REALNETWORKS INC
Form 10-K
February 26, 2015

UNITED STATES SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549
Form 10-K
(Mark One)

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

For the Fiscal Year Ended December 31, 2014
OR

¨ 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)

1501 First Avenue South, Suite 600, Seattle, Washington, 98134
(206) 674-2700
(Address of principal executive offices, zip code, telephone number)
Securities registered pursuant to Section 12(b) of the Act:

Title of Each Class	Name of Each Exchange on Which Registered
Common Stock, Par Value $0.001 per share	The NASDAQ Stock Market
Preferred Share Purchase Rights	The NASDAQ Stock Market

Securities registered pursuant to Section 12(g) of the Act:
None
(Title of Class)
Indicate by check mark if the registrant is a well-known seasoned issuer, as defined in Rule 405 of the Securities Act. Yes ¨ No þ

Indicate by check mark if the registrant is not required to file reports pursuant to Section 13 or Section 15(d) of the Act Yes ¨ No þ

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 ¨

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate website, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (§ 232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). Yes þ No ¨

Indicate by check mark if disclosure of delinquent filers pursuant to Item 405 of Regulation S-K is not contained herein, and will not be contained, to the best of the registrant's knowledge, in definitive proxy or information statements incorporated by reference in Part III of this Form 10-K or any amendment to this Form 10-K. þ

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

Large accelerated filer ¨ Accelerated filer þ Non-accelerated filer ¨ (Do not check if a smaller reporting company) Smaller reporting company ¨

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

The aggregate market value of the common stock held by non-affiliates of the registrant was $176 million on June 30, 2014, based on the closing price of the common stock on that date, as reported on the Nasdaq Global Select Market. Shares held by each executive officer and director have been excluded in that such persons may be deemed to be affiliates. In the case of 5% or greater shareholders, we have not deemed such shareholders to be affiliates unless there are facts and circumstances which would indicate that such shareholders exercise any control over our company, or unless they hold 10% or more of our outstanding common stock. This determination of affiliate status is not necessarily a conclusive determination for other purposes.

The number of shares of the registrant’s common stock outstanding as of January 30, 2015 was 36,102,915.

DOCUMENTS INCORPORATED BY REFERENCE

The registrant has incorporated by reference the information required by Part III of this Annual Report from its Proxy Statement relating to its 2015 Annual Meeting of Shareholders or an amendment to this Form 10-K, to be filed within 120 days after the end of its fiscal year ended December 31, 2014.

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PART I.

This Annual Report on Form 10-K 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-looking statements. All statements contained in this report that do not relate to matters of historical fact should be considered forward-looking statements. Forward-looking statements include statements with respect to:

- future revenues, operating expenses, income and other taxes, tax benefits, net income (loss) per diluted share available to common shareholders, acquisition costs and related amortization, and other measures of results of operations;
- the effects of our past acquisitions and expectations for future acquisitions and divestitures;
- plans, strategies and expected opportunities for future growth, increased profitability and innovation;
- the effects of our past strategic partnerships and joint ventures, and the prospects for creation and growth of strategic partnerships and the resulting financial benefits from such partnerships;
- the expected financial position, performance, growth and profitability of, and investment in, our businesses and the availability of resources;
- our involvement in potential claims, legal proceedings and government investigations, the expected course and costs of existing claims, legal proceedings and government investigations, and the potential outcomes and effects of both existing and potential claims, legal proceedings and governmental investigations on our business, prospects, financial condition or results of operations;
- the expected benefits and other consequences of our growth plans, strategic initiatives, and restructurings;
- our expected introduction and monetization of new and enhanced products, services and technologies across our businesses;
- expected challenges facing our legacy products;
- the effects of legislation, regulations, administrative proceedings, court rulings, settlement negotiations and other factors that may impact our businesses;
- the continuation and expected nature of certain customer relationships;
- impacts of competition and certain customer relationships on the future financial performance and growth of our businesses;
- the effects of U.S. and foreign income and other taxes on our business, prospects, financial condition or results of operations; and
- the effect of economic and market conditions on our business, prospects, financial condition or results of operations.

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 included or referred to in the section of Item 1 entitled "Competition," in Item 1A entitled "Risk Factors" and in Item 3 entitled "Legal Proceedings." 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.

Item 1. Business

Overview

RealNetworks creates innovative applications and services that make it easy to connect with and enjoy digital media. We invented the streaming media category in 1995 and continue to connect consumers with their digital media both directly and through partners, aiming to support every network, device, media type and social network. We provide the digital media services and products we create to consumers, mobile carriers and other businesses.

Consumers use our services and software to store, organize, play and manage their digital media content. Our consumer products and services include our video sharing and storage application, our casual and casino games, our direct-to-consumer ringback tone and productivity tool, and RealPlayer, our widely distributed media player. Network service providers, such as mobile carriers, use our products and services to create and deliver digital media and messaging services, such as ringback tones, music on demand and intercarrier messaging, for their subscribers.

We were incorporated in 1994 in the State of Washington. Our common stock is listed on The NASDAQ Stock Market under the symbol “RNWK.”

In this Annual Report on Form 10-K for the year ended December 31, 2014, RealNetworks, Inc., together with its subsidiaries, is referred to as “RealNetworks”, the “Company”, “we”, “us”, or “our”. "RealPlayer," and other trademarks of ou appearing in this report are our property.

Segments

We manage our business and report revenue and operating income (loss) in three segments: (1) RealPlayer Group, (2) Mobile Entertainment, and (3) Games. We allocate certain corporate expenses which are directly attributable to supporting the business, including but not limited to a portion of finance, legal, human resources and headquarters facilities, to our reportable segments rather than retaining those expenses in our corporate segment.

RealPlayer Group

Our RealPlayer Group business consists of our new video sharing and storage product, RealPlayer Cloud, which we released worldwide in the first half of 2014, and our RealPlayer media player software and related products and services. Our new RealPlayer Cloud product contributed an immaterial amount of revenue in 2014 , however, in line with our growth plan, we are focusing our investments in this segment on this new product.

Our RealPlayer media player software includes features and services that enable consumers to discover, play, download, manage and edit digital video, specifically, allowing them to stream audio and video, download and save photos and videos from the web, transfer and share content on social networks, and edit their own video content. Building on this business, our new RealPlayer Cloud product gives consumers even more options and control over their digital memories. With the RealPlayer Cloud product, consumers can find, watch, save and share their videos on multiple devices and across 13 different platforms.

In our RealPlayer segment, revenue has historically been derived from sales of the premium version of our media player, and from the distribution of third-party software products to consumers who wish to download additional applications when downloading our software products. We also generate revenue through our RealPlayer subscription products, including RealPlayer Cloud and our SuperPass service. RealPlayer Cloud, an integrated video player and cloud service, is free to consumers up to a certain storage level after which additional storage is available based on a tiered subscription fee. SuperPass is our subscription service that provides consumers with access to a broad range of digital entertainment content for a monthly fee.

In addition to consumer products, we also license our technology to a variety of mobile network operators worldwide to preinstall our mobile media player software on mobile phones.

Mobile Entertainment

Mobile Entertainment consists primarily of the digital media services we provide to network service providers as software as a service (SaaS) offerings. The large majority of revenues from this segment are in Asia and North America. During the fourth quarter of 2013, we launched LISTEN, our application that allows smartphone users to utilize ringback tones as a productivity tool.

Our SaaS services include ringback tones and messaging services principally sold to a large number of mobile carriers worldwide, and music on demand services principally sold in Korea. These SaaS services generated most of the revenue within our Mobile Entertainment segment in 2014, although most of our investment-related expenditures have been focused on

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LISTEN. In connection with our SaaS services, we also offer business intelligence, subscriber management and billing for our carrier customers.

Our ringback tone services enable callers to hear subscriber-selected music instead of the traditional electronic ringing sound while waiting for the person they have called to answer. We primarily offer ringback tone services via carriers, where, in return for providing, operating and managing the ringback tone service for the carrier customers, we generally enter into revenue-sharing arrangements with the carriers based on monthly subscription fees, content download fees or a combination of such fees paid by subscribers. Our interactive and highly customizable LISTEN product takes the ringback tone service to a new level, allowing the subscriber to utilize the app as more of a time management and productivity tool .

Our intercarrier messaging services are delivered through various carrier partners within the U.S. and internationally. The revenue we earn from our intercarrier messaging service is subject to a revenue-sharing arrangement with our carrier partners.

Our music on demand services, provided through our partner in Korea, offer a wide range of songs for downloading or streaming to PCs and mobile devices through various payment arrangements.

Games

We own and operate a large casual games service, offering casual games via digital downloads, online subscription play, third-party portals, social networks and mobile devices. Casual games typically have simple graphics, rules and controls and are quick to learn. Casual games include board, card, puzzle, word and hidden-object games.

We develop, publish, license and distribute casual games. We have a large and diverse portfolio of original games developed by our in-house game studios, games developed by us from content we license from other intellectual property holders, and games licensed to us by third parties that we distribute to our customers. We also partner with external game developers who develop games for us on an outsourced basis, which gives those developers access to our large distribution network in exchange for distribution rights to their games. We distribute games principally in North America, Europe and Latin America through our GameHouse, Zylom and Atrativa websites and through websites owned or managed by third parties.

