smaller reporting company)	Smaller reporting company 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, 2008 was 142,629,479.

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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, 2008	December 31, 2007
ASSETS		
Current assets:		
Cash and cash equivalents	$ 415,805	$ 476,697
Short-term investments	106,862	79,932
Trade accounts receivable, net of allowances for doubtful accounts and sales returns	71,177	84,674
Deferred costs, current portion	8,598	6,408
Prepaid expenses and other current assets	39,168	33,845
Total current assets	641,610	681,556
Equipment, software, and leasehold improvements, at cost:		
Equipment and software	124,406	109,621
Leasehold improvements	30,875	30,632
Total equipment, software, and leasehold improvements, at cost	155,281	140,253
Less accumulated depreciation and amortization	94,763	83,756
Net equipment, software, and leasehold improvements	60,518	56,497
Restricted cash equivalents and investments	14,670	15,509
Equity investments	8,126	9,976
Other assets	16,419	10,161
Deferred tax assets, net	40,169	40,913
Other intangible assets, net	90,506	107,677
Goodwill	341,551	353,153
Total assets	$ 1,213,569	$ 1,275,442
LIABILITIES AND SHAREHOLDERS EQUITY		
Current liabilities:		
Accounts payable	$ 29,748	$ 56,160
Accrued and other liabilities	106,654	114,136
Deferred revenue, current portion	40,680	39,564
Related party payable	9,992	17,241
Convertible debt	100,000	100,000
Accrued loss on excess office facilities, current portion	4,311	3,389
Total current liabilities	291,385	330,490
Deferred revenue, non-current portion	1,608	2,663

Accrued loss on excess office facilities, non-current portion	4,797	7,311
Deferred rent	4,675	4,518
Deferred tax liabilities, net, non-current portion	18,311	22,060
Other long-term liabilities	10,152	13,683
Total liabilities	330,928	380,725
Minority interest in Rhapsody America ($68.2 million redemption value at June 30, 2008)	10,931	19,613
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 143,269 shares in 2008 and 142,298 shares in 2007	143	142
Additional paid-in capital	670,008	653,904
Accumulated other comprehensive (loss) income	(2,888)	17,732
Retained earnings	204,447	203,326
Total shareholders equity	871,710	875,104
Total liabilities and shareholders equity	$ 1,213,569	$ 1,275,442

See accompanying notes to unaudited condensed consolidated financial statements.

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

	Quarter Ended June 30,		Six Months Ended June 30,	
	2008	2007	2008	2007
Net revenue (A)	$ 152,648	$ 136,171	$ 300,211	$ 265,643
Cost of revenue (B)	55,645	49,199	111,038	95,142
Gross profit	97,003	86,972	189,173	170,501
Operating expenses:				
Research and development	29,065	25,005	54,071	48,484
Sales and marketing	53,054	50,081	106,650	99,781
Advertising with related party	9,240		16,580	
General and administrative	18,337	17,063	35,421	34,417
Restructuring costs			686	
Subtotal operating expenses	109,696	92,149	213,408	182,682
Antitrust litigation benefit, net				(60,747)
Total operating expenses, net	109,696	92,149	213,408	121,935
Operating (loss) income	(12,693)	(5,177)	(24,235)	48,566
Other income (expenses):				
Interest income, net	3,375	8,065	8,333	17,167
Equity in net loss of investments	(107)		(198)	(132)
Gain on sale of equity investments, net	222	132	222	132
Minority interest in Rhapsody America	8,177		16,792	
Gain on sale of interest in Rhapsody America	3,371		7,097	
Other income, net	50	485	818	952
Other income, net	15,088	8,682	33,064	18,119
Income before income taxes	2,395	3,505	8,829	66,685
Income taxes	(3,700)	(2,178)	(7,708)	(25,397)
Net (loss) income	$ (1,305)	$ 1,327	$ 1,121	$ 41,288
Basic net (loss) income per share	$ (0.01)	$ 0.01	$ 0.01	$ 0.26
Diluted net income per share	$ (0.01)	$ 0.01	$ 0.01	$ 0.24
Shares used to compute basic net income per share	142,905	153,880	142,946	157,929
Shares used to compute diluted net income per share	142,905	169,033	156,000	173,822

Comprehensive (loss) income:				
Net (loss) income	$ (1,305)	$ 1,327	$ 1,121	$ 41,288
Unrealized holding gains (losses) on short-term and equity investments, net of income taxes	145	(2,663)	(289)	(5,719)
Foreign currency translation losses	(12,269)	1,268	(20,331)	(1,659)
Comprehensive (loss) income	$ (13,429)	$ (68)	$ (19,499)	$ 33,910

(A) Components of net revenue:				
License fees	$ 28,613	$ 22,212	$ 54,368	$ 44,049
Service revenue	124,035	113,959	245,843	221,594
	$ 152,648	$ 136,171	$ 300,211	$ 265,643

(B) Components of cost of revenue:				
License fees	$ 10,614	$ 7,882	$ 20,002	$ 16,174
Service revenue	45,031	41,317	91,036	78,968
	$ 55,645	$ 49,199	$ 111,038	$ 95,142

See accompanying notes to unaudited condensed consolidated financial statements.

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

	Six Months Ended June 30, 2008	Six Months Ended June 30, 2007
Cash flows from operating activities:		
Net income	$ 1,121	$ 41,288
Adjustments to reconcile net income to net cash (used in) provided by operating activities:		
Depreciation and amortization	25,701	20,905
Stock-based compensation	11,520	11,307
Loss on disposal of equipment, software, and leasehold improvements	182	163
Equity in net loss of investments	198	132
Gain on sale of equity investments, net	(222)	(132)
Excess tax benefit from stock option exercises	(88)	(596)
Accrued loss on excess office facilities	(1,592)	(1,795)
Unrealized gain on trading securities		(2,102)
Purchase of trading securities		(270,000)
Deferred income taxes	(2,138)	(6,069)
Minority interest	(16,792)	
Gain on sale of interest in Rhapsody America	(7,097)	
Other	89	51
Net change in certain operating assets and liabilities	(39,160)	552
Net cash used in operating activities	(28,278)	(206,296)
Cash flows from investing activities:		
Purchases of equipment, software, and leasehold improvements	(15,231)	(11,525)
Purchases of short-term investments	(95,671)	(38,768)
Proceeds from sales and maturities of short-term investments	68,741	70,343
Purchases of other intangibles assets		(2,060)
Decrease in restricted cash equivalents and investments, net	839	1,800
Payment of acquisition costs, net of cash acquired	(10,164)	(25,351)
Proceeds from sales of equity investments	1,225	1,615
Net cash used in investing activities	(50,261)	(3,946)
Cash flows from financing activities:		
Net proceeds from sale of common stock under employee stock purchase plan and exercise of stock options	6,041	12,277
Excess tax benefit from stock option exercises	88	596
Net proceeds from sales of interest in Rhapsody America	14,607	
Repurchase of common stock	(681)	(107,905)

Net cash (used in) provided by financing activities	20,055	(95,032)
Effect of exchange rate changes on cash and cash equivalents	(2,408)	(410)
Net decrease in cash and cash equivalents	(60,892)	(305,684)
Cash and cash equivalents, beginning of period	476,697	525,232
Cash and cash equivalents, end of period	$ 415,805	$ 219,548
Supplemental disclosure of cash flow information:		
Cash paid for income taxes	$ 8,341	$ 13,160
Supplemental disclosure of non-cash investing and financing activities:		
Accrued acquisition costs	$	$ 368

See accompanying notes to unaudited condensed consolidated financial statements.

REALNETWORKS, INC. AND SUBSIDIARIES
NOTES TO UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS
Quarters and Six Months Ended June 30, 2008 and 2007

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.

On August 20, 2007, RealNetworks and MTV Networks, a division of Viacom International Inc. (MTVN), created Rhapsody America LLC (Rhapsody America) to jointly own and operate a business-to-consumer digital audio music service. RealNetworks held a 51% interest in Rhapsody America as of June 30, 2008. Rhapsody America s financial position and operating results have been consolidated into RealNetworks financial statements since its formation in August 2007. The minority interest s proportionate share of income (loss) is included in Minority interest in Rhapsody America in the unaudited condensed consolidated statements of operations and comprehensive income (loss). MTVN s proportionate share of equity is included in Minority interest in Rhapsody America in the unaudited condensed consolidated balance sheets.

The Company acquired 99.7% of WiderThan Co., Ltd. (WiderThan) during the quarter ended December 31, 2006. The Company acquired substantially all of the remaining shares of WiderThan during the quarter 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 quarter and six months ended June 30, 2007 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 quarter and six months ended June 30, 2008 are not necessarily indicative of the results that may be expected for any subsequent quarter or for the year ending December 31, 2008. 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, 2007.

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.

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 are imposed on and concurrent with revenue-producing transactions. Such taxes are recorded on a net basis and are not included in net revenue of the Company.

Accounting for Gains on Sale of Subsidiary Stock. The effects of any changes in the Company s ownership interest resulting from the issuance of equity capital by consolidated subsidiaries are accounted for as either a gain or loss in the statement of operations pursuant to SAB No. 51, Accounting for the Sales of Stock of a Subsidiary. SAB No. 51 requires that the difference between the carrying amount of the parent s investment in a subsidiary and the underlying net book value of the subsidiary after the issuance of stock by the subsidiary be reflected as either a gain or loss in the statement of operations if the appropriate recognition criteria has been met or reflected as an equity transaction. RealNetworks has elected to reflect SAB No. 51 gains or losses in its unaudited condensed statement of operations.

Note 2. Recent Accounting Pronouncements

In December 2007, the FASB issued SFAS No. 141R, *Business Combinations* (SFAS 141R), which establishes principles and requirements for how an acquirer recognizes and measures in its financial statements the identifiable assets acquired, the liabilities assumed, and any noncontrolling interest in an acquiree, including the recognition and measurement of goodwill acquired in a business combination. The requirements of SFAS 141R are effective for the Company for periods beginning after December 15, 2008. Early adoption is prohibited. The Company is in the process of evaluating this guidance and therefore has not yet determined the impact that SFAS 141R will have on the Company s financial position or results of operations upon adoption.

In December 2007, the FASB issued SFAS No. 160, *Noncontrolling Interest in Consolidated Financial Statements*, an amendment of ARB No. 51 (SFAS 160), which will change the accounting and reporting for minority interests and which will be recharacterized as noncontrolling interests and classified as a component of equity within the consolidated balance sheets. SFAS 160 requires that changes in a parent s ownership interest while the parent retains its controlling financial interest shall be accounted for as equity transactions. As a result, beginning in 2009, the gain on sales of interest in Rhapsody America will no longer be recorded in the statement of operations, but will be reflected as a component of shareholders equity. The requirements of SFAS 160 are effective for the Company for periods beginning after December 15, 2008. Early adoption is prohibited. The Company is in the process of evaluating all the impacts of this guidance and therefore has not yet determined the full impact that SFAS 160 will have on the Company s financial position or results of operations upon adoption.