Consumers can play and purchase games from our catalog of online and downloadable PC games. We typically introduce new games by offering a free trial before purchase on an individual basis or as part of one of our subscription services. In addition to revenue from sales of games and subscriptions, we generate revenue from display advertising that is shown to consumers during online play.

We also develop, monetize and optimize games and game play experiences on social networks. Building on our 2013 acquisition of Slingo, Inc., during the second half of 2014 we launched our latest game, Slingo Adventure, on Facebook and mobile platforms worldwide. We monetize social and mobile games largely through sales of games licenses, advertising and microtransactions from mobile and social games. We have also adapted our games for play on mobile handsets, smartphones and tablets, which can be purchased in app stores.

See Note 18, Segment Information, in this 10-K for additional details on our segments.

Rhapsody

At December 31, 2014, we owned approximately 43% of the issued and outstanding stock of Rhapsody. See Note 4, Rhapsody Joint Venture, in this 10-K for additional details. Rhapsody provides music products and services that enable consumers to have access to digital music content from a variety of devices. The Rhapsody unlimited subscription service offers unlimited access to a catalog of tens of millions of music tracks by way of on-demand streaming and conditional downloads. Rhapsody also operates a radio-like service, branded as "UnRadio" in the U.S., through which users can listen to online radio stations based on selected artists or genres and download favorite tracks played on those stations for offline playback. Rhapsody currently offers music services in 32 different territories (under the Rhapsody or Napster brands) and generates revenue primarily through subscriptions to its music services either directly to consumers or through distribution partners, such as mobile carriers.

Customers and Seasonality

Our customers include consumers and businesses located throughout the world. Sales to customers outside the U.S., primarily in Asia and Europe, were 61%, 56% and 54% of our revenue during the years ended December 31, 2014, 2013 and 2012, respectively. See Note 18, Segment Information for details on geographic concentrations and see Note 6, Allowance for Doubtful Accounts Receivable and Sales Returns, for details on customer revenue concentrations.

We experience seasonality in our business, particularly with respect to the fourth quarter of our fiscal year. Our consumer businesses, which include advertising revenue, make up a large percentage of our revenue, and the fourth quarter has traditionally been the seasonally strongest quarter for Internet advertising.

Research and Development

We devote a substantial portion of our resources to developing new products, enhancing existing products, expanding and improving our fundamental technology, and strengthening our technological expertise in all our businesses. During the years ended December 31, 2014, 2013, and 2012, we expended 34%, 30% and 24%, respectively, of our revenue on research and development activities.

Sales, Marketing and Distribution

Our marketing programs are aimed at increasing brand awareness of our products and services and stimulating demand. We use a variety of methods to market our products and services, including paid search advertising, affiliate marketing programs, advertising in print, electronic and other online media, direct mail and email offers to qualified potential and existing customers, and providing product specific information through our websites. We also cross-market products and services offered by some of our businesses through the RealPlayer and Games marketing and distribution channels. We also have subsidiaries and offices in several countries that market and sell our products outside the U.S.

Our products and services are marketed through direct and indirect channels. We use public relations, trade shows, events and speaking opportunities to market our products and services. We also use a variety of online channels, including social media, to promote and sell our products and services directly.

We market and sell our RealPlayer services directly through our own websites such as Real.com, as well as indirectly through affiliate partnerships.

Our Mobile Entertainment sales, marketing and business development team works closely with many of our enterprise, infrastructure, wireless, broadband and media customers to identify new business opportunities for our entertainment applications, services and systems. Through ongoing communications with the product and marketing divisions of our customers, we tailor our SaaS offerings to their strategic needs and the needs of their subscribers.

Our games are marketed directly from our websites and through third-party distribution channels, such as search engines, online portals, mobile phone application stores, major social networks and content publishers.

Customer Support

Customer support is integral to the provision of nearly all of our consumer products and services. Consumers who purchase and use our consumer software products and services can get assistance via the Internet, email or telephone, depending on the product or service. For most of our consumer products, we contract with third-party outsource support vendors to provide the primary staffing for our first-tier customer support globally. We also provide various support service options for our business customers and for software developers using our software products and associated services. Support service options include hotline telephone support, online support services, and on-site support personnel covering technical and business-related support topics.

Competition

The market for software and services for digital media delivery over the Internet and wireless networks is intensely competitive. Many of our current and potential competitors have longer operating histories, greater name recognition or brand awareness, more employees or significantly greater resources than we do.

Our RealPlayer Cloud product faces significant competition from cloud storage providers, including several large, well-resourced companies, as well as video sharing services, which include both well known, firmly established companies and entrepreneurial, nimble startups. In addition, as we continue to develop this product and expand its reach, we expect to see growing competition from companies offering innovative features for engaging with users' video content. Our RealPlayer media player continues to face competition from alternative streaming media playback technologies which have obtained very broad market penetration.

In our Mobile Entertainment segment, our SaaS business competes with a large and diverse number of domestic and international companies, and each of our SaaS offerings tends to face competitors specific to that product or service. Our SaaS business continues to experience significant competitive pricing pressure from carriers and the proliferation of smartphone applications and services, some of which do not depend on our carrier customers for distribution to consumers. Many of our SaaS services require a high degree of integration with carrier or service provider networks and thus require a high degree of operational expertise. In addition, our ability to enhance services with new features as the digital entertainment market evolves is critical to our competitive position, as is our knowledge of the consumer environment to which these services are targeted.

Our Games business competes with a variety of distributors, publishers and developers of casual games for PC and mobile platforms and for social networks. We compete in this market primarily on the basis of the quality and convenience of our services, the reach and quality of our distribution and the quality and breadth of our game catalog. In addition, the market for casual games has become increasingly price competitive in recent years. Our in-house content development studios compete with other developers and publishers of social and mobile games based on our ability to develop and publish high quality games that resonate with consumers, our effectiveness at building our brands, and our ability to secure broad distribution relationships with major social networks and mobile carriers. Our social and mobile games compete with a range of developers. Our family of websites serving the PC casual games market competes with other high volume distribution channels for downloadable, online and social games.

Intellectual Property

As of December 31, 2014, we had seven U.S. patents, 43 South Korean patents, 13 patents in other countries and more than 30 pending patent applications worldwide relating to various aspects of our technology. In 2012, we completed the sale of certain patents, patent applications and related rights held by us, and certain of our assets relating to our next generation video codec technologies to Intel. We regularly analyze our patent portfolio and prepare additional patent applications on current and anticipated features of our technology in various jurisdictions across the world.

In addition to our patent portfolio, we have assembled, over time, an international portfolio of trademarks and service marks that covers certain of our products and services. We also have applications pending for additional trademarks and service marks in jurisdictions around the world, and have several unregistered trademarks. Many of our marks begin with the word “Real” (such as RealPlayer). We are aware of other companies that use “Real” in their marks alone or in combination with other words, and we do not expect to be able to prevent all third-party uses of the word “Real” for all goods and services.

Our ability to compete across our businesses partly depends on the superiority, uniqueness and value of the technology that we both develop and license 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. These efforts to protect our intellectual property rights may not be effective in preventing misappropriation of our technology, or may not prevent the development and design by others of products or technologies similar to or competitive with those we develop.

Employees

At December 31, 2014, we had approximately 769 employees, of which 359 were based in the Americas, 251 were based in Asia, and 159 were based in Europe. None of our employees are subject to a collective bargaining agreement.

Position on Charitable Responsibility

In periods when we have achieved sustained profitability, we intend to donate 5% of our net income to charitable organizations, which will reduce our net income for those periods. The non-profit RealNetworks Foundation, established in 2001, manages a substantial portion of our charitable giving efforts. Through the Foundation, we support our employees' philanthropic efforts by matching their donations of time and money to charitable organizations.

Available Information

Our corporate Internet address is www.realnetworks.com. We make available free of charge on www.investor.realnetworks.com our annual reports on Form 10-K, quarterly reports on Form 10-Q and current reports on Form 8-K, and amendments to these reports, as soon as reasonably practicable after we electronically file such material with, or furnish it to, the Securities and Exchange Commission (SEC). However, the information found on our corporate website is not part of this or any other report.

Item 1A. Risk Factors

You should carefully consider the risks described below together with all of the other information included in this annual report on Form 10-K. The risks and uncertainties described below are not the only ones facing our company. Additional risks and uncertainties not presently known to us or that we presently deem less significant may also impair our business operations. If any of the following risks actually occurs, our business, financial condition or operating results, and the trading price of our common stock, could be materially harmed.

Our business and financial results will be materially adversely impacted if we are unable to successfully implement our growth plan, strategic initiatives, and restructuring efforts.

Beginning in mid-2012, we have developed a growth plan that involves the launch of at least one major new product in each of our three business units. In tandem with our growth plan, we have embarked upon strategic initiatives intended to simplify and accelerate our operations, and restructuring efforts intended to streamline costs and bring more focus to our businesses. The simultaneous execution of all of these measures is ambitious and we have not attempted to pursue this level of transition in our history. We can provide no assurance that we will be successful in implementing our growth plan, strategic initiatives, and restructuring efforts, either in a timely manner or at all, and our failure to do so would have a material adverse impact on our business and financial results.