In March 2008, the FASB affirmed the consensus of FSP APB 14-1, *Accounting for Convertible Debt Instruments That May Be Settled in Cash upon Conversion (Including Partial Cash Settlement)* (FSP APB 14-1). which applies to all convertible debt instruments that have a net settlement feature , which means instruments that by their terms may be settled either wholly or partially in cash upon conversion. FSP APB 14-1 requires issuer s of convertible debt instruments that may be settled wholly or partially in

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cash upon conversion to separately account for the liability and equity components in a manner reflective of the issuer s nonconvertible debt borrowing rate. Previous guidance provided for accounting for this type of convertible debt instrument entirely as debt. The FSP requires retrospective application to all periods presented and does not grandfather existing debt instruments. FSP APB 14-1 is effective for financial statements issued for fiscal years beginning after December 15, 2008 and interim periods within those fiscal years. The Company is currently evaluating the impact FSP APB 14-1 may have on the Company s financial position or results of operations upon adoption.

In April 2008, the FASB issued FSP No. 142-3, *Determination of the Useful Life of Intangible Assets* (FSP 142-3). FSP 142-3 amends the factors that should be considered in developing renewal or extension assumptions used to determine the useful life of a recognized intangible asset under FASB Statement No. 142, *Goodwill and Other Intangible Assets*. FSP 142-3 is effective for financial statements issued for fiscal years beginning after December 15, 2008. Early adoption is prohibited. The Company is currently evaluating the impact FSP No. 142-3 may have on the Company s financial position or results of operations upon adoption.

In May 2008, the FASB issued SFAS No. 162, *The Hierarchy of Generally Accepted Accounting Principles*, (SFAS 162). This Statement identifies the sources of accounting principles and the framework for selecting the principles to be used in the preparation of financial statements of nongovernmental entities that are presented in conformity with U.S. GAAP (the GAAP hierarchy). While the effective date of this pronouncement has not yet been determined, the Company is currently assessing the impact SFAS 162 may have on the Company s financial position or results of operations upon adoption.

Note 3. Stock-Based Compensation

The Company accounts for stock-based compensation in accordance with SFAS No. 123R revised 2004, *Share-Based Payment* (SFAS 123R). 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 123R. The Company recognizes compensation cost related to stock options granted prior to the adoption of SFAS 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 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:

	Quarters Ended June 30,		Six Months Ended June 30,	
	2008	**2007**	**2008**	**2007**
Expected dividend yield	0%	0%	0%	0%
Risk-free interest rate	2.96%	4.73%	2.61%	4.72%
Expected life (years)	4.2	4.1	4.2	4.1
Volatility	45%	42%	45%	42%

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

	Quarters Ended June 30,	Six Months Ended June 30,

	2008	**2007**	**2008**	**2007**
Cost of service revenue	$ 662	$ 154	$ 896	$ 313
Research and development	2,146	1,641	4,059	3,413
Sales and marketing	1,433	2,203	3,341	4,590
General and administrative	1,790	1,624	3,224	2,991
Total stock-based compensation expense	$ 6,031	$ 5,622	$ 11,520	$ 11,307

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No stock-based compensation was capitalized as part of the cost of an asset during the three and six month periods ended June 30, 2008 or 2007. As of June 30, 2008, $44.9 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. Rhapsody America

Formation

On August 20, 2007, RealNetworks and MTVN created Rhapsody America to jointly own and operate a business-to-consumer digital audio music service. Under the Rhapsody America venture agreements:

RealNetworks contributed its Rhapsody service subscribers, RadioPass subscribers, cash of $16.4 million, contracts, revenue from existing Rhapsody subscribers, marketing materials, player hardware, rhapsody.com and related URLs, certain liabilities, and distribution arrangements in exchange for a 51% equity interest in Rhapsody America. RealNetworks also licensed certain assets to Rhapsody America, including Rhapsody content, Rhapsody technology, the Rhapsody brands and related materials.

MTVN contributed its URGE service subscribers, cash, contracts, marketing materials, and revenue from existing URGE subscribers, certain liabilities, plus the note payable described below, in exchange for a 49% equity interest in Rhapsody America. MTVN has also licensed certain assets to Rhapsody America, including URGE content, brands and related materials.

In addition to the assets described above, MTVN also contributed a $230 million five-year note payable in consideration for acquiring MTVN s interest in the venture. Rhapsody America must use the proceeds from the note solely to purchase advertising from MTVN. As MTVN makes payments on the note, Rhapsody America records equity and RealNetworks realizes an immediate appreciation in the carrying value of the Company s interests in the venture and recognizes a gain if the gain is reasonably assured in accordance with SAB 51. MTVN made payments of $7.2 million and $14.4 million during the quarter and six months ended June 30, 2008, respectively. As a result, RealNetworks realized and recorded gains of $3.7 million and $7.3 million during the quarter and six months ended June 30, 2008, respectively, as all of the SAB 51 gain criteria were met. As of June 30, 2008, $39.4 million in payments were made on the note since the formation of Rhapsody America.

The assets and liabilities contributed by RealNetworks to Rhapsody America have been recorded at their historical cost basis as RealNetworks maintained a controlling interest in the assets and liabilities. The assets and liabilities contributed by MTVN to Rhapsody America have been recorded at their estimated fair values in the unaudited condensed consolidated balance sheets as of June 30, 2008 and December 31, 2007. MTVN s contribution included identifiable intangible assets with estimated fair values as of the date of formation of $7.6 million. The respective estimated fair values were determined by management as of the date of the acquisition. RealNetworks realized an immediate appreciation in the carrying value of its interests in Rhapsody America and recognized a gain on sale of music interests upon formation of $3.9 million under SAB 51 as all of the gain criteria were met.

A summary of the intangible assets contributed by MTVN is as follows (in thousands):

Trade Name and Trademarks	$ 4,000
Existing Technology	1,900
Existing Subscribers	1,680
Total Identifiable Intangible Assets	$ 7,580

The identified intangible assets have a weighted average estimated useful life of 4.1 years. All of the intangible assets are being amortized over their estimated useful lives on a straight line basis.

As agreed to during the initial formation of Rhapsody America, RealNetworks and MTVN provided additional funding in the quarter ended December 31, 2007, for future operations of $17.4 and $16.7 million, respectively.

Call/Put Rights

Pursuant to the terms of the Rhapsody America limited liability company agreement, RealNetworks has the right to purchase from MTVN, and MTVN has a right to require RealNetworks to purchase, MTVN s interest in Rhapsody America. The Company has

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evaluated the terms of the call and put rights under applicable accounting literature, including SFAS No. 133, Accounting for Derivatives and Hedging Activities, and SFAS No. 150, Accounting for Certain Financial Instruments with Characteristics of Both Liabilities and Equity, and concluded that neither of these rights represent freestanding financial instruments or derivatives that should be accounted for separately.

These call and put rights are exercisable upon the occurrence of certain events any time after January 1, 2011 and during certain periods in each of 2012, 2013 and 2014 and every two years thereafter and are not exercisable any time prior to January 1, 2011. If MTVN exercises its put right, RealNetworks has the right to pay a portion of the purchase price for MTVN s interest in cash and shares of RealNetworks capital stock, subject to certain maximum amounts with the balance (if any) paid with a note. If RealNetworks exercises its call right, MTVN has the right to demand payment of part of the purchase price for its membership interest in shares of RealNetworks capital stock. If a portion of the purchase price for MTVN s interest is payable in shares of RealNetworks capital stock, such shares could consist of our common stock representing up to 15% of the outstanding shares of RealNetworks common stock immediately prior to the transaction, and shares of our non-voting stock representing up to an additional 4.9% of the outstanding shares of RealNetworks common stock immediately prior to the transaction representing a maximum of 19.9% of RealNetworks capital stock. If RealNetworks pays a portion of the purchase price for MTVN s membership interest in shares of RealNetworks common stock and non-voting stock, RealNetworks other shareholders voting and economic interests in RealNetworks could be diluted and MTVN will become one of RealNetworks significant shareholders.

The redemption prices of MTVN s interest in Rhapsody America under both the call and put rights are calculated based on the provisions within the limited liability agreement and are impacted by the total appraised value of Rhapsody America and assume repayment of the $230 million five-year note payable from MTVN. Once the call right becomes exercisable, the redemption price of MTVN s interest in Rhapsody America under the call right will be equal to the greater of $230 million or the appraised value of MTVN s interest in Rhapsody America at the redemption date. Once the put right becomes exercisable, the redemption price of MTVN s interest in Rhapsody America under the put right will be equal to, upon the occurrence of certain events, the appraised value of MTVN s interest in Rhapsody America at the redemption date or will be based on a formula that is intended to approximate the appraised value at the redemption date. The hypothetical current redemption price of MTVN s interest in Rhapsody America under the put right at June 30, 2008 is $68.2 million. The current redemption price has been adjusted under the formula in the limited liability agreement for the remaining outstanding amounts due of $190.6 million on the note payable as of June 30, 2008.

Note 5. Fair Value Measurements

Effective January 1, 2008, the Company implemented SFAS No. 157, *Fair Value Measurement* (SFAS 157), for its financial assets and liabilities that are re-measured and reported at fair value at each reporting period, and non-financial assets and liabilities that are re-measured and reported at fair value at least annually. In accordance with the provisions of FSP No. FAS 157-2, *Effective Date of FASB Statement No. 157*, the Company elected to defer implementation of SFAS 157 as it relates to its non-financial assets and non-financial liabilities that are recognized and disclosed at fair value in the financial statements on a nonrecurring basis until January 1, 2009. The Company is evaluating the impact, if any, this Standard will have on its non-financial assets and liabilities that are recognized or disclosed at fair value on a nonrecurring basis.

The adoption of SFAS 157 with respect to financial assets and liabilities and non-financial assets and liabilities that are re-measured and reported at fair value at least annually did not have an impact on the financial results of the Company in the first quarter of 2008. The Company will continue to evaluate the impact, if any, that the implementation of this standard will have on its financial statements as it relates to its non-financial assets and liabilities.

SFAS No. 157 establishes a hierarchy that prioritizes fair value measurements based on the types of inputs used for the various valuation techniques (market approach, income approach and cost approach). The levels of the hierarchy are described below:

Level 1: Observable inputs such as quoted prices in active markets for identical assets or liabilities

Level 2: Inputs other than quoted prices that are observable for the asset or liability, either directly or indirectly; these include quoted prices for similar assets or liabilities in active markets and quoted prices for identical or similar assets or liabilities in markets that are not active

Level 3: Unobservable inputs that reflect the reporting entity s own assumptions

The following table presents information about the Company s financial assets that have been measured at fair value as of June 30, 2008 and indicates the fair value hierarchy of the valuation inputs utilized to determine such fair value.

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		Fair Value Measurements as of June 30, 2008		
(in thousands)	Total	Level 1	Level 2	Level 3
Cash equivalents				
Money market funds	$ 308,937	$ 308,937	$	$
Corporate notes and bonds	29,981	29,981		
Short-term investments				
Corporate notes and bonds	43,174	43,174		
U.S. government agency securities	63,688	63,688		
Equity investments				
Publicly traded investments	7,003	7,003		
Total	$ 452,783	$ 452,783	$	$

Investments in marketable securities classified as short-term investments and equity investments of public companies are measured at fair value using quoted market prices and are classified within Level 1 of the valuation hierarchy. The Company carries its equity investments in private companies at cost and are excluded from the provisions of SFAS 157. The Company has consistently applied these valuation techniques in all periods presented.

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Note 6. Cash, Cash Equivalents, Trading Securities, Short-Term Investments, and Restricted Cash Equivalents and Investments

Cash, cash equivalents, trading securities, short-term investments, and restricted cash equivalents and investments as of June 30, 2008 consist of the following (in thousands):

	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Estimated Fair Value
Cash and cash equivalents:				
Cash	$ 76,887	$	$	$ 76,887
Money market mutual funds	308,937			308,937
Corporate notes and bonds	29,981			29,981
Total cash and cash equivalents:	415,805			415,805
Short-term investments:				
Corporate notes and bonds	43,554	19	(399)	43,174
U.S. Government agency securities	63,622	93	(27)	63,688
Total short-term investments:	107,176	112	(426)	106,862
Total cash, cash equivalents and short-term investments	$ 522,981	$ 112	$ (426)	$ 522,667
Restricted cash equivalents and investments	$ 14,670	$	$	$ 14,670

Cash, cash equivalents, short-term investments, and restricted cash equivalents as of December 31, 2007 consist of the following (in thousands):

	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Estimated Fair Value
Cash and cash equivalents:				
Cash	$ 105,615	$	$	$ 105,615
Money market mutual funds	198,148			198,148
Corporate notes and bonds	172,934			172,934
Total cash and cash equivalents	476,697			476,697
Short-term investments:				
Corporate notes and bonds	43,552		(981)	42,571

U.S. Government agency securities	37,296	65		37,361
Total short-term investments	80,848	65	(981)	79,932
Total cash, cash equivalents, and short-term investments	$ 557,545	$ 65	$ (981)	$ 556,629
Restricted cash equivalents and investments	$ 15,509	$	$	$ 15,509

At June 30, 2008 and December 31, 2007, restricted cash equivalents and investments represent cash equivalents and short-term investments pledged as collateral against two letters of credit for a total of $14.7 million and $15.5 million, respectively, in connection with two lease agreements.

Realized gains or losses on sales of available-for-sale securities for the quarters ended June 30, 2008 and 2007 were not significant.

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, 2008 are as follows (in thousands):

	Amortized Cost	Estimated Fair Value
Within one year	$ 31,327	$ 30,976
Between one year and five years	75,849	75,886
Total available-for-sale investments	$ 107,176	$ 106,862

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Note 7. 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	Allowance For Sales Returns
Balances, December 31, 2007	$ 1,117	$ 1,338
Additions charged to expenses/revenue	372	1,934
Amounts written off	(218)	(2,119)
Balances, June 30, 2008	$ 1,271	$ 1,153

As of June 30, 2008, no one customer accounted for more than 10% of trade accounts receivable or for more than 10% of total revenue during the quarter or six months ended June 30, 2008. As of December 31, 2007, one international customer accounted for 19% of trade accounts receivable. The same international customer accounted for 12% of total revenue during the quarter and six months ended June 30, 2007.

Note 8. Equity Investments

As of June 30, 2008 and December 31, 2007, the carrying value of equity investments in publicly traded companies primarily relates to J-Stream Inc. (J-Stream), a Japanese media services company, of which the Company owns approximately 10.6% of the outstanding shares. 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, 2008		December 31, 2007	
	Cost	Carrying Value	Cost	Carrying Value
Publicly traded investments	$ 933	$ 7,003	$ 933	$ 8,085
Privately held investments	2,458	1,123	2,740	1,891
Total equity investments	$ 3,391	$ 8,126	$ 3,673	$ 9,976

Note 9. Other Intangible Assets

Other intangible assets at June 30, 2008 consist of the following (in thousands):

	Gross Amount	Accumulated Amortization	Net
Customer relationships	$ 75,804	$ 20,724	$ 55,080
Developed technology	47,907	22,756	25,151
Patents, trademarks and tradenames	13,741	6,536	7,205
Service contracts and other	6,469	3,399	3,070
Total other intangible assets	$ 143,921	$ 53,415	$ 90,506

Other intangible assets at December 31, 2007 consist of the following (in thousands):

	Gross Amount	Accumulated Amortization	Net
Customer relationships	$ 80,435	$ 15,273	$ 65,162
Developed technology	48,173	18,539	29,634
Patents, trademarks and tradenames	13,833	5,000	8,833
Service contracts and other	6,815	2,767	4,048
Total other intangible assets	$ 149,256	$ 41,579	$ 107,677

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Amortization expense related to other intangible assets during the quarter and six months ended June 30, 2008 was $6.9 million and $13.9 million, respectively. Amortization expense related to other intangible assets during the quarter and six months ended June 30, 2007 was $5.7 million and $11.3 million, respectively.

As of June 30, 2008, estimated future amortization of other intangible assets is as follows (in thousands):

2008 (remaining six months)	$ 12,555
2009	23,222
2010	18,579
2011	13,109
2012	11,955
Thereafter	11,086
Total	$ 90,506

Note 10. Goodwill

Changes in goodwill are as follows (in thousands):

Balance, December 31, 2007	$ 353,153
Increases due to current year acquisitions	1,682
Decreases for the reduction of liabilities assumed related to the acquisition of Sony NetServices GmbH	(538)
Effects of foreign currency translation	(12,746)
Balance, June 30, 2008	$ 341,551

Note 11. Accrued and Other Liabilities

Accrued and other liabilities consist of (in thousands):

	June 30, 2008	December 31, 2007
Royalties and other fulfillment costs	$ 41,588	$ 37,554
Employee compensation, commissions and benefits	21,463	21,639
Sales, VAT and other taxes payable	13,252	18,156
Legal fees and contingent legal fees	2,883	3,439
Other	27,468	33,348
Other	$ 106,654	$ 114,136

Note 12. Loss on Excess Office Facilities

The accrued loss of $9.1 million for estimated future losses on excess office facilities located near the Company s corporate headquarters in Seattle Washington at June 30, 2008, is shown net of expected future sublease income of $6.4 million, which was committed under sublease contracts at the time of the estimate. The Company regularly evaluates the market for office space in the cities where it has operations. If the market for such space declines further in future periods, the Company may have to revise its estimates further, which may result in additional losses on excess office facilities.

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

Accrued loss on excess office facilities, December 31, 2007	$ 10,700
Less amounts amortized from the accrued loss on excess office facilities	(1,592)
Accrued loss on excess office facilities, June 30, 2008	9,108
Less current portion	4,311
Accrued loss on excess office facilities, non-current portion	$ 4,797

Note 13. Repurchase of Common Stock

In May 2008, the Company s Board of Directors authorized a new share repurchase program for the repurchase of up to an aggregate of $50.0 million of its outstanding common stock. During the quarter ended June 30, 2008, the Company purchased 0.2 million shares of its common stock at an average cost of $6.87 per share for an aggregate value of $1.5 million. As of June 30, 2008, $48.5 million remained authorized for repurchase under the repurchase program.

Note 14. 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):

	Quarters Ended June 30,		Six Months Ended June 30,	
	2008	2007	2008	2007
Weighted average common shares outstanding used to compute basic net income per share	142,905	153,880	142,946	157,929
Dilutive potential common shares:				
Stock options and restricted stock		4,403	2,304	5,143
Convertible debt		10,750	10,750	10,750
Shares used to compute diluted net income per share	142,905	169,033	156,000	173,822

During the quarter and six months ended June 30, 2008, 32.8 million and 33.1 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 quarter 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.

Note 15. Commitments and Contingencies

Borrowing Arrangements. The Company s subsidiary, WiderThan, has entered into two lines of credit with two Korean domestic banks with an aggregate maximum available limit of $2.8 million at interest rates of approximately 1.6% 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 $1.0 million bearing interest at 7.3%. During the quarter and six months ended June 30, 2008, the Company did not draw on these lines of credit and there were no balances outstanding as of June 30, 2008 and December 31, 2007.

The Company s subsidiary, WiderThan, uses corporate charge cards issued by a Korean domestic bank with an aggregate line of credit of up to $4.8 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), which 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 quarter and six months ended June 30, 2008, the Company did not draw on the letter of credit and there was no balance outstanding as of June 30, 2008 or December 31, 2007.

The Company s subsidiary, WiderThan, has purchased guarantees amounting to $0.5 million from Seoul Guarantee Insurance which guarantees payments for one year under certain supply contracts the Company has with a customer in Korea.

Purchase Obligations. As of June 2008, the Company has commitments with third party vendors to pay $16.9 million and $23.4 million through the years ended May 31, 2009 and 2010, respectively. These commitments are ordinary course expenses relating to the Company's on-going business operations.

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, and on October 4, 2007, the district court for the Northern District of California granted the motion to stay the case pending reexamination of the proceedings. 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 appealed the court s ruling.

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. These rates are still under appeal and are subject to industry-wide settlement negotiations, in some of which the Company is a participant. Additionally, the CRB is currently holding hearings that will determine mechanical royalty rates associated with the statutory license for digital phonorecord deliveries, including tethered downloads. These rates are also subject to industry-wide settlement negotiations. Finally, the Company is involved in a proceeding in the Southern District of New York that will determine a royalty rate for the public performance of music contained in the ASCAP catalogue. In April 2008, the district court issued a preliminary ruling that sets forth, among other things, a methodology to be used to calculate the royalties owed to ASCAP. The methodology to be used to calculate the royalties is incomplete and contains elements that require negotiation and agreement by the parties in addition to further hearings and decisions by the district court. On July 16, 2008, the court issued its ruling relating to the application of the new rates. The Company is working with ASCAP to make a final determination of amounts due under the court s ruling. The Company believes it has sufficiently accrued for expected royalties as of December 31, 2007 and June 30,2008. It is too soon to tell what ultimate effect the district court s preliminary ruling will have on the Company or what additional royalty amounts, if any, might ultimately be payable to ASCAP. Any of these three proceedings may result in higher rates or other terms that are unfavorable to the Company. Due to the uncertainties previously described, the Company is unable to reasonably estimate the amount of possible additional liabilities associated with the resolution of these matters beyond what has been previously recorded.

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.

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Note 16. Segment Information

SFAS No. 131, Disclosures about Segments of an Enterprise and Related Information, establishes standards for the way in which public companies disclose certain information about operating segments in their financial reports. After the formation of Rhapsody America in August 2007, the Company has defined three reportable segments consistent with SFAS No. 131, based on factors such as how the Company manages its operations and how its Chief Operating Decision Maker reviews results. 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 Music, Consumer and Technology Products and Solutions segments and, therefore, the Company reports these as operating segments as defined by SFAS No. 131. The accounting policies used to derive segment results are generally the same as those described in Note 1.

The Music segment includes the operations of Rhapsody America as well as the aspects of our music business not included as part of Rhapsody America. The revenue and costs from these businesses include: digital media subscription services such as Rhapsody and RadioPass; and sales of digital music and advertising. These products and services are 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.