We need to successfully introduce and monetize new products and services to sustain and grow our businesses.

In order to sustain our current level of business and to implement our growth plan, we must successfully introduce and monetize new products and services. The process of developing new, and enhancing existing, products and services is complex, costly and uncertain, and is subject to a number of risks. Providing products and services that are attractive and useful to subscribers and consumers is in part subject to unpredictable and volatile factors beyond our control, including end-user preferences and competing products and services. Any failure by us to timely respond to or accurately anticipate consumers' changing needs, emerging technological trends or important changes in the market or competition for products and services that we introduce, or that we plan to introduce, could increase the current rate of decline in our 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 the products and services that we are developing will meet the needs of a large enough group of consumers, which may result in no return or a loss on our investments.

During 2013 and 2014, each of our businesses introduced at least one new product or service. In early 2014, our RealPlayer business completed the global launch of RealPlayer Cloud, our integrated video player and cloud service. In November 2013, our Mobile Entertainment business completed its European launch of LISTEN, an application and service for smartphone users featuring ringback tones and other services. LISTEN was launched with T-Mobile in the U.S. in April 2014. In August 2013, our Games business launched GameHouse Casino Plus with the Golden Dreams Sweepstakes feature and, in September 2014, launched Slingo Adventure. To date, we have not generated significant revenue from any of these new products and services. Over the past several quarters, we have invested heavily in the development of these and other new products and enhanced features for such products, and we expect to continue to invest heavily both in further development and in sales and marketing efforts aimed at monetizing these products and services. These investments have and are expected to continue to have a significant negative impact on our cash position and there can be no assurance that our efforts will generate any meaningful revenue. If we are unable to generate sustained interest in these products and services, and therefore drive revenue growth, our financial results will be materially negatively impacted.

Furthermore, new products and services may be subject to legal challenge. Responding to any such 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, any of which could materially harm our operating results and our ability to grow our businesses.

Our legacy products and services face new and continuing challenges, causing our revenues to materially decline.

As we increasingly focus our development and sales and marketing efforts on our newly launched products and services, sales of our legacy products and services have suffered and will continue to suffer. For instance, while the efforts of our RealPlayer team are targeted increasingly towards enhanced development and monetization of our new RealPlayer Cloud product, we have significantly reduced our marketing of SuperPass and have redirected our development resources away from RealPlayer Plus, both of which have resulted in declines in the number of subscribers of those legacy products.

Our legacy products and services also face continuing market challenges, including the rapid move to smartphones and tablets, and the introduction of new operating systems. We have historically distributed our legacy products and services through desktop computers and feature phones, but the number of people who access similar products and services through smartphones and tablets has increased dramatically in the past several years. There are many challenges involved in developing and marketing products and services for users of smartphones and tablets, and there is no guarantee that we will be able to transition or effectively monetize our legacy products and services to these devices. In addition, our consumer-based products and services have historically been distributed through desktop operating platforms. As new operating systems are introduced or updated for these platforms, we are likely to continue to face difficulties reaching our traditional customer base and other unknown distribution challenges. If we continue to have difficulty transitioning our legacy products and services for use on new devices or updated operating systems, then our revenues will continue to decline and our business could be significantly harmed.

Our restructuring efforts may not yield the anticipated benefits to our shareholders.

Since 2012, we have taken steps to restructure and simplify our business and operations. In September 2012, we announced plans to divisionalize our business, which we implemented during the first quarter of 2013, and to significantly reduce operating expenses, in part through a reduction in our workforce that was substantially concluded by the end of the second quarter of 2013. In August 2014, we announced a further reduction in our workforce and related cost reductions. We continue to assess opportunities to further streamline our operations and make our businesses more efficient. There can be no assurance, however, that our past or future restructuring efforts will be successful. 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 for our businesses. Our restructuring activities have included implementing cost-cutting initiatives, which may not lead to future profitability and which could materially impact our ability to compete in future periods. If we are unable to effectively re-align the cost structure of our businesses or streamline and simplify our operations, our stock price may continue to be adversely affected, and we and our shareholders will not realize the anticipated financial, operational and other benefits from such initiatives.

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

Many of our current and potential competitors in our businesses have longer operating histories, greater name recognition, more employees and significantly greater resources than we do. To effectively compete in the markets for our products and services, 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,
- loss of current and potential customers, or partners and potential partners who provide content we distribute to our customers,
- changes to our products, services, technologies, licenses or business practices or strategies,
- lengthened sales cycles,
- industry-wide changes in content distribution to customers or in trends in consumer consumption of digital media products and services,
- pressure to prematurely release products or product enhancements, or
- degradation in our stature or reputation in the market.

The market for mobile entertainment services, including our ringback tones and music on demand solutions, is highly competitive and evolving rapidly, particularly with the growth in the use of smartphones. Increased use of smartphones has resulted in a proliferation of applications and services that compete with our SaaS services and, in many cases, are not dependent upon our carrier customers to make them available to subscribers. Increased competition has in the past resulted in pricing pressure, forcing us to lower the selling price of our services. We expect this pricing pressure to continue to materially harm our operating results and financial condition.

Our recently launched RealPlayer Cloud product faces competition from other cloud service providers, including some that are firmly established in the marketplace and have access to extensive resources, as well as video sharing services, which include both well known and established companies and entrepreneurial startups. In addition, as we continue to develop this product and expand its reach, we expect to see growing competition from companies offering innovative features for engaging with users' video content. Our RealPlayer software services compete with alternative streaming media playback technologies and audio and video formats which have obtained very broad market penetration. If we are unable to compete successfully, most notably through the development, marketing and monetization of RealPlayer Cloud, our RealPlayer business could continue to decline.

The branded services in our Games business compete with other online aggregators and distributors of online, downloadable and social 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 that may be able to adjust to market conditions, including responding effectively to the growing popularity of casual games on social networks, faster than us. We also face significant price competition in the casual games market, and some of our competitors may be able to lower prices more aggressively than us. We expect competition to continue to intensify in this market from these and other competitors. Our games development studios compete primarily with other developers of online, downloadable, mobile and social casual PC games and must continue to develop popular and high-quality game titles. Our Games business must also continue to execute on opportunities to expand the play of our games on a variety of non-PC platforms, including social networks, in order to maintain our competitive position and to grow the business. If we are unable to slow recent revenue declines or achieve future growth in our revenue, particularly as we continue to invest in social and mobile games as the market for these games continues to rapidly evolve, revenue in our Games business will continue to decline and the business will suffer.

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 the SaaS offerings we provide to carriers. Many of our SaaS contracts with carriers 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 mobile carrier customers could purchase similar 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, some of our SaaS contracts require us to incur significant set-up costs prior to the launch of services with a carrier customer. For example, in the fourth quarter of 2011, we reduced our forecast for profitability associated with certain carrier customer contracts for which the total costs exceeded the total revenue we expect to recognize from these contracts, and as a result, we recorded impairment of deferred costs totaling $20.0 million. We may be required to record additional impairments or other charges in future periods related to our carrier customer contracts, which would negatively impact our results of operations.

In addition, none of our SaaS contracts with carriers obligates our carrier customers to market or distribute any of our SaaS offerings. Despite the lack of marketing commitments, revenue related to our SaaS offerings 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 SaaS offerings, or the termination, non-renewal or renegotiation of contract terms that are less favorable to us would result in the loss of future revenues from our SaaS offerings.

Finally, nearly all 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. Pursuant to these indemnifications obligations, we have in the past agreed to control the defense on behalf of certain of our carrier customers related to patent infringement proceedings. In 2013, we settled two such litigation matters. Future claims against which we may be obligated to defend our carrier customers could result in payments that could materially harm our business or our consolidated financial statements.

A majority of the revenue that we generate in our Mobile Entertainment business segment is dependent upon our relationships with a few customers, and any deterioration of these relationships could materially harm our revenue.

We generate a significant portion of our revenue from sales of our mobile entertainment services to a few of our mobile carrier customers, including SK Telecom, a leading wireless carrier in South Korea, and its affiliates. In the near term, we expect that we will continue to generate a significant portion of our total revenue from these customers. If these customers fail to market or distribute our services or terminate or fail to renew their business contracts with us, or if our relationships with these customers deteriorate in any significant way, we may be unable to replace the affected business arrangements with acceptable alternatives. Failure to maintain our relationships with these customers could have a material negative impact on our revenue.

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

Maintaining and growing the distribution of digital media products through our websites and our other distribution channels has historically been important to our business, including growth through the introduction of new products and services distributed through these channels. It is unlikely that consumers will continue to download and use our digital media products consistent with past usage, so we expect that our ability to generate revenue from those products will be continue to be reduced, which could lead to lower than expected adoption of newly introduced products and services. Our inability to maintain continued high volume distribution of our digital media products could also 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. Our revenue from the distribution of third-party products will also be negatively impacted if those products are not widely downloaded by consumers, including due to the relative market saturation of such products. Most of our revenue from the distribution of third-party products was historically derived from a single customer, however, that relationship ended during the third quarter of 2014, and we entered into an agreement with a new distribution partner. Our distribution revenue has been, and we expect will continue to be, materially negatively impacted by these factors.