The Consumer segment primarily includes revenue and costs from: the sale of individual games through the Company s RealArcade service and its Games related websites; the Company s GamePass and FunPass subscription service; the Company s 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 the Company s Music business. These products and services are 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.

The Technology Products and Solutions segment includes revenue and costs 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.

Amounts that are not included within the above segment descriptions are shown below as Reconciling Amounts. Included within these amounts are items such as interest income and net antitrust litigation benefit.

Segment income (loss) before income taxes for the quarter ended June 30, 2008 is as follows (in thousands):

	Music	Consumer	Technology Products and Solutions	Reconciling Amounts	Consolidated
Net revenue	$ 37,170	$ 64,183	$ 51,295	$	$ 152,648
Cost of revenue	20,693	14,362	20,590		55,645
Gross profit	16,477	49,821	30,705		97,003
Operating expenses	32,652	44,029	32,778	237	109,696
Operating income (loss)	(16,175)	5,792	(2,073)	(237)	(12,693)

Total non-operating income, net	11,548			3,540	15,088
Income (loss) before income taxes	$ (4,627)	$ 5,792	$ (2,073)	$ 3,303	$ 2,395

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Segment income (loss) before income taxes for the six months ended June 30, 2008 is as follows (in thousands):

	Music	Consumer	Technology Products and Solutions	Reconciling Amounts	Consolidated
Net revenue	$ 75,249	$ 122,390	$ 102,572	$	$ 300,211
Cost of revenue	42,212	26,975	41,851		111,038
Gross profit	33,037	95,415	60,721		189,173
Operating expenses	65,623	81,661	64,964	1,160	213,408
Operating income (loss)	(32,586)	13,754	(4,243)	(1,160)	(24,235)
Total non-operating income, net	23,889			9,175	33,064
Income (loss) before income taxes	$ (8,697)	$ 13,754	$ (4,243)	$ 8,015	$ 8,829

Segment income (loss) before income taxes for the quarter ended June 30, 2007 is as follows (in thousands):

	Music	Consumer	Technology Products and Solutions	Reconciling Amounts	Consolidated
Net revenue	$ 36,801	$ 50,314	$ 49,056	$	$ 136,171
Cost of revenue	19,804	9,436	19,959		49,199
Gross profit	16,997	40,878	29,097		86,972
Operating expenses	24,037	34,814	33,096	202	92,149
Operating income (loss)	(7,040)	6,064	(3,999)	(202)	(5,177)
Total non-operating income, net				8,682	8,682
Income (loss) before income taxes	$ (7,040)	$ 6,064	$ (3,999)	$ 8,480	$ 3,505

Segment income (loss) before income taxes for the six months ended June 30, 2007 is as follows (in thousands):

	Music	Consumer	Technology Products and Solutions	Reconciling Amounts	Consolidated
Net revenue	$ 70,928	$ 101,227	$ 93,488	$	$ 265,643
Cost of revenue	38,679	18,564	37,899		95,142
Gross profit	32,249	82,663	55,589		170,501
Operating expenses	48,986	67,721	63,634	(58,406)	121,935
Operating income (loss)	(16,737)	14,942	(8,045)	58,406	48,566
Total non-operating income, net				18,119	18,119
Income (loss) before income taxes	$ (16,737)	$ 14,942	$ (8,045)	$ 76,525	$ 66,685

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):

	Quarters Ended June 30,		Six Months Ended June 30,	
	2008	**2007**	**2008**	**2007**
United States	$ 100,898	$ 88,035	$ 200,067	$ 172,589
Europe	27,196	20,522	51,363	38,232
Republic of Korea	12,770	18,885	26,090	37,284
Rest of the World	11,784	8,729	22,691	17,538
Total net revenue	$ 152,648	$ 136,171	$ 300,211	$ 265,643

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

	June 30, 2008	December 31, 2007
United States	$ 191,213	$ 186,665
Republic of Korea	202,415	235,728
Europe	90,527	87,181
Rest of the World	8,420	7,753
Total long-lived assets	$ 492,575	$ 517,327

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

	June 30, 2008	December 31, 2007
United States	$ 586,838	$ 576,994
Republic of Korea	201,685	228,153
Europe	85,291	79,410
Rest of the World	8,827	10,160
Total net assets	$ 882,641	$ 894,717

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

	June 30, 2008	December 31, 2007
Music	$ 37,029	$ 37,029
Consumer	134,745	129,621
Technology products and solutions	169,777	186,503
Total goodwill	$ 341,551	$ 353,153

Note 17. Related Party Transactions

Transactions with MTVN. As part of the formation of Rhapsody America, MTVN contributed a $230 million five-year note payable in partial consideration for acquiring MTVN s interest in the venture. Rhapsody America is obligated to purchase $230 million in advertising and related integrated marketing on MTVN network properties over a five-year period. During the quarter ended June 30, 2008, Rhapsody America received $7.2 million in cash as a note payment and spent $9.2 million in advertising with MTVN. During the six months ended June 30, 2008, Rhapsody America received $14.4 million in cash as a note payment and spent $16.6 million in advertising with MTVN. During the year ended December 31, 2007, Rhapsody America received $25.0 million in cash as a note payment and spent $24.4 million in advertising with MTVN.

MTVN provides various support services directly to Rhapsody America for which it bills the venture directly. Included within the support services are items such as facilities, personnel and overhead which are allocated based on various measures depending on the service provided, including employee headcount, or number of users of a service. MTVN charged costs for the support services, revenue and related costs for the quarter and six months ended June 30, 2008 was $0.6 and $1.0 million, respectively. This amount is included in the unaudited condensed consolidated financial statements within the related party payable of $10.0 million as of June 30, 2008.

The Company also agreed to grant options to acquire shares of RealNetworks, Inc. common stock to Rhapsody America employees as part of the venture with MTVN and has included the expense associated with these options in its statement of operations and comprehensive income. MTVN s share of the expense associated with the stock options granted to Rhapsody America employees is calculated based on its ownership percentage and is billed directly by the Company to MTVN under a separate agreement. The

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Company has charged $0.2 million to MTVN related to stock options since the formation of the venture. This amount was paid in full by MTVN prior to June 30, 2008.

RealNetworks also provides various support services, including items such as facilities, information technology systems, personnel and overhead, directly to Rhapsody America. The allocation of other support service costs are based on various measures depending on the service provided, including employee headcount, time employees spend on providing services to Rhapsody America, server usage or number of users of a service. The allocations of these costs are billed directly to Rhapsody America. RealNetworks has treated these allocations as intercompany transactions and all such transactions were eliminated in consolidation.

Note 18. Subsequent Events

On July 1, 2008, the Company s convertible debt put option was exercised by the holders of approximately $99.9 million of the debt. The Company has accepted for purchase all of the debt validly surrendered and not withdrawn. The purchase price for the debt pursuant to the put option was $1,000 in cash per $1,000 principal amount at maturity. After the purchase pursuant to the put option, approximately $0.1 million principal amount at maturity of the debt remains outstanding.

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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, tax benefits, net income per diluted share, acquisition costs and related amortization, and other measures of results of operations;

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

plans, strategies and expected opportunities for growth, increased profitability and innovation in 2008 and future years;

the creation of new strategic partnerships and broadening of existing strategic partnerships and the advantages and growth we will achieve as a result of such partnerships (including in connection with our Games, Music and Technology Products and Solutions businesses);

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

the governance, management, accounting and integration of our Rhapsody America venture;

the dilutive impact on our shareholders if the call or put rights contained in the limited liability agreement for Rhapsody America are exercised and result in the issuance of additional shares of our common stock;

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

RealNetworks intention to separate its games business, distribute shares of the newly created games company to its shareholders, the potential sale of up to 20% of the shares of the new games company in an initial public offering and the anticipated tax-free nature of the proposed transactions;

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 and the availability of resources;

our expectations regarding acquisition activity in 2008 and our focus on the integration of completed acquisitions;

our relationships with our employees;

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. Our mission is to deliver world class digital entertainment experiences music, games or video wherever and whenever consumers want them. 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 AT&T and Verizon in the U.S., Vodafone in Europe, and SK Telecom in 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 (1) develop technology that provides meaningful differentiation to our chosen markets in digital entertainment services; (2) build a direct relationship with, and grow, our worldwide user base; and (3) create strong business partnerships with device makers, media companies, service providers and other distribution channels in order to build a sustainable and profitable global business. We intend to continue to expand our products and services beyond the PC to mobile devices and to create compelling digital media experiences on a variety of entertainment 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.

We have recently 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 providing free music streaming for top music websites, and our introduction of downloadable games monetized through 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.

On May 8, 2008 we announced that we intend to separate our casual games business into an independent company and to distribute shares of the newly created games company to our shareholders. We also announced that we may precede the spin-off with an initial public offering and sale of up to 20% of the shares of the new games company. We expect that either a spin-off or an IPO and subsequent spin-off will be tax-free to our shareholders. In addition to final approval by the our board of directors, completion of the transaction will be subject to a number of factors, including the effectiveness of a registration statement, the receipt of a favorable letter ruling from the Internal Revenue Service, the receipt of an opinion of tax counsel, market conditions, as well as the execution of inter-company agreements and other matters.

In the quarter ended June 30, 2008, total revenue grew 12% as compared with the quarter ended June 30, 2007, due primarily to continued growth in our Consumer segment which accounted for a majority of the growth. Consumer revenue growth was driven by increased revenue from our Media Software and Services business, increased sales of our games products as well as the effects from the April 2008 acquisition of Trymedia.

Our music revenue growth has slowed over the past two quarters due primarily to continuing challenges facing our subscription music business including limited distribution of compatible music devices, low consumer awareness of subscription music services, Apple s dominance of the portable mp3 player business and the persistant availability of free, unlicensed music content from peer-to-peer services. In response, we have shifted our business strategy and marketing efforts toward new, long-term initiatives as opposed to short-term subscriber growth. These initiatives included the launches of our new online mp3 store and of our Rhapsody subscription services with Verizon Wireless, as well as and the development of music-discovery services for consumer music websites, such as Yahoo, and MTV.com and the iLike application on Facebook. These three initiatives were launched on June 30, and had no revenue impact on our second quarter results.

We manage our business, and correspondingly report segment revenue and profit (loss), based on three segments: Music, Consumer and Technology Products and Solutions, each of which is described further below under Revenue by Segment and Costs of Revenue by Segment.

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;

Minority interest;

Accounting for gains on sale of subsidiary stock; and

Accounting for income taxes.

Accounting for taxes collected from customers.

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 music 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 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, 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 many arrangements, we contract directly with end user customers, are the primary obligor and carry all collectibility risk. In such arrangements we report the 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 the 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 costs in excess of total expected revenue are considered not recoverable and charged to operations in the period in which the determination is made.

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.

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 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 that 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 in this report.

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 in our common stock price 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. Prior to the adoption of SFAS No. 123R, we measured compensation expense for our employee stock-based compensation plans using the intrinsic value method prescribed by Accounting Principles Board Opinion (APB) No. 25, *Accounting for Stock Issued to Employees*. Under APB No. 25, when the exercise price of our employee stock options was equal to the market price of the underlying stock on the date of the grant, no compensation expense was recognized.