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

The trading price for our common stock has a history of volatility. Although our recent stock price history shows more stability, with a range from $6.00 to $8.38 per share during the 52-week period ended December 31, 2014 it also shows continued weakness. As a result of the rapidly changing markets in which we compete, our operating results may fluctuate from period to period, which may contribute to volatility of our stock price.

In past periods, our operating results have been affected by personnel reductions and related restructuring charges, lease exit and related charges, and impairment charges for certain of our equity investments, goodwill and other long-lived assets. In addition to these factors, the general difficulty in forecasting our operating results and metrics could result in actual results that differ significantly from expected results, causing volatility and continued weakness in our stock price.

Certain of our product and service investment 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 fluctuate. Weakness in our operating performance is likely to cause continued weakness in our stock price.

Any impairment to our goodwill, indefinite-lived intangible assets and definite-lived assets could result in a significant charge to our earnings.

In accordance with accounting principles generally accepted in the United States, we are required to test goodwill and indefinite-lived intangible assets for possible impairment on an annual basis based upon a fair value approach, or more frequently in the event of certain indications of possible impairment. We review definite-lived assets for impairment whenever events or changes in circumstances indicate the carrying amount of such assets may not be recoverable. These events or circumstances could include a significant change in the business climate, including a significant sustained decline in a reporting unit’s market value, legal factors, operating performance indicators, competition, sale or disposition of a significant portion of our business, a significant sustained decline in our market capitalization and other factors. If we were to determine that an impairment had occurred, we would be required to record an impairment charge, which could have a significant negative, and unpredicted, impact on our financial results. The total carrying value of our goodwill, indefinite-lived intangible assets and definite-lived assets as of December 31, 2014 was $44 million.

Continued loss of revenue from our subscription services may continue to harm our operating results.

Our operating results have been and could continue to be adversely impacted by the loss of subscription revenue related to our legacy services and by the failure to generate revenue related to our new services. 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 with competitive service offerings, or because customer service issues are not satisfactorily resolved. Revenue from our SuperPass subscription service, for example, has declined in recent periods due to changes in consumer preferences and changes on our part to focus on other products and services we offer, and we expect these trends to continue. For the subscription services we offer, we must continue to obtain compelling digital media content for our video and games services in order to maintain and increase usage and overall customer satisfaction for these products. Our operating results may be negatively impacted if we cannot obtain content for our subscription services on commercially reasonable terms.

Government regulation of the Internet is evolving, and unfavorable developments could have an adverse effect on our operating results.

We are subject to regulations and laws specific to the marketing, sale and delivery of goods and services over the Internet. These laws and regulations, which continue to evolve, cover taxation, user privacy, data collection and protection, copyrights, electronic contracts, sales procedures, automatic subscription renewals, credit card processing procedures, consumer protections, digital games distribution, broadband Internet access and content restrictions. We cannot guarantee that we have been or will be fully compliant in every jurisdiction, as it is not entirely clear how existing laws and regulations governing issues such as privacy, taxation and consumer protection apply or will be enforced with respect to the products and services we sell through the Internet. Moreover, as Internet commerce continues to evolve, increasing regulation and/or enforcement efforts by federal, state and foreign agencies and the prospects for private litigation claims related to our data collection, privacy policies or other e-commerce practices become more likely. In addition, the adoption of any laws or regulations or the imposition of other legal requirements that adversely affect our ability to market, sell, and deliver our products and services could decrease our ability to offer or customer demand for our service offerings, resulting in lower revenue. Future regulations, or changes in laws and regulations or their existing interpretations or applications, could also require us to change our business practices, raise compliance costs or other costs of doing business and result in additional historical or future liabilities for us, resulting in adverse impacts on our business and our operating results.

As a consumer-facing business, we receive complaints from our customers regarding our consumer marketing efforts and our customer service practices. Some of these customers may also complain to government agencies, and from time to time, those agencies have made inquiries to us about these practices. In addition, we may receive complaints or inquiries directly from governmental agencies that have not been prompted by consumers. In May of 2012, we resolved an investigation and complaint filed against us by the Washington State Office of the Attorney General, or Washington AG, relating to our consumer marketing practices through the entry of a consent decree filed in King County, Washington Superior Court. While we resolved that matter, we cannot provide assurance that the Washington AG or other governmental agencies will not bring future claims regarding our marketing, or consumer services or other practices.

Global and national economic conditions have in the past and could in the future have a material adverse impact on our business, financial condition and results of operations.

Our business and operations depend significantly on global and national economic conditions. Because consumers may consider the purchase of our digital entertainment products and services to be a discretionary expenditure, their decision whether to purchase our products and services may be influenced by macroeconomic factors that affect consumer spending such as unemployment, access to credit, negative financial news, and declines in income. In addition, our carrier customers and business partners may reduce their business or advertising spending with us in the face of adverse macroeconomic conditions, such as financial market volatility, government austerity programs, tight credit, and declines in asset values.. We have in the past recorded material asset impairment charges due in part to weakness in the global economy, and we may need to record additional impairments to our assets in future periods in the event of renewed weakness and uncertainty in the global or national economy. Accordingly, any significant weakness in the national and/or global economy could materially impact our business, financial condition and results of operations in a negative manner.

Rhapsody could continue to recognize losses, which would negatively impact our results of operations and financial condition.

On March 31, 2010, we completed the restructuring of our digital audio music service joint venture, Rhapsody America LLC. As a result of the restructuring, we no longer have operational control over Rhapsody and Rhapsody’s operating performance is no longer consolidated with our consolidated financial statements. Rhapsody has generated accounting losses since its inception and we have recognized losses on our investment in the convertible preferred stock of Rhapsody since the restructuring. If Rhapsody continues to incur losses, or if it otherwise experiences a significant decline in its business, we may incur further losses on our investment, which could have an adverse effect on our financial condition and results of operations. See Note 4, Rhapsody Joint Venture, for details on the liquidation preference on our convertible preferred investment.

Given the current proportion of the outstanding equity of Rhapsody that we hold, we need to receive Rhapsody’s unaudited quarterly financial statements and related information in order to timely prepare our quarterly consolidated financial statements and also to report certain of Rhapsody’s financial results, as may be required, in our quarterly reports on Form 10-Q. In addition, we may be required to include Rhapsody’s annual audited financial statements in our annual report on Form 10-K in future periods. As we no longer exert operational control over Rhapsody, we cannot guarantee that Rhapsody will deliver its financial statements and related information to us in a timely manner, or at all, or that the unaudited financial statement information provided by Rhapsody will not contain inaccuracies that are material to our reported results. Any failure to timely obtain Rhapsody’s quarterly financial statements or to include its audited financial statements in our future annual reports on Form 10-K, if required, could cause our reports to be filed in an untimely manner, which would preclude us from utilizing certain registration statements and could negatively impact our stock price.

The loss of key personnel, or difficulty recruiting and retaining them, could significantly harm our business or jeopardize our ability to meet our growth objectives.

Our success depends substantially on the contributions and abilities of certain key executives and employees. We have experienced a significant amount of executive-level turnover in the past several years, which has had and could continue to have a negative impact on our ability to retain key employees. Rob Glaser, our founder, Chairman and initial chief executive officer, resigned as chief executive officer in 2010, was appointed as interim chief executive officer in July 2012, and was named permanent chief executive officer in July 2014. In addition, each member of our executive team is either new to RealNetworks or new to his or her executive position. We cannot provide assurance that we will effectively manage these executive-level transitions, which may impact our ability to retain key executives and employees and which could harm our business and operations to the extent there is customer or employee uncertainty arising from such transitions.

Our success is also substantially dependent upon our ability to identify, attract and retain highly skilled management, technical and sales personnel. Qualified individuals are in high demand and competition for such qualified personnel in our industry, particularly engineering talent, is intense, and we may incur significant costs to attract or retain them. Our ability to attract and retain personnel may also be made more difficult by the uncertainty created by our recent executive-level turnover and by our continued restructuring efforts, which have involved reductions in our workforce. 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 and divestitures involve costs and risks that could harm our business and impair our ability to realize potential benefits from these transactions.

As part of our business strategy, we have acquired and sold technologies and businesses in the past and expect that we will continue to do so in the future. The failure to adequately manage transaction costs and address the financial, legal and operational risks raised by acquisitions and divestitures of technology and businesses could harm our business and prevent us from realizing the benefits of these transactions. In addition, we may identify and acquire target companies, but those companies may not be complementary to our current operations and may not leverage our existing infrastructure or operational experience, which may increase the risks associated with completing acquisitions.

Transaction-related costs and financial risks related to completed and potential future purchase or sale transactions may harm our financial position, reported operating results, or stock price. Previous acquisitions have resulted in significant expenses, including amortization of purchased technology, amortization of acquired identifiable intangible assets and the incurrence of charges for the impairment of goodwill and other intangible assets, which are reflected in our operating expenses. New acquisitions and any potential additional future impairment of the value of purchased assets, including goodwill, could have a significant negative impact on our future operating results. For example, in 2013 we acquired Slingo, Inc. pursuant to which we recorded $8.0 million of intangible assets and $9.9 million in goodwill, and Muzicall Limited pursuant to which we recorded $5.4 million of intangible assets and $1.3 million in goodwill. In compliance with accounting principles generally accepted in the United States, we evaluate these assets for impairment at least annually. Factors that may be considered a change in circumstances, indicating that our goodwill, indefinite-lived intangible assets or definite-lived assets may not be recoverable, include reduced future revenue and cash flow estimates due to changes in our forecasts, and unfavorable changes to valuation multiples and discount rates due to changes in the market. If we were to conclude that any of these assets were impaired, we would have to recognize an impairment charge that could significantly impact our financial results.

Purchase and sale transactions also involve operational risks that could harm our existing operations or prevent realization of anticipated benefits from a transaction. 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, managing and integrating acquired businesses in remote locations or in countries in which we have little or no prior experience;
- diversion of management time and other resources from existing operations;
- 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 may be unable to adequately protect our proprietary rights or leverage our technology assets, and may face risks associated with third-party claims relating to intellectual property rights associated with our products and services.

Our ability to compete across our businesses partly depends on the superiority, uniqueness and value of our technology, including both internally developed technology and technology licensed from third parties. To protect our proprietary rights, we rely on a combination of patent, trademark, copyright and trade secret laws, confidentiality agreements with our employees and third parties, and protective contractual provisions. 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. We also routinely receive challenges to our trademarks and other proprietary intellectual property that we are using in our business activities in China. 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. While we sold to Intel Corporation in 2012 most of our patents, including patents that covered streaming media, we agreed to indemnify Intel for certain third-party infringement claims against these patents up to the purchase price we received in the sale. We may also 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 contract breaches, infringement of copyrights, trademark rights, trade secret rights or other proprietary rights, or alleging unfair competition or violations of privacy rights. These claims, even if not meritorious, could force us to spend significant financial and managerial resources. Given the broad distribution of some of our consumer products, any individual claim related to those products could give rise to liabilities that may be material to us. For example, in July 2012, VoiceAge Corporation brought a lawsuit against us alleging breach of our obligation to pay them licensing fees under our patent license agreement with VoiceAge and seeking a material amount in damages. While we settled the dispute with VoiceAge in the fourth quarter of 2013, similar future lawsuits could result in significant legal expenses, monetary damages, penalties or injunctive relief against us that could have a material adverse impact on our future consolidated financial statements. In addition, in 2012 we sold substantially all of our patent assets to Intel. We believe that our patent portfolio may have in the past discouraged third parties from bringing infringement or other claims against us relating to the use of our technologies in our business. Accordingly, we cannot predict whether the sale of these patent assets to Intel will result in additional infringement or other claims against us from third parties.

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 and security of our information systems and networks. A significant or repeated reduction in the performance, reliability, security 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 due to its geographic concentration 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.

The growth of our business is dependent in part on successfully managing our international operations.

Our international operations involve risks inherent in doing business globally, including difficulties in managing operations due to distance, language, and cultural differences, local economic conditions, different or conflicting laws and regulations, taxes, and exchange rate fluctuations. The functional currency of our foreign subsidiaries is the local currency of the country in which each subsidiary operates. We translate our subsidiaries' revenues into U.S. dollars in our financial statements, and continued volatility in foreign exchange rates, particularly if the U.S. dollar strengthens against the euro or the Korean won, may result in lower reported revenue or net assets in future periods. Our foreign currency exchange risk management program reduces, but does not eliminate, the impact of currency exchange rate movements. If we do not effectively manage any of the risks inherent in running our international businesses, our operating results and financial condition could be harmed.

We may be subject to market risk and legal liability in connection with our data collection and data security capabilities.

Many of our products are interactive Internet applications that by their very nature require communication between a client and server to operate. For example, to provide better consumer experiences and to operate effectively, our products send information, including personally identifiable information, to our servers or servers hosted by third parties. In addition, we sell many of our products and services through online sales transactions directly with consumers, through which we collect and store credit card information. In connection with our direct sales to consumers, we may be the victim of fraudulent transactions, including credit card fraud, which presents a risk to our revenue and potentially disrupts service to our consumers. While we take measures to protect our consumer data, we have experienced unauthorized access to our consumer data in the past, and it is possible that our security controls over consumer data may not prevent future improper access or disclosure of credit card information or personally identifiable information. We have an extensive privacy policy concerning the collection, use and disclosure of user data involved in interactions between our client and server products. A security breach that leads to disclosure of consumer account information (including personally identifiable information) or any failure by us to comply with our posted privacy policy or existing or new legislation regarding privacy issues could harm our reputation, impact the market for our products and services, subject us to litigation, and require us to expend significant resources to mitigate the breach of security, comply with breach notification laws or address related matters. In addition, we need to maintain compliance with standards of the Payment Card Industry, or PCI, for data security in connection with our use of credit card services for payment.

If we fail to maintain the PCI compliance standards we may be subject to substantial monetary penalties and we could lose the ability to accept credit card payments for transactions with our customers. Any of these consequences could materially harm our business or our consolidated financial statements.

Changes in regulations applicable to the Internet and e-commerce that increase the taxes on the services we provide could materially harm our business and operating results.

As Internet commerce continues to evolve, increasing taxation by state, local or foreign tax authorities becomes more likely. For example, taxation of electronically delivered products and services or other charges imposed by government agencies may also be imposed. We believe we collect transactional taxes and are compliant and current in all jurisdictions where we believe we have a collection obligation for transaction taxes. Any regulation imposing greater taxes or other fees for products and services could result in a decline in the sale of products and services and the viability of those products and services, harming our business and operating results. A successful assertion by one or more states or foreign tax authorities that we should collect and remit sales or other taxes on the sale of our products or services could result in substantial liability for past sales.

In those countries where we have a tax obligation, we collect and remit value added tax, or VAT, on sales of “electronically supplied services” provided to European Union residents. 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.

Our Chairman of the Board and Chief Executive Officer beneficially owns approximately 36% of our stock, which gives him significant control over certain major decisions on which our shareholders may vote or may discourage an acquisition of us.

Robert Glaser, our Chairman of the Board and Chief Executive Officer, beneficially owns approximately 36% of our common stock. As a result, Mr. Glaser and his affiliates 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.

The stock ownership of Mr. Glaser and his affiliates 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 transactions 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.

Mr. Glaser has special rights under our articles of incorporation to appoint or remove members of the strategic transactions 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. These rights and his role as Chairman of the Board of Directors, together with Mr. Glaser’s

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significant beneficial ownership, create unique potential for concentrated influence of Mr. Glaser over potentially material transactions involving RealNetworks and decisions regarding the future strategy and leadership of RealNetworks.

We have adopted a shareholder rights plan, which was amended and restated in December 2008, which 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, 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 1B. Unresolved Staff Comments

None.

Item 2. Properties

Our corporate and administrative headquarters and certain research and development and sales and marketing personnel are located at our facility in Seattle, Washington.

We lease properties primarily in the following locations that are utilized by all of our business segments, unless otherwise noted below, to house our research and development, sales and marketing, and general and administrative personnel:

Location	Area leased (sq. feet)	Lease expiration
Seattle, Washington	86,000	August 2024, with an option to renew for two five-year periods
Seoul, Republic of Korea (1)	30,000	October 2015

(1) This facility is utilized only by our Mobile Entertainment segment.

In addition, we lease smaller facilities in the U.S. and foreign countries, some of which support the operations of all of our business segments while others are dedicated to a specific business segment. We believe that our properties are in good condition, adequately maintained and suitable for the conduct of our business. For additional information regarding our obligations under leases, see Note 16, Commitments and Contingencies, in this 10-K.

Item 3. Legal Proceedings

See Note 16, Commitments and Contingencies, in this 10-K.

Item 4. Mine Safety Disclosures

Not applicable.

PART II.

Item 5. Market for Registrant’s Common Equity, Related Shareholder Matters and Issuer Purchases of Equity Securities

Our common stock is traded on The NASDAQ Stock Market under the symbol RNWK.

The high and low intraday sales prices for our common stock were as follows:

	Years Ended December 31,			
	2014		2013	
	High	Low	High	Low
First Quarter	$8.00	$6.83	$8.01	$7.13
Second Quarter	8.09	7.03	7.82	7.16
Third Quarter	8.38	6.91	8.70	6.87
Fourth Quarter	7.45	6.00	8.95	7.09

As of January 30, 2015, there were approximately 160 holders of record of our common stock. Most shares of our common stock are held by brokers and other institutions on behalf of shareholders.

In 2011 we paid a special cash dividend of $1.00 per common share to the holders of our common stock. However, the declaration and payment of any future dividends, as well as the amount thereof, are subject to the discretion of our board of directors and will depend upon our results of operations, financial condition, capital levels, cash requirements, future prospects and other factors deemed relevant by our board of directors. Accordingly, there can be no assurance that we will declare and pay any dividends in the future.

Comparison of 5 year cumulative total return to shareholders on RealNetworks, Inc., common stock with the cumulative total return on the NASDAQ Composite Index and the Dow Jones U.S. Technology Index for the period beginning on December 31, 2009 and ended on December 31, 2014.