Minority Interests. The Company records minority interest expense (benefit) which reflects the portion of the earnings (losses) of majority-owned entities which are applicable to the minority interest partners in accordance with Accounting Research Bulletin No. 51, *Consolidated Financial Statements* (ARB No. 51). Redeemable minority interests that are redeemable at either fair value or are based on a formula that is intended to approximate fair value are accounted for in accordance with ARB No. 51. As of June 30, 2008 and December 31, 2007, the Company s minority interests solely related to redeemable minority interests in Rhapsody America. Minority interest expense (benefit) is included in the unaudited condensed consolidated statement of operations and comprehensive income for 2008.

Accounting for Gains on Sale of Subsidiary Stock. We account for any changes in our ownership interest resulting from the issuance of equity capital by consolidated subsidiaries as either a gain or loss in the statement of operations pursuant to SAB No. 51 *Accounting for the Sales of Stock of a Subsidiary*. SAB No. 51 requires that the difference between the carrying amount of the parent s investment in a subsidiary and the underlying net book value of the subsidiary after the issuance of stock by the subsidiary be reflected as either a gain or loss in the statement of operations if the appropriate recognition criteria has been met or reflected as an equity transaction. We have elected to reflect SAB No. 51 gains or losses in our consolidated statement of operations and comprehensive income.

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 basis 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 more likely than not, 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 and comprehensive income. Factors we consider in making such an assessment include, but are not limited to: past performance and our expectation of future taxable income, macroeconomic 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.

As of June 30, 2008, there have been no material changes to the Company s uncertain tax positions disclosures as provided in Note 15 of the 2007 Annual Report on Form 10-K. We do not anticipate that the total unrecognized tax benefits will significantly change within the next twelve months.

We file numerous consolidated, combined, 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. We are currently under United States Internal Revenue Service income tax audit for our wholly-owned subsidiary WiderThan Americas, Inc. for the period ended December 31, 2005.

Accounting for Taxes Collected From Customers. We collect various types of taxes from our customers, assessed by governmental authorities, that are imposed on and concurrent with revenue-producing transactions. Such taxes are recorded on a net basis and are not included in our net revenue.

Revenue by Segment

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

	Quarters Ended June 30,			Six Months Ended June 30,		
	2008	**Change**	**2007**	**2008**	**Change**	**2007**
Music	$ 37,170	1%	$ 36,801	$ 75,249	6%	$ 70,928
Consumer	64,183	28	50,314	122,390	21	101,227
Technology Products and Solutions	51,295	5	49,056	102,572	10	93,488
Total net revenue	$ 152,648	12%	$ 136,171	$ 300,211	13%	$ 265,643

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

	Quarters Ended June 30,		Six Months Ended June 30,	
	2008	**2007**	**2008**	**2007**
Music	24%	27%	25%	27%
Consumer	42	37	41	38
Technology Products and Solutions	34	36	34	35
Total net revenue	100%	100%	100%	100%

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. 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.

Music revenue increased 1% and 6% during the quarter and six months ended June 30, 2008, respectively, compared with the quarter and six months ended June 30, 2007. The increase during the quarter and six months ended June 30, 2008 was due primarily to slight growth in revenue from our subscription-based music products, offset by a nominal decrease in sales of music track downloads which together accounted for the majority of the revenue increases in both periods. No other single factor contributed materially to the change during the periods. Our music revenue growth has slowed over the past two quarters due primarily to continuing challenges facing our subscription music business, including limited distribution of compatible music devices, low consumer awareness of subscription music services, Apple s dominance of the portable mp3 player business and the persistent availability of free unlicensed music content from peer-to-peer services.

Consumer. Consumer revenue primarily includes revenue from: digital media subscription services such as GamePass, FunPass, SuperPass and stand-alone subscriptions; sales and distribution of third-party software and services; sales of digital content such as 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 revenue increased 28% and 21% during the quarter and six months ended June 30, 2008, compared with the quarter and six months ended June 30, 2007, respectively. Factors contributing to the change in revenue are discussed below in the sections included within Consumer revenue.

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 5% and 10% during the quarter and six months ended June 30, 2008, respectively, compared with the quarter and six months ended June 30, 2007. The increase during the quarter ended June 30, 2008 was due primarily to an increase in royalties from handset shipments and sales of application services to wireless carriers, including ringback tones, music-on-demand, inter-carrier messaging, and video-on-demand services offset by a decrease in server software revenue and system integration revenue. These changes accounted for substantially all of the revenue increases in both periods.

Consumer Revenue

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

	Quarters Ended June 30,			Six Months Ended June 30,		
	2008	**Change**	**2007**	**2008**	**Change**	**2007**
Games	$ 34,945	40%	$ 24,895	$ 66,743	37%	$ 48,797
Media Software and Services	29,238	15	25,419	55,647	6	52,430
Total consumer products and services revenue	$ 64,183	28%	$ 50,314	$ 122,390	21%	$ 101,227

Games. Games revenue primarily includes revenue from: the sale of individual games through our RealArcade service and our Games related websites; our GamePass and FunPass subscription service; and advertising through RealArcade and our Games related websites.

Games revenue increased 40% and 37% during the quarter and six months ended June 30, 2008, respectively, compared with the quarter and six months ended June 30, 2007. These increases were due primarily to increased syndication revenue of $4.0 million generated from our Trymedia acquisition, as well as an increase in advertising and subscription revenue generated through our RealArcade service and our websites. These increases in syndication, advertising and subscription revenue together accounted for 84% and 63% of the increase for the quarter and six months ended June 30, 2008, respectively. No other single factor contributed materially to the change during the periods. We believe the growth in Games revenue is due in part to product improvements and increasing consumer acceptance and adoption of digital media products and services. We cannot predict with accuracy how our 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.

Media Software and Services. Media Software and Services revenue primarily includes revenue from: our SuperPass and stand-alone premium video subscription services; premium versions of RealPlayer such as 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 increased 15% and 6% during the quarter and six months ended June 30, 2008, respectively, compared with the quarter and six months ended June 30, 2007. The increase during the quarter and six months ended June 30, 2008 was due primarily to an increase in distribution partner revenue and from sales of premium versions of RealPlayer, offset by a decrease in SuperPass revenue. These factors accounted for substantially all of the revenue increase for both periods. No other single factor contributed materially to the change during the period.

Geographic Revenue

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

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	Quarters Ended June 30,			Six Months Ended June 30,		
	2008	Change	2007	2008	Change	2007
United States	$ 100,898	15%	$ 88,035	$ 200,067	16%	$ 172,589
Europe	27,196	33	20,522	51,363	34	38,232
Republic of Korea	12,770	(32)	18,885	26,090	(30)	37,284
Rest of the world	11,784	35	8,729	22,691	29	17,538
Total net revenue	$ 152,648	12%	$ 136,171	$ 300,211	13%	$ 265,643

Revenue in the U.S. increased 15% and 16% for the quarter and six months ended June 30, 2008, respectively, compared to the quarter and six months ended June 30, 2007. The increases were due primarily to growth in our Consumer segment, including the acquisition of Trymedia in April 2008. See *Revenue by Segment* above for further discussion of these changes.

Revenue in Europe increased 33% and 34% during the quarter and six months ended June 30, 2008, respectively, compared to the quarter and six months ended June 30, 2007. The increases were due primarily to the continued growth of our Games and Technology Products and Solutions businesses in Europe. See *Revenue by Segment* above for further discussion of these changes.

Revenue in the Republic of Korea decreased 32% and 30% for the quarter and six months ended June 30, 2008, respectively, compared to the three and six months ended June 30, 2007. These decreases were due primarily to a decline in revenue from our systems integration business. See *Revenue by Segment* above for further discussion of these changes.

License and Service Revenue

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

	Quarters Ended June 30,			Six Months Ended June 30,		
	2008	Change	2007	2008	Change	2007
License fees	$ 28,613	29%	$ 22,212	$ 54,368	23%	$ 44,049
Service revenue	124,035	9	113,959	245,843	11	221,594
Total net revenue	$ 152,648	12%	$ 136,171	$ 300,211	13%	$ 265,643

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

	Quarters Ended June 30,		Six Months Ended June 30,	
	2008	2007	2008	2007
License fees	19%	16%	18%	17%
Service revenue	81	84	82	83
Total net revenue	100%	100%	100%	100%

License Fees. License fees primarily include revenue from: sales of content such as game licenses and digital music tracks; sales of our media delivery system software; sales of premium versions of our RealPlayer and related products; sales of messaging gateways to mobile carriers; and sales of third-party products. License fees include revenue from all of our reporting segments.

License revenue increased 29% and 23% during the quarter and six months ended June 30, 2008, respectively, compared to the quarter and six months ended June 30, 2007. The increase during the quarter and six months ended June 30, 2008 was due primarily to an increase in revenue from sales of premium version of RealPlayer, increased syndication revenue generated from our Trymedia acquisition and increased royalties from handset shipments. These factors accounted for substantially all of the increase during the quarter and six months ended. No other single factor contributed materially to the change during the periods.

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 all of our reporting segments.

Service revenue increased 9% and 11% during the quarter and six months ended June 30, 2008, respectively, compared with the quarter and six months ended June 30, 2007. The increase during the quarter ended June 30, 2008 was due primarily to increased subscription revenue from our Music and Games businesses, increased distribution partner revenue from our Consumer segment and increased sales of application services offset by a decrease in system integration revenue. These changes accounted for substantially all of the overall increase for both periods; 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, 2008 of $42.3 million compared with $42.2 million at December 31, 2007. The change in deferred revenue was due to an increase in unearned subscription services offset by the recognition of prepayments from wireless carriers for applications to deliver ringback tone, music-on-demand, and video-on-demand. These changes accounted for substantially all of the overall increase.

Cost of Revenue by Segment

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

	Quarters Ended June 30,			Six Months Ended June 30,		
	2008	Change	2007	2008	Change	2007
Music	$ 20,693	4%	$ 19,804	$ 42,213	9%	$ 38,679
Consumer	14,362	52	9,436	26,974	45	18,564
Technology products and solutions	20,590	3	19,959	41,851	10	37,899
Total cost of revenue	$ 55,645	13%	$ 49,199	$ 111,038	17%	$ 95,142

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

	Quarters Ended June 30,		Six Months Ended June 30,	
	2008	2007	2008	2007
Music	56%	54%	56%	55%
Consumer	22	19	22	18
Technology products and solutions	40	41	41	41
Total cost of revenue	36%	36%	37%	36%

Cost of Music. Cost of Music revenue consists primarily of cost of content and delivery of the content included in our music subscription service offerings; royalties paid on sales and streams of music; hardware devices and accessories; and fees paid to third-party vendors for order fulfillment and support services. Cost of Music revenue increased 4% and 9% during the quarter and six months ended June 30, 2008, respectively, compared with the quarter and six months ended June 30, 2007 primarily due to content and royalties costs related to our music subscription service resulting from the service being a higher percentage of revenue. Increases in these costs accounted for substantially all of the increases for the quarter and six months ended June 30, 2008. No other single factor contributed materially to the change during the periods.