The total return on our common stock and each index assumes the value of each investment was $100 on December 31, 2009, and that all dividends were reinvested. Return information is historical and not necessarily indicative of future performance.

Item 6. Selected Financial Data

The following selected consolidated financial data should be read in conjunction with "Management's Discussion and Analysis of Financial Condition and Results of Operations" and the Consolidated Financial Statements and Notes to Consolidated Financial Statements included elsewhere in this report.

	Years Ended December 31,				
	2014	2013	2012	2011	2010
	(In thousands, except per share data)				
Consolidated Statements of Operations Data:					
Net revenue	$156,212	$206,196	$258,842	$335,686	$401,733
Cost of revenue	76,381	79,091	103,731	126,637	144,723
Extinguishment of liability	(10,580)	—	—	—	—
Impairment of deferred costs	—	—	—	19,962	—
Gross profit	90,411	127,105	155,111	189,087	257,010
Sale of patents and other technology assets, net of costs	—	—	116,353	—	—
Operating expenses:					
Research and development	52,765	60,880	63,194	70,212	100,955
Sales and marketing	66,926	80,011	90,301	111,300	118,543
Advertising with related party	—	—	—	—	1,065
General and administrative	34,001	36,643	43,891	37,181	51,217
Restructuring and other charges	4,992	5,765	15,225	8,650	12,361
Lease exit and related charges (gains)	880	3,089	3,290	(646)	7,396
Loss on litigation settlements	—	11,525	—	—	—
Total operating expenses	159,564	197,913	215,901	226,697	291,537
Operating income (loss)	(69,153)	(70,808)	55,563	(37,610)	(34,527)
Other income (expense), net (A)	(1,382)	16,721	1,796	(6,819)	204
Income (loss) before income taxes	(70,535)	(54,087)	57,359	(44,429)	(34,323)
Income tax expense (benefit)	1,280	4,903	12,518	(17,329)	(36,451)
Net income (loss)	(71,815)	(58,990)	44,841	(27,100)	2,128
Net loss attributable to the noncontrolling interest in Rhapsody	—	—	—	—	2,910
Net income (loss) attributable to common shareholders	$(71,815)	$(58,990)	$44,841	$(27,100)	$5,038
Diluted net income (loss) per share attributable to common shareholders	$(2.00)	$(1.66)	$1.28	$(0.79)	$0.26
Shares used to compute diluted net income (loss) per share	35,947	35,553	35,122	34,185	34,013
Special cash dividend of $1.00 per common share	—	—	—	$136,793	—

(A) Includes a $21.4 million pretax gain from the sale of equity securities in 2013. See Note 5, Fair Value Measurements, in this 10-K for more details.

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	As of December 31, 2014	2013	2012	2011	2010
	(In thousands)				
Consolidated Balance Sheets Data:					
Cash, cash equivalents, and short-term investments	$161,706	$226,155	$271,414	$185,072	$334,321
Working capital	136,429	191,522	237,646	160,787	286,315
Total assets	250,299	342,781	433,897	393,397	577,936
Shareholders’ equity	197,198	268,981	342,728	286,894	425,239

Item 7. Management’s Discussion and Analysis of Financial Condition and Results of Operations

Overview

We manage our business and report revenue and operating income (loss) in three segments: (1) RealPlayer Group, (2) Mobile Entertainment, and (3) Games. Within our RealPlayer Group, revenue is derived from the sale of our RealPlayer media player software and related products, , our new RealPlayer Cloud service, and our SuperPass service . Our Mobile Entertainment business generates revenue from the sale of its SaaS services, which include ringback tones, music on demand, and intercarrier messaging, and our LISTEN product. Our Games business, through its Slingo, GameHouse and Zylom brands, derives revenue from sales of games licenses, online games subscription services, advertising on games sites and social networks, microtransactions within online and social games, and sales of mobile games.

We allocate certain corporate expenses which are directly attributable to supporting our businesses, including but not limited to a portion of finance, legal, human resources and headquarters facilities, to our reportable segments. The allocation of these costs to our business units ensures accountability for financial and operational performance within each of our reportable segments. Our most significant expenses relate to cost of revenue, compensating employees, and selling and marketing our products and services.

In 2014 our consolidated revenue declined by $50.0 million compared with 2013, due to a decrease of $36.0 million in RealPlayer Group revenue, a $12.7 million decrease in Games revenue, and a $1.3 million decrease in Mobile Entertainment revenue.

Revenue from our legacy products continues to decline as a result of certain changes in our businesses and market-driven factors. Our SaaS business within Mobile Entertainment continues to be negatively impacted by the proliferation of smartphone applications and services, some of which do not depend on our carrier customers for distribution to consumers. In addition, we are still experiencing pricing pressure from carriers for our intercarrier messaging services. Furthermore, we are no longer investing in our Helix product. In our Games segment, our business continues to be challenged as consumer game play continues to shift from downloadable PC games to social networks and mobile devices. Since 2011, we have been focusing on developing social and mobile games and monetizing those game play experiences. In our RealPlayer Group segment, revenue is being negatively impacted as a result of our transition to a new third party distribution partner at significantly lower rates compared to our previous partner, lower distribution in our licensing business and due to our focus towards RealPlayer Cloud and away from our legacy products.

Over the past several quarters, we have developed a growth plan, implemented strategic initiatives, and executed certain restructuring efforts, all in an effort to grow our businesses, move towards profitability, and streamline our operations. In line with our growth plan, we continue to invest in each of our three business units. During the first half of 2014, we released RealPlayer Cloud worldwide. This global roll out allows us to reach our base of over ten million active RealPlayer users around the world. In our Mobile Entertainment business we continue our efforts to roll out our new LISTEN product. In our Games business, we launched Slingo Adventure worldwide on Facebook and on mobile platforms during the second half of 2014. We expect to continue to invest heavily in our growth initiatives, including further development and marketing efforts around our products. These investments have negatively impacted our recent operating results, which may continue until the expected revenue growth materializes.

In addition to our revenue growth plans, we have continued to better align our operating expenses with our revenue profile through various restructuring actions, as described below in Consolidated Operating Expenses. These actions drove the $38.3 million decline in our operating expenses during 2014 compared to 2013 of which $11.5 million of the decline was due to a litigation settlement in 2013.

Summary of Results

Consolidated results of operations were as follows (dollars in thousands):

	2014	2013	2012	2014-2013 Change	% Change	2013-2012 Change	% Change
Total revenue	$156,212	$206,196	$258,842	$(49,984)	(24)%	$(52,646)	(20)%
Cost of revenue	76,381	79,091	103,731	(2,710)	(3)%	(24,640)	(24)%
Extinguishment of liability	(10,580)	—	—	(10,580)	—%	—	—%
Gross profit	90,411	127,105	155,111	(36,694)	(29)%	(28,006)	(18)%
Gross margin	58%	62%	60%	(4)%		2%	
Sale of patents and other technology assets, net of costs	—	—	116,353	—	—%	(116,353)	(100)%
Total operating expenses	159,564	197,913	215,901	(38,349)	(19)%	(17,988)	(8)%
Operating income (loss)	$(69,153)	$(70,808)	$55,563	$1,655	2%	$(126,371)	(227)%

2014 compared with 2013

Revenue decreased by $50.0 million, or 24%. The reduction in revenue resulted from a decline of $36.0 million in our RealPlayer Group segment, a decline of $12.7 million in our Games segment, and a decline of $1.3 million in our Mobile Entertainment segment, due to the factors described above. Gross margin decreased to 58% from 62%, primarily as a result of our transition to a new third party distribution arrangement at significantly lower rates compared to our previous partner in our RealPlayer business, and to declining sales in our storefront business in Games. These decreases in gross margin were partially offset by the extinguishment in Q1 2014 of certain accrued royalty liabilities of $10.6 million associated with our historical music business, which had been originally recorded based on statutory rates.

Operating expenses decreased by $38.3 million primarily due to reductions in personnel and related costs of $10.9 million, reductions in marketing costs of $10.4 million and lower costs related to our 2013 headquarters relocation of $5.7 million, which resulted from our ongoing expense re-alignment efforts, as well as litigation settlement costs of $11.5 million in the prior year.

2013 compared with 2012

Revenue decreased by $52.6 million, or 20%. The reduction in revenue resulted from a decline of $19.1 million in our Mobile Entertainment segment, a decline of $17.2 million in our Games segment, and a decline of $16.3 million in our RealPlayer Group segment, due to the factors described above. Gross margin increased to 62% from 60%, primarily as a result of lower personnel and related costs that resulted from our ongoing expense alignment efforts. Operating expenses decreased by $18.0 million primarily due to reductions in personnel and related costs that resulted from our ongoing expense alignment efforts, partially offset by litigation settlement costs of $11.5 million.