Cost of Consumer. Cost of Consumer revenue consists primarily of cost of content and delivery of the content included in our digital media subscription service offerings; royalties paid on sales of games and other third-party products; amounts paid for licensed technology; costs of product media, duplication, manuals and packaging materials; and fees paid to third-party vendors for order fulfillment and support services. Cost of Consumer revenue increased 52% and 45% during the quarter and six months ended June 30, 2008, respectively, compared with the quarter and six months ended June 30, 2007. The increase during the quarter and six months ended June 30, 2008 was due primarily to growth in subscription revenue from our games subscription services, and increased costs of content of our digital media subscription service, and increased costs of content related to syndication game sales due to the acquisition of TryMedia. These factors accounted for substantially all of the increases for the quarter and six months ended June 30, 2008. No other single factor contributed materially to the change during the periods. The increase of costs of content were primarily responsible for the increase of costs as a percentage of revenue.

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 service carriers and third-party vendors for order fulfillment, cost of personnel providing support and consulting services, and expenses incurred in providing our streaming media hosting services. Cost of technology products and solutions increased 3% and 10% during the quarter and six months ended June 30, 2008, respectively, compared with the quarter and six months ended June 30, 2007. The increased costs were related to the increase of revenue generated from sales of application services to wireless carriers. This accounted for substantially all of the increase for the quarter and six months ended June 30, 2008; no other single factor contributed materially to the change during the periods.

Cost of License and Service Revenue

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

	Quarters Ended June 30,			Six Months Ended June 30,		
	2008	Change	2007	2008	Change	2007
License fees	$ 10,614	35%	$ 7,882	$ 20,002	24%	$ 16,174
Service revenue	45,031	9	41,317	91,036	15	78,968
Total cost of revenue	$ 55,645	13%	$ 49,199	$ 111,038	17%	$ 95,142

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

	Quarters Ended June 30,		Six Months Ended June 30,	
	2008	2007	2008	2007
License fees	37%	35%	37%	37%
Service revenue	36	36	37	36
Total cost of revenue	36%	36%	37%	36%

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 increased 35% and 24% during the quarter and six months ended June 30, 2008, respectively, compared with the quarter and six months ended June 30, 2007 due primarily to increases in online sales of games including increased costs of content related to syndication game sales due to the acquisition of Trymedia (which was completed on April 1, 2008). Increases in these costs accounted for 93% of the increase for the quarter ended June 30, 2008 and substantially all of the increase for the six months ended June 30, 2008; 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 9% and 15% during the quarter and six months ended June 30, 2008, respectively, compared with the quarter and six months ended June 30, 2007. Substantially all of the increase in the cost of service revenue in the quarter and six months ended June 30, 2008, were due to increases in volume and revenue from carrier application services, delivery of streaming music, and delivery of our games subscription service; 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):

	Quarters Ended	Six Months Ended

	2008	June 30, Change	2007	2008	June 30, Change	2007
Research and development	$29,065	16%	$25,005	$54,071	12%	$48,484
As a percentage of total net revenue	19%		18%	18%		18%

Research and development expenses, including non-cash stock-based compensation, increased 16% and 12% during the quarter and six months ended June 30, 2008, respectively, compared with the quarter and six months ended June 30, 2007. This increase was due primarily to an overall increase in personnel and related costs, expenses related to Trymedia (acquired in April 2008) and

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consulting services which accounted for substantially all of the total increase in research and development costs. No other single factor contributed materially to the increase during the period. The increase in research and development expenses as a percentage of total net revenue for the quarter ended June 30, 2008 is due primarily to a higher growth in total research and development expenses.

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):

	Quarters Ended June 30,			Six Months Ended June 30,		
	2008	**Change**	**2007**	**2008**	**Change**	**2007**
Sales and marketing	$53,054	6%	$50,081	$106,650	7%	$99,781
As a percentage of total net revenue	35%		37%	36%		38%

Sales and marketing expenses, including non-cash stock-based compensation, increased 6% and 7% during the quarter and six months ended June 30, 2008, respectively, compared with the quarter ended June 30, 2007. Increases in consulting services, costs related to Trymedia, amounts amortized from the other intangible assets capitalized in our acquisitions and advertising accounted for approximately 61% and 48% of the total increase in sales and marketing expenses during the quarter and six months ended June 30, 2008, respectively. An additional 23% and 24% of the increase in sales and marketing expenses during the quarter and six months ended June 30, 2008, respectively, was due to an increase in amortization of other intangible assets capitalized in our acquisitions. 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):

	Quarters Ended June 30,			Six Months Ended June 30,		
	2008	**Change**	**2007**	**2008**	**Change**	**2007**
General and administrative	$18,337	7%	$17,063	$35,421	3%	$34,417
As a percentage of total net revenue	12%		13%	12%		13%

General and administrative expenses, including non-cash stock-based compensation, increased 7% and 3% during the quarter and six months ended June 30, 2008, respectively, compared with the quarter and six months ended June 30, 2007. Increases in personnel and related costs and other taxes and licenses, offset by decreases in our legal fees, accounted for substantially all of the increase in general and administrative expenses during the quarter ended June 30, 2008. Increases in personnel and related costs, consulting and legal fees, offset by decreases in our charitable donations and accounting fees, accounted for substantially all of the increase in general and administrative expenses during the six months ended June 30, 2008. The decrease in general and administrative expenses as a percentage of total net revenue is due to a higher growth in total net revenue.

Advertising with Related Party

Rhapsody America is obligated to purchase $230 million in advertising and related integrated marketing on MTVN cable channels over the term of the agreement. During the quarter and six months ended June 30, 2008, Rhapsody America spent $9.2 million and $16.6 million in advertising with MTVN. No such amounts were spent during the quarter and six months ended June 30, 2007.

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 and six months ended June 30,

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2008. 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.

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):

	Quarters Ended June 30,			Six Months Ended June 30,		
	2008	Change	2007	2008	Change	2007
Interest income, net	$ 3,375	(58)%	$ 8,065	$ 8,333	(51)%	$ 17,167
Equity in net loss of investments	(107)	n/a		(198)	50	(132)
Gain on sale of equity investment	222	68	132	222	68	132
Minority interest in Rhapsody America	8,177	n/a		16,792	n/a	
Gain on sale of interest in Rhapsody America	3,371	n/a		7,097	n/a	
Other income, net	50	(90)	485	818	(14)	952
Other income, net	$ 15,088	74%	$ 8,682	$ 33,064	82%	$ 18,119

Other income, net increased during the quarter and six months ended June 30, 2008 due primarily to minority interest in Rhapsody America and the gains recognized on the sale of interest in Rhapsody America. These were offset in part by a decrease in interest income due to a decrease in our average investment balance.

Income Taxes

During the quarters ended June 30, 2008 and 2007, we recognized income tax expense of $3.7 million and $2.2 million, respectively, related to U.S. and foreign income taxes. During the six months ended June 30, 2008 and 2007, we recognized income tax expense of $7.7 million and $25.4 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. The increase in tax expense as a percentage of pre-tax income during the quarter and six months ended June 30, 2008 was the result of our lower net income combined with losses not benefited in certain foreign jurisdictions.

As of June 30, 2008, there have been no material changes to the Company s uncertain tax positions disclosures as provided in Note 15 of the 2007 Annual Report on Form 10-K. We do not anticipate that total unrecognized tax benefits will significantly change within the next twelve months.

We file numerous consolidated, combined, 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. We are currently under United States Internal Revenue Service income tax audit for our wholly-owned subsidiary WiderThan Americas, Inc. for the period ended December 31, 2005.

New Accounting Pronouncements

In December 2007, the FASB issued SFAS No. 141R, Business Combinations (SFAS 141R), which establishes principles and requirements for how an acquirer recognizes and measures in its financial statements the identifiable assets acquired, the liabilities assumed, and any noncontrolling interest in an acquiree, including the recognition and measurement of goodwill acquired in a business combination. The requirements of SFAS 141R are effective for the Company for periods beginning after December 15, 2008. Early adoption is prohibited. We are in the process of evaluating this guidance and therefore have not yet determined the impact that SFAS 141R will have on our financial position or results of operations upon adoption.

In December 2007, the FASB issued SFAS No. 160, Noncontrolling Interest in Consolidated Financial Statements, an amendment of ARB No. 51 (SFAS 160), which will change the accounting and reporting for minority interests and which will be recharacterized as noncontrolling interests and classified as a component of equity within the consolidated balance sheets. SFAS 160 requires that changes in a parent s ownership interest while the parent retains its controlling financial interest shall be accounted for as equity transactions. As a result, beginning in 2009, the gain on sales of interest in Rhapsody America will no longer be recorded in the statement of operations, but will be reflected as a component of shareholders equity. The requirements of SFAS 160 are effective for the Company for periods beginning after December 15, 2008. Early adoption is prohibited. We are in the process of evaluating all the impacts of this guidance and therefore have not yet determined the full impact that SFAS 160 will have on our financial position or results of operations upon adoption.

In March 2008, the FASB affirmed the consensus of FSP APB 14-1, *Accounting for Convertible Debt Instruments That May Be Settled in Cash upon Conversion (Including Partial Cash Settlement)* (FSP APB 14-1) which applies to all convertible debt instruments that have a net settlement feature , which means instruments that by their terms may be settled either wholly or partially in cash upon conversion. FSP APB 14-1 requires issuer s of convertible debt instruments that may be settled wholly or partially in cash upon conversion to separately account for the liability and equity components in a manner reflective of the issuer s nonconvertible debt borrowing rate. Previous guidance provided for accounting for this type of convertible debt instrument entirely as debt. The FSP requires retrospective application to all periods presented and does not grandfather existing debt instruments. FSP APB 14-1 is effective for financial statements issued for fiscal years beginning after December 15, 2008 and interim periods within those fiscal years. We are currently evaluating the impact FSP APB 14-1 may have on our financial position or results of operations upon adoption.

In April 2008, the FASB issued FSP No. 142-3, *Determination of the Useful Life of Intangible Assets* (FSP 142-3). FSP 142-3 amends the factors that should be considered in developing renewal or extension assumptions used to determine the useful life of a recognized intangible asset under FASB Statement No. 142, *Goodwill and Other Intangible Assets*. FSP 142-3 is effective for financial statements issued for fiscal years beginning after December 15, 2008. Early adoption is prohibited. We are currently evaluating the impact FSP No. 142-3 may have on our financial position or results of operations upon adoption.

In May 2008, the FASB issued SFAS No. 162, *The Hierarchy of Generally Accepted Accounting Principles*, (SFAS 162). This Statement identifies the sources of accounting principles and the framework for selecting the principles to be used in the preparation of financial statements of nongovernmental entities that are presented in conformity with U.S. GAAP (the GAAP hierarchy). While the effective date of this pronouncement has not yet been determined, the Company is currently assessing the impact SFAS 162 may have on our financial position or results of operations upon adoption.