Segment Results

RealPlayer Group

RealPlayer Group segment results of operations were as follows (dollars in thousands):

	2014	2013	2012	2014-2013 Change	% Change	2013-2012 Change	% Change
Total revenue	$39,201	$75,206	$91,469	$(36,005)	(48)%	$(16,263)	(18)%
Cost of revenue	14,508	16,220	21,544	(1,712)	(11)%	(5,324)	(25)%
Gross profit	24,693	58,986	69,925	(34,293)	(58)%	(10,939)	(16)%
Gross margin	63%	78%	76%	(15)%		2%	
Total operating expenses	55,742	60,484	55,223	(4,742)	(8)%	5,261	10%
Operating income (loss)	$(31,049)	$(1,498)	$14,702	$(29,551)	NM	$(16,200)	(110)%

2014 compared with 2013

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Total RealPlayer Group revenue decreased by $36.0 million, or 48%. This decrease was primarily a result of our transition to a new third party distribution arrangement at significantly lower rates compared to our previous partner that caused our third party distribution revenue to decrease by $16.0 million, and lower subscription revenue of $5.5 million due to fewer SuperPass subscribers. Further contributing to the decline was a decrease in RealPlayer license revenue of $7.6 million due to our focus away from our RealPlayer product and towards increasing RealPlayer Cloud subscriptions, and a decrease of $5.9 million in distribution of intellectual property licenses.
Gross margin decreased by 15 percentage points, due primarily to our transition to a new third party distribution arrangement at significantly lower rates compared to our previous partner. Operating expenses decreased by $4.7 million primarily due to decreased marketing spend of $5.5 million mainly related to our third party distribution arrangements.
2013 compared with 2012
Total RealPlayer Group revenue decreased by $16.3 million, or 18%. This decrease was primarily a result of lower subscriptions revenue of $11.8 million due to fewer subscribers, primarily attributable to our SuperPass product.
Gross margin increased by 2 percentage points, due primarily to a higher proportion of lower margin revenue in the prior year.
Operating expenses increased by $5.3 million. Personnel and related costs increased $5.2 million, primarily due to investment in our new RealPlayer Cloud service.

Mobile Entertainment
Mobile Entertainment segment results of operations were as follows (dollars in thousands):

	2014	2013	2012	2014-2013 Change	% Change	2013-2012 Change	% Change
Total revenue	$79,901	$81,181	$100,318	$(1,280)	(2)%	$(19,137)	(19)%
Cost of revenue	50,399	47,608	57,670	2,791	6 %	(10,062)	(17)%
Gross profit	29,502	33,573	42,648	(4,071)	(12)%	(9,075)	(21)%
Gross margin	37 %	41 %	43 %	(4)%		(2)%	
Total operating expenses	33,325	35,839	52,614	(2,514)	(7)%	(16,775)	(32)%
Operating income (loss)	$(3,823)	$(2,266)	$(9,966)	$(1,557)	(69)%	$7,700	77 %

2014 compared with 2013
Mobile Entertainment revenue decreased by $1.3 million, or 2%. This decrease was primarily due to a decrease of $3.4 million due to termination of carrier contracts and a decrease of $1.2 million in our Helix business. These decreases, along with certain other declines in our SaaS business, were partially offset by an increase of $4.9 million in music on demand revenue, primarily in Korea.
Gross margin declined by 4 percentage points in 2014, due primarily to a higher proportion of lower margin revenue, such as music on demand, compared to the prior year.

2013 compared with 2012
In the quarter ended September 30, 2013, we acquired Muzicall, a ringback tone company based in London, for total cash consideration of $6.7 million. This acquisition is intended to accelerate our growth initiatives within the Mobile Entertainment segment.
Mobile Entertainment revenue decreased by $19.1 million, or 19%. This decrease was primarily due to reduced revenue from our SaaS offerings of $16.0 million, resulting from $17.0 million of lost revenue upon the termination of certain SaaS contracts over the previous six quarters. Slightly offsetting this decrease was an increase in ringback tones revenue of $2.1 million, resulting from our purchase of Muzicall.
Gross margin declined by 2 percentage points, due primarily to a higher proportion of lower margin revenue, such as music on demand, in the current year.

Operating expenses declined by $16.8 million primarily due to reductions in personnel and related costs of $17.2 million that resulted in part from the termination of certain SaaS contracts mentioned above, as well as from our ongoing expense re-alignment efforts. Partially offsetting these declines was an increase in total operating expense of $2.5 million as a result of the acquisition of Muzicall in 2013.

Games

Games segment results of operations were as follows (dollars in thousands):

	2014	2013	2012	2014-2013 Change	% Change	2013-2012 Change	% Change
Total revenue	$37,110	$49,809	$67,055	$(12,699)	(25)%	$(17,246)	(26)%
Cost of revenue	11,074	13,359	21,828	(2,285)	(17)%	(8,469)	(39)%
Gross profit	26,036	36,450	45,227	(10,414)	(29)%	(8,777)	(19)%
Gross margin	70%	73%	67%	(3)%		6%	
Total operating expenses	37,170	47,177	51,890	(10,007)	(21)%	(4,713)	(9)%
Operating income (loss)	$(11,134)	$(10,727)	$(6,663)	$(407)	(4)%	$(4,064)	(61)%

2014 compared with 2013

Games revenue decreased by $12.7 million, or 25%. Lower revenue from subscription products, advertising and license sales contributed $5.8 million, and $3.7 million, and $2.2 million, respectively, to the decline during the period.

Cost of revenue decreased by $2.3 million, or 17%. The decrease was primarily due to the decrease in partner royalties expense, which has a direct correlation with the decrease in Games revenue, in addition to reduced personnel costs. Gross margin decreased due primarily to a higher proportion of lower margin revenue in the current year.

Operating expenses decreased by $10.0 million, or 21%. The decrease was primarily due to reductions in personnel and related costs of $4.9 million, and reductions in marketing expense of $4.3 million.

2013 compared with 2012

In the quarter ended June 30, 2013, we acquired Slingo, a social casino games company based in the U.S., for total cash consideration of $15.6 million. This acquisition is intended to enhance our footprint in the social casino games arena. Associated with this are incremental costs for investment in new products, which have directly impacted our operating loss before taxes.

Games revenue decreased by $17.2 million, or 26%. Lower revenue from license sales, subscription products, and advertising contributed $8.3 million, $5.8 million, and $4.3 million, respectively, to the decline during the period. Slightly offsetting these decreases was an increase of $2.1 million in games revenue as a result of the acquisition of Slingo.

Cost of revenue decreased by $8.5 million, or 39%. The decrease was due to the decrease in partner royalties expense, which has a direct correlation with the decrease in Games revenue. Gross margin increased due to lower margin projects that occurred in the prior year periods, in addition to lower personnel and related costs in the current period resulting from our ongoing expense alignment efforts.

Operating expenses decreased by $4.7 million, or 9%. The decrease was primarily due to reductions in personnel and related costs of $5.5 million, and reductions in marketing expense of $1.9 million. Partially offsetting these declines was an increase in total operating expense of $3.9 million as a result of the acquisition and investment in new products related to Slingo.

Corporate

We allocate certain corporate expenses which are directly attributable to supporting the business to our reportable segments. These allocated corporate expenses include but are not limited to a portion of finance, legal, human resources and headquarters facilities. Remaining expenses, which are not directly attributable to supporting the business, are reported as corporate items. All restructuring, extinguishment of liability, lease exit and related charges, and, for 2013, the loss on litigation settlements, are included in the corporate segment.

Corporate segment results of operations were as follows (dollars in thousands):

	2014	2013	2012	2014-2013 Change	% Change	2013-2012 Change	% Change
Cost of revenue	$400	$1,904	$2,689	$(1,504)	(79)%	$(785)	(29)%
Extinguishment of liability	(10,580)	—	—	(10,580)	100%	—	—%
Gain on sale of patents and other technology assets, net of costs	—	—	116,353	—	—%	(116,353)	(100)%
Total operating expenses	33,327	54,413	56,174	(21,086)	(39)%	(1,761)	(3)%
Operating income (loss)	$(23,147)	$(56,317)	$57,490	$33,170	59%	$(113,807)	(198)%

2014 compared with 2013

During the quarter ended March 31, 2014 certain accrued royalty liabilities of $10.6 million associated with our historical music business, which had originally been recorded based on statutory rates, were extinguished.

Cost of revenue decreased by $1.5 million. The decrease was due primarily to lower costs resulting from the 2013 Seattle headquarters relocation.

Operating expenses decreased by $21.1 million, or 39%. The decrease was primarily due to savings from the 2013 relocation of our Seattle headquarters totaling $5.7 million, reduced restructuring and lease exit charges of $3.0 million and the litigation settlements of $11.5 million that occurred in 2013.

2013 compared with 2012

The 2012 gain from the sale of patents and other technology assets to Intel Corporation of $116.4 million reflects the cash proceeds of $120.0 million in the second quarter, less $3.6 million of direct transaction expenses incurred during the first and second quarters.

Operating expenses decreased by $1.8 million, or 3%. The decrease was primarily due to reductions in personnel and related costs of $3.0 million, in addition to reduced restructuring charges of $9.7 million. Partially offsetting these decreases were the 2013 litigation settlements of $11.5 million.