Liquidity and Capital Resources

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

	June 30, 2008	December 31, 2007
Working capital	$350,225	$351,066
Cash, cash equivalents, and short-term investments	522,667	556,629
Restricted cash	14,670	15,509

Cash, cash equivalents, and short-term investments decreased primarily for the use of cash in operations as well as the purchases of equipment, software and leasehold improvements.

The following summarizes cash flows (in thousands):

	June 30, 2008	June 30, 2007
Cash used in operating activities	$(28,278)	$(206,296)
Cash used in investing activities	(50,261)	(3,946)
Cash provided by (used in) financing activities	20,055	(95,032)

Net use of cash in operating activities in 2008 was primarily due to a net decrease in certain operating assets and liabilities totaling $39.2 million which includes a decrease in accounts payable, and related party payables along with increases to prepaids and other current assets of $39.0 million, offset by net income, and decreases in accounts receivable of $13.5 million. Operating activities use of cash in 2007 was primarily from 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.

In 2008, investing activities used cash primarily for purchases of equipment, software, and leasehold improvements of $15.2 million and $10.2 million of acquisition costs, net of cash acquired from the acquisition of Trymedia and the payment of anniversary and performance costs relating to the Zylom purchase which were previously accrued. Purchases net of sales and maturities of short-term investments used cash of $26.9 million during 2008. In 2007, investing activities used cash primarily for purchases of equipment, software, and leasehold improvements of $11.5 million as well as the purchases of SNS and Exomi which used cash net of cash acquired of $21.0 million. Sales and maturities net of purchases of short-term investments provided cash of $31.5 million during the six months ended June 30, 2007.

Financing activities provided cash from the proceeds from the sales of interest in Rhapsody America of $14.6 million in 2008 and sales of common stock under employee stock purchase plan and exercise of stock options of $6.0 million in 2008 and $12.3 million in 2007. The cash provided was offset with the repurchase of our common stock of $0.7 million and $107.9 million during the six months ended June 30, 2008 and 2007, respectively.

In May 2008 our Board of Directors authorized a new share repurchase program for the repurchase of up to an aggregate of $50.0 million of our outstanding common stock. During the quarter ended June 30, 2008, we purchased 0.2 million shares of its common stock at an average cost of $6.87 per share for an aggregate value of $1.5 million. As of June 30, 2008, $48.5 million remained authorized for repurchase under the repurchase program.

We currently have no planned significant capital expenditures for 2008 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.

As of June 2008, we have commitments with third party vendors to pay $16.9 million and $23.4 million through the years ended May 31, 2009 and 2010, respectively. These commitments are ordinary course expenses relating to our on-going business operations.

On July 1, 2008, our convertible debt put option was exercised by the holders of approximately $99.9 million of the debt. We have accepted for purchase all of the debt validly surrendered and not withdrawn. After the purchase pursuant to the put option, approximately $0.1 million principal amount at maturity of the debt remains outstanding.

Our contractual obligations include convertible debt, office leases, and contractual payments due to content and other service providers. 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 quarters ended June 30, 2008 and 2007.

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 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 during the quarter ended June 30, 2008. Based on our cash, cash equivalents, short-term investments, and restricted cash equivalents at June 30, 2008, a hypothetical 10% increase/decrease in interest rates would increase/decrease our annual interest income and cash flows by approximately $0.5 million.

Investment Risk. As of June 30, 2008, 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. Based upon an evaluation of the facts and circumstances during the quarters and six month periods ended June 30, 2008 and 2007, we determined that no additional other-than-temporary decline in fair value had occurred and therefore no impairment charges were recorded.

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 quarter and six months ended June 30, 2008 and 2007.

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 quarter ended June 30, 2008 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 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. These rates are still under appeal and are subject to industry-wide settlement negotiations, in some of which we are a participant. The CRB is currently holding hearings that will determine mechanical royalty rates associated with the statutory license for digital phonorecord deliveries, including tethered downloads. These rates are also subject to industry-wide settlement negotiations. Finally, we are involved in a proceeding in the Southern District of New York that will determine a royalty rate for the public performance of music contained in the ASCAP catalogue. In April 2008, the district court issued a preliminary ruling that sets forth, among other things, a methodology to be used to calculate the royalties owed to ASCAP. The methodology to be used to calculate the royalties is incomplete and contains elements that require negotiation and agreement by the parties in addition to further hearings and decisions by the district court. On July 16, 2008, the court issued its ruling relating to the application of the new rates. We are working with ASCAP to make a final determination of amounts due under the courts ruling. We believe we have sufficiently accrued for expected royalties as of December 31, 2007 and June 30, 2008. It is too soon to tell what ultimate effect district court s preliminary ruling will have on us or what additional royalty amounts, if any, might ultimately be payable to ASCAP. Any of these three proceedings may result in higher rates or other terms that are unfavorable to us.

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 in Note 15 to the financial statements included in this report, 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 quarterly 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 Recently Announced Separation of Our Games Business

We recently announced our intention to separate our global games business into an independent company and to distribute shares of the newly created games company to our shareholders. We also indicated that we may precede the spin-off with an initial public offering and sale of up to 20% of the shares of the games company. If such transactions are not completed, our stock price and business may be adversely affected.

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On May 8, 2008, we announced our intention to separate our global games business into an independent company and distribute shares of the newly created games company to our shareholders. We also indicated that we may precede the spin-off with an initial public offering and sale of up to 20% of the shares of the new games company. We may not complete such transactions, each of which are subject to a number of factors including, among others, market conditions, the final approval of our board of directors, the effectiveness of a registration statement, the receipt of a favorable letter ruling from the Internal Revenue Service and the execution of inter-company agreements.

If the transactions are delayed or not completed, our stock price could decline, we will have incurred significant expenses which we will be unable to recover and we will not be able to recover the significant diversion of management and employee attention that we will have incurred in preparing for the transactions. In addition, our business and operations may be harmed to the extent there is customer or employee uncertainty surrounding the future direction of our product and service offerings and strategy.

Our games business represents a significant portion of our business and a spin-off or initial public offering of the games business may cause our operating results to suffer and may cause our revenues, income and stock price to decline.

The games business represents a significant portion of our business that is currently reported as a component of our Consumer segment in our consolidated financial statements. For the fiscal years ended 2007, 2006 and 2005, the games business represented approximately 19%, 22% and 17% of our revenues, respectively. Following the spin-off, the games business will no longer be a division of RealNetworks and its financial results, including its revenues and income, will no longer be included in RealNetworks consolidated financial statements. Accordingly, our historical consolidated financial information will not necessarily be comparable with our financial position, results of operations and cash flows after the games business ceases to be a division. We are unable to predict what the market price of our common stock will be after the spin-off or the potential initial public offering and the market price of our common stock could be volatile for several months after either transaction. Moreover, even if such transactions are consummated, we cannot assure you that we will be able to successfully achieve the intended benefits of either transaction or that they will result in any increase in value for our shareholders.

In connection with the proposed spin-off and potential initial public offering, we intend to prepare separate, audited historical annual financial statements and unaudited historical quarterly financial statements for our games business on a stand-alone basis. The operating results and financial data reflected in the stand-alone financial statements of our games business could differ from the operating results and financial data reported by us on a consolidated basis due to adjustments made during the preparation and/or audit of the stand-alone financial statements.

The separation and possible initial public offering of the games business is a substantial undertaking that may disrupt our ongoing business and may increase expenses, which may affect our results of operations or financial condition.

The planning and implementation of the separation of the games business from RealNetworks and the possible initial public offering and spin-off of the games company will require substantial dedication of management resources, and we expect to incur significant expenses related to the transactions. We have not yet made any adjustments to our historical financial information to reflect the significant changes that may occur in our cost structure, funding and operations as a result of these transactions. In addition, the efforts required to implement these transactions may disrupt our ongoing business activities, may result in employee distraction and may harm our business and our ability to attract, retain and motivate key employees. Additionally, perceived uncertainties as to our future direction may result in difficulties in recruiting and retaining employees and may also have a negative impact on our relationships with our customers, suppliers, vendors and partners and may result in the loss of business opportunities. If any of the foregoing occurs, our results of operations or financial condition would suffer.

Risks Related to Our Music and Consumer Businesses

Our music and consumer businesses face substantial competitive challenges that may prevent us from being successful in, and negatively impact future growth in, those businesses.

Many of our current and potential competitors in our music and consumer businesses 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 in these businesses include a number of large and powerful companies, such as

Microsoft and Apple. To effectively compete in the markets for our music and consumer businesses, we may experience the following consequences, any of which would adversely affect our operating results and the trading price of our stock:

- reduced prices or margins,

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- loss of current and potential customers, market share and market power,
- changes to our products, services, technologies, licenses or business practices or strategies,
- lengthened sales cycles,
- pressure to prematurely release products or product enhancements, or
- degradation in our stature and reputation in the market.

In addition, we face the following risks relating to our music, media software and solutions and games businesses:

Music. Our online music services now offered through our Rhapsody America joint venture with MTVN 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 iPhone. Microsoft has also begun offering premium music services in conjunction with its Windows Media Player and also 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 as well as other providers of free, ad-supported music services. 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, unlicensed content. 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. Rhapsody America may not be able to compete effectively in this highly competitive and rapidly evolving market, which may negatively impact the future growth of our Music business.

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 continue to be 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. If we are unable to compete successfully, the future growth of our Media Software and Services business will be negatively impacted. In addition, our overall ability to sell subscription services depends in part on the use of RealNetworks formats on the Internet, and declines in the use of our formats may negatively affect our subscription revenue and increase costs of obtaining new subscribers.

Games. Our RealArcade, GameHouse, and Zylom branded services compete with other online aggregators and distributors of online and downloadable casual PC games. Some of these competitors have high volume distribution channels and greater financial resources than we do. Our games business also competes with many other smaller companies which may be able to adjust to market conditions faster than us. 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 development studios compete primarily with other developers of online, 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.

The success of our subscription services businesses depends upon our ability to increase subscription revenue and to license compelling content on commercially reasonable terms.

Our operating results could be adversely impacted by the loss of subscription revenue, including the revenue generated from the online music services offered by our Rhapsody America joint venture. 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. In addition, we must continue to obtain compelling digital media content for our video, music, and games services in order to maintain and increase usage and overall customer satisfaction for these products. Our online music service offerings available through our Rhapsody America venture depend on music licenses from the major music labels and publishers, and the failure to renew these licenses under terms that are commercially reasonable and acceptable to us would harm Rhapsody America s ability to generate revenues from its subscription services.

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 be on our subscription revenue.

Music publishing royalty rates for music subscription services offered through RealNetworks and Rhapsody America 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, including those now conducted by Rhapsody America. We or Rhapsody America may be required to pay a rate that is higher than we expect, as the issue was submitted to a Rate Court by the American Society of Composers, Authors and Publishers (ASCAP) for judicial determination. We have license agreements to reproduce musical compositions with the Harry Fox Agency, an agency that represents music publishers, and with many independent music publishers as required in the creation and delivery of on-demand streams and tethered downloads, but these license agreements generally 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.

An appeal of, or other industry settlement relating to, 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. These rates are still under appeal and are also subject to industry-wide settlement negotiations, in some of which we are a participant. The appeal or other industry settlement, whether or not we directly participate in the settlement, may result in higher rates or other terms that are unfavorable to us, which could adversely impact our operating results and our ability to provide our radio services in the future.

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 and the popularity of the Adobe Flash format. 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 sales of our subscription services, and therefore could harm our business and our prospects.

We face risks with respect to certain matters in the governance and management of our Rhapsody America joint venture and the integration and operation of assets that have been combined to form Rhapsody America.

We and MTVN have formed Rhapsody America LLC, a Delaware limited liability company. We own, through a wholly owned subsidiary, 51% of the limited liability company membership interests of Rhapsody America and MTVN owns, through a wholly owned subsidiary, the remaining 49%. We are entitled to appoint the general manager to manage the day-to-day operations of Rhapsody America. Rhapsody America is governed by a limited liability company agreement which, among other things, requires unanimous approval of the members for certain key operational activities, such as adopting a budget and authorizing certain capital expenditures, and for significant company events, such as mergers, asset sales, distributions, affiliate transactions and issuance, sale and repurchase of membership interests of Rhapsody America. If we are not able to agree with MTVN on any of those items, if the members are unable to agree on any other significant operational or financial matter requiring approval of the members, or if there is any event that adversely impacts our relationship with MTVN, the business, results of operations and financial condition of Rhapsody America may be adversely affected and, consequently, our business may suffer. In addition, MTVN may have or develop economic or other business interests or goals that are inconsistent with our or Rhapsody America s business interests or goals.

Neither we nor the current management of Rhapsody America have extensive experience in managing and operating complex joint ventures of this nature, and the integration and operational activities may strain our internal resources, distract us from managing our day-to-day operations, and impact our ability to retain key employees in Rhapsody America. The nature of our and MTVN s contributions of services and assets to Rhapsody America required detailed cost allocation agreements that are complex to implement and manage and may result in significant costs that could adversely affect our operating results. The allocation of these support service costs is based on various measures depending on the service provided, and require significant internal resources. Many of the allocation methodologies are complicated, which may result in inaccuracies in the total charges to be billed to Rhapsody America. In addition, the variable nature of these costs to be allocated to Rhapsody America may result in fluctuations in the period-over-period results of our Music business.

We and MTVN have certain contractual rights relating to the purchase and sale of MTVN s membership interest in Rhapsody America that may be settled in part through the issuance of additional shares of our capital stock, which would dilute our other shareholders voting and economic interests in us, and may require us to pay MTVN a price that exceeds the appraised value of its proportionate interest in Rhapsody America.

Pursuant to the terms of the Rhapsody America limited liability company agreement, we have a right to purchase from MTVN, and MTVN has a right to require us to purchase, MTVN s membership interest in Rhapsody America. These call and put rights are exercisable upon the occurrence of certain events and during certain periods in each of 2012, 2013 and 2014 and every two years thereafter and may be settled, in part, through the issuance of shares of our capital stock, subject to specified limitations. If a portion of the purchase price for MTVN s membership interest is payable in shares of our capital stock, such shares could represent up to 15% of the outstanding shares of our common stock immediately prior to the transaction. In addition, we may also be obligated to issue shares of our non-voting stock representing up to an additional 4.9% of the outstanding shares of our common stock immediately prior to the transaction. If we pay a portion of the purchase price for MTVN s membership interest in shares of our common stock and non-voting stock, our other shareholders voting and economic interests in us will be diluted, and MTVN will become one of our significant shareholders. In certain situations, if MTVN exercises its right to require us to purchase its membership interests in Rhapsody America, we may be required to pay MTVN a price that provides a return to MTVN over the appraised value of MTVN s proportionate interest in Rhapsody America.

Risks Related to Our Technology Products and Solutions Business

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 generate a material portion of our revenue from operations in the Republic of Korea (South Korea), primarily from our mobile entertainment services offered 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 significant portion of our total revenue from South Korea, particularly through SK Telecom. In recent periods, revenue from SK Telecom has declined within our systems integration business and may continue to decline in future periods. 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. Furthermore, our relationship with SK Telecom may be affected by the general state of the economy of South Korea and tensions between North Korea and South Korea, which have fluctuated and may increase or change abruptly as a result of current and future events. Failure to maintain our relationship with SK Telecom 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 could be materially harmed.

Contracts with our carrier customers subject us to significant risks that could negatively impact our revenue or otherwise harm our operating results.

We 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. Because most of our carrier customer contracts are nonexclusive, 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 could 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. Despite the lack of marketing commitments, revenue related to our application services is, to a large extent, dependent upon the marketing and promotion activities of our carrier customers. In addition, 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. The loss of carrier customers, a reduction in marketing or promotion of our applications, or the termination, non-renewal or renegotiation of contract terms that are less favorable to us would likely result in the loss of future revenues from our carrier application services.

Finally, certain of our carrier contracts obligate us to indemnify the carrier customer for certain liabilities and losses incurred by them, including liabilities resulting from third party claims for damages that arise out of the use of our technology. These indemnification terms provide us with certain procedural safeguards, including the right to control the defense of the indemnified party. We have accepted tenders of indemnification from two of our carrier customers related to one pending patent infringement proceeding, and we are vigorously defending them. This pending proceeding or future claims against which we may be obligated to defend our carrier customers could result in paying amounts pursuant to these obligations that could materially harm our operating results.

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 current providers of music-on-demand services for online or other non-mobile platforms, some of which have greater financial resources than we do. In addition, the major music labels may demand more aggressive revenue sharing arrangements or impose an alternative business model less favorable to us. In addition, while most of our carrier customers do not offer internally developed application services that compete with ours, if 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. 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 traditional system software licensing business has been negatively impacted by competitive factors, and we may not experience improved 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. Although the settlement agreement we entered into with Microsoft relating to our claims regarding Microsoft s anticompetitive practices contained a substantial cash payment to us and a series of technology agreements, 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 in a way that improves our operating results or shareholder return on an investment in our stock.

Risks Related to Our Business in General

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

The trading price for our common stock has been volatile, ranging from $5.07 to $8.27 per share during the 52-week period ended June 30, 2008. As a result of the rapidly changing markets in which we compete, our operating results may fluctuate from period-to-period, which may continue to contribute to the volatility of our stock price. 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, including, but not limited to:

- our inability to realize SAB No. 51 gains within the statement of operations upon adoption of SFAS 160 in 2009, impairments of goodwill and other long-lived assets,

integrating and operating newly acquired businesses and assets,

the seasonality of our business, which has experienced increased revenues in the fourth quarter of our fiscal year, and the general difficulty in forecasting our operating results and metrics, which could result in actual results that differ significantly from expected results.

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. Fluctuations in our operating results, particularly when experienced beyond what we expected, could cause the trading price of our stock to continue to fluctuate.

New products and services may not achieve market acceptance or may be subject to legal challenge that could 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. For example, we launched a new version of our media delivery software, RealPlayer 11, that consumers can use 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. 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. 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. Furthermore, new products and services may be subject to legal challenge. For example, although we believe RealPlayer 11 is legal, there are 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. 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 our products or services, or to pay damages.

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, including 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.

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 and expect that we will continue to do so in the future. Since late 2006 through the second quarter of 2008, we completed the acquisition of substantially all of WiderThan Co., Ltd. and the acquisitions of Sony NetServices GmbH, Exomi Oy, Game Trust, Inc. and Trymedia. 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.

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

Access to the Internet through devices other than a 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 and services 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. In addition, in order for our services, in particular, the digital music services offered through Rhapsody America, to continue to grow, we must design services that interoperate effectively with a variety of hardware devices. To achieve this interoperability, we and Rhapsody America 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 do not successfully make our products and technologies compatible with emerging standards and the most popular devices used to access digital media or successfully design our service to interoperate with the music playback devices that our customers own, we may miss market opportunities and our business and results will suffer.

We may be unable to adequately protect our proprietary rights or leverage our patent portfolio, 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 patent portfolio and other 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. However, our efforts to protect our intellectual property rights may not assure our ownership rights in our intellectual property, protect or enhance the competitive position of our products and services or effectively prevent misappropriation of our technology. In addition, we do not know whether our patents will ultimately be deemed enforceable, valid, or infringed. As disputes regarding the validity and scope of patents or 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 patents and other intellectual property rights or to determine the validity and scope of other parties proprietary rights, enter into royalty or licensing agreements on unfavorable terms or redesign our product features and services. Any such dispute would likely be costly and distract our management, and the outcome of any such dispute could fail to improve our business prospects or otherwise harm our business.

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 Note 15 to the financial statements included in this report.

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 hurt customer demand for our products, 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, which expenditures could adversely affect our operating results.

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

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.

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 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 or from our Internet commerce activities.

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. The collection and remittance of VAT subjects us to additional currency fluctuation risks.

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.

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

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Our directors and executive officers beneficially own more than 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 more than one third of our common stock himself. 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.

In addition, Mr. Glaser has special rights under our articles of incorporation to appoint or remove members of the strategic transaction committee at his discretion that could make it more difficult for RealNetworks to be sold or to complete another change of control transaction without Mr. Glaser s consent.

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.

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

(a) Not applicable

(b) Not applicable

(c) Purchases of Equity Securities by the Issuer and Affiliated Purchasers (in thousands, except per share amounts):

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Period		Total Number of Shares Repurchased (In thousands)	Average Price Paid Per Share	Total Number of Shares Purchased as Part of Publicly Announced Plans or Programs	Approximate Dollar Value of Shares that May Yet Be Purchased Under the Plans or Programs
5/1/2008	5/31/2008	11	$ 7.01	11	$ 7.01
6/1/2007	6/30/2007	207	6.86	207	6.86
Total		218	$ 6.87	218	$ 6.87

In May 2008 the Board of Directors of the company authorized a new share repurchase program for the repurchase of up to an aggregate of $50.0 million of the Company s outstanding common stock. All of the repurchases in the table above were made through that program.

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 3, 2008. The matters voted on at the Annual Meeting and votes cast on such matters were as follows:

The election of one Class 2 director to serve until the 2011 Annual Meeting of Shareholders, or until such director s earlier retirement, resignation or removal, or at the election of his successor.

Directors Elected	For	Withheld
Jonathan D. Klein	130,774,814	1,362,025

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

Eric A. Benhamou
Robert Glaser
Edward Bleier
Jeremy Jaech
Kalpana Raina

The ratification of the appointment of KPMG LLP as the Company s registered public accounting firm for the fiscal year ended December 31, 2008.

	Votes
For	131,411,965
Against	610,187
Broker non-votes	
Abstain	114,687

Item 5. Other Information

None

Item 6. Exhibits

Exhibits Required by Item 601 of Regulation S-K

Exhibit Number	Description
10.1	Offer Letter dated July 1, 2008 between RealNetworks, Inc. and John Giamatteo
10.2	Form of MBO Plan Document under the Real Networks, Inc. 2008 Executive Compensation Program
10.3	Form of MBO Plan Document under the RealNetworks, Inc. 2008 Chief Executive Officer Compensation Program
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

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Exhibit Number	**Description**
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, 2008.

REALNETWORKS, INC.

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

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