Consolidated Operating Expenses

Our operating expenses consist primarily of salaries and related personnel costs including stock based compensation, consulting fees associated with product development, sales commissions, amortization of certain intangible assets capitalized in our acquisitions, professional service fees, advertising costs, and restructuring charges. Operating expenses were as follows (dollars in thousands):

	2014	2013	2012	2014-2013 Change	% Change	2013-2012 Change	% Change
Research and development	$52,765	$60,880	$63,194	$(8,115)	(13)%	$(2,314)	(4)%
Sales and marketing	66,926	80,011	90,301	(13,085)	(16)%	(10,290)	(11)%
General and administrative	34,001	36,643	43,891	(2,642)	(7)%	(7,248)	(17)%
Restructuring and other charges	4,992	5,765	15,225	(773)	(13)%	(9,460)	(62)%
Lease exit and related charges (gains)	880	3,089	3,290	(2,209)	(72)%	(201)	(6)%
Loss on litigation settlements	—	11,525	—	(11,525)	100%	11,525	100%
Total consolidated operating expenses	$159,564	$197,913	$215,901	$(38,349)	(19)%	$(17,988)	(8)%

Research and development expenses decreased by $8.1 million, or 13%, in the year ended 2014, compared with 2013. While we continue to invest in new products, we saw an overall decrease in personnel and related costs of $5.4 million, resulting from our ongoing expense re-alignment efforts in addition to $3.8 million savings from the relocation of our Seattle headquarters.

Research and development expenses decreased by $2.3 million, or 4%, in the year ended 2013, compared with 2012. While we continue to invest in new products, we saw an overall decrease in personnel and related costs of $3.6

million, resulting from our ongoing expense re-alignment efforts.

Sales and marketing expenses decreased by $13.1 million, or 16%, in the year ended 2014, compared with 2013. The decrease was due primarily due to reductions in marketing expenses of $10.5 million, related to our third party distribution arrangements.

Sales and marketing expenses decreased by $10.3 million, or 11%, in the year ended 2013, compared with 2012. The decrease was due primarily to a decrease in personnel and related costs of $7.8 million resulting from our ongoing expense re-alignment efforts.

General and administrative expenses decreased by $2.6 million, or 7%, in the year ended 2014, compared with 2013. Contributing to the decrease for the period was a decrease in personnel and related costs of $1.8 million resulting from our ongoing expense re-alignment efforts.

General and administrative expenses decreased by $7.2 million, or 17%, in the year ended 2013, compared with 2012. Contributing to the decrease for the period was a decrease in personnel and related costs of $6.0 million, and to $1.3 million related to the expense in 2012 for the final settlement of the Washington State Attorney General's office matter, as disclosed in the 2012 10-K.

Restructuring and other charges and Lease exit and related charges consist of costs associated with the ongoing reorganization of our business operations and our ongoing expense re-alignment efforts. The restructuring expense amounts in all years primarily related to severance costs due to workforce reductions. For additional details on these charges see Note 10, Restructuring Charges and Note 11, Lease Exit and Related Charges.

Loss on litigation settlements recorded during 2013 relates to settlement agreements executed in October 2013, for which we paid in full an aggregate amount of $11.5 million during the fourth quarter of 2013, as discussed in Note 16, Commitments and Contingencies.

Other Income (Expenses)

Other income (expenses), net was as follows (dollars in thousands):

	2014	Change	2013	Change	2012
Interest income, net	$556	(51)%	$1,133	(5)%	$1,192
Gain (loss) on sale of equity investments,net	2,371	(89)%	21,389	322%	5,072
Equity in net loss of Rhapsody	(4,452)	29%	(6,268)	10%	(5,709)
Other income (expense), net	143	(69)%	467	(62)%	1,241
Total other income (expense), net	$(1,382)	(108)%	$16,721	831%	$1,796

As described further in Note 4, Rhapsody Joint Venture, we account for our investment in Rhapsody under the equity method of accounting. The net carrying value of our investment in Rhapsody is not necessarily indicative of the underlying fair value of our investment.

The 2014 gain on sale of equity investments, net, was due to a $2.4 million gain on the sale of a portion of our shares held in J-Stream. The 2013 gain on sale of equity investments, net, was due to a $21.4 million gain on the sale of all of our remaining shares of common stock in LoEn Entertainment, Inc. The 2012 gain on sale of equity investments, net, was driven by the sale of a portion of our shares in LoEn and a gain on the sale of our Film.com assets, totaling $5.3 million. For additional details on the J-Stream and LoEn transactions see Note 5, Fair Value Measurements.

Income Taxes

During the years ended December 31, 2014, 2013, and 2012, we recognized income tax expense of $1.3 million, $4.9 million and $12.5 million, respectively, related to U.S. and foreign income taxes.

The tax expense for the year ended December 31, 2014 was largely the result of foreign withholding taxes and income taxes in foreign jurisdictions. The tax expense for the year ended December 31, 2013 was largely the result of valuation allowances we recorded in certain foreign jurisdictions. The tax expense for the year ended December 31, 2012 was largely the result of the sale of certain patent assets and other technology assets to Intel Corporation for gross cash consideration of $120 million in 2012.

We assess the likelihood that our deferred tax assets will be recovered based upon our consideration of many factors, including the current economic climate, our expectations of future taxable income, our ability to project such income, and the appreciation of our investments and other assets. We maintain a partial valuation allowance of $149.5 million for our deferred

tax assets due to uncertainty regarding their realization as of December 31, 2014. The net increase in the valuation allowance since December 31, 2013 of $20.6 million was the result of an increase in current year deferred tax assets for which the Company maintains a valuation allowance.
We generate income in a number of foreign jurisdictions, some of which have higher tax rates and some of which have lower tax rates relative to the U.S. federal statutory rate. Changes to the blend of income between jurisdictions with higher or lower effective tax rates than the U.S. federal statutory rate could affect our effective tax rate. For the year ended December 31, 2014, decreases in tax expense from income generated in foreign jurisdictions with lower tax rates in comparison to the U.S. federal statutory rate were offset by increases in tax expense from income generated in foreign jurisdictions having comparable, or higher tax rates in comparison to the U.S. federal statutory rate.
As of December 31, 2014 and 2013, we had $3.5 million and $4.5 million of unrecognized tax benefits, respectively. The decrease in unrecognized tax benefits is due to the expiration of statute of limitations. As of December 31, 2014, there are no unrecognized tax benefits remaining that would affect our effective tax rate if recognized, as the offset would increase the valuation allowance. The total amount of unrecognized tax benefits that would affect our effective tax rate if recognized was $0.4 million as of December 31, 2013. We file numerous consolidated and separate income tax returns in the U.S. including federal, state and local, as well as foreign jurisdictions. With few exceptions, we are no longer subject to U.S. federal income tax examinations for tax years before 2008 or state, local, or foreign income tax examinations for years before 1993. We are currently under audit by various states and foreign jurisdictions for certain tax years subsequent to 1993. We are currently under audit for United States federal returns for the consolidated group (RealNetworks, Inc. and Subsidiaries) for the year ended December 31, 2012.
Geographic Revenue
Revenue by geographic region was as follows (dollars in thousands):

	2014	2013	2012	2014-2013 Change	% Change	2013-2012 Change	% Change
United States	$61,660	$90,250	$117,844	$(28,590)	(32)%	$(27,594)	(23)%
Europe	26,575	38,155	56,473	(11,580)	(30)%	(18,318)	(32)%
Korea	39,852	46,601	40,467	(6,749)	(14)%	6,134	15%
Rest of World	28,125	31,190	44,058	(3,065)	(10)%	(12,868)	(29)%
Total Revenue	$156,212	$206,196	$258,842	$(49,984)	(24)%	$(52,646)	(20)%

Revenue in the U.S. decreased by $28.6 million, or 32%, in the year-ended 2014, compared with 2013. The decline was mainly due to a reduction in revenue from the distribution of our third party software products of $14.9 million, a decline in revenue from our games business of $3.6 million, a decline of $4.7 million relating to our SuperPass subscriptions offering, a decrease in revenue from our RealPlayer Plus product of $2.4 million, and a decline in our SaaS revenue of $1.9 million.
Revenue in the U.S. declined by $27.6 million, or 23%, in the year-ended 2013, compared with 2012. The decline was primarily due to reductions in revenue generated from our SaaS offerings of $13.0 million, lower sales of RealPlayer Group subscriptions, mainly including our SuperPass product, of $8.3 million, and lower sales of games subscriptions and licenses of $5.8 million.
Revenue in Europe decreased by $11.6 million, or 30%, in the year-ended 2014, compared with 2013. The decrease was primarily due to lower revenue from our Games segment of $7.7 million, lower revenue generated from sales of RealPlayer Plus totaling $1.9 million and a $1.3 million decrease in revenue from the distribution of our third party software products.
Revenue in Europe decreased by $18.3 million, or 32%, in the year-ended 2013, compared with 2012. The decrease was primarily due to lower revenue from our Games segment of $9.3 million, reductions in revenue generated from our SaaS offerings of $3.3 million, and lower intellectual property license revenue of $2.8 million.
Revenue in Korea decreased by $6.7 million, or 14%, in the year-ended 2014, compared with 2013. The decrease was primarily due to decreased revenue from intellectual property licensing of $8.3 million. Revenue from our SaaS

offerings, however, increased approximately $2.1 million, due in part to increased music on demand revenue of $5.7 million, partially offset by a decrease in several other SaaS offerings totaling $3.6 million.
Revenue in Korea increased by $6.1 million, or 15%, in the year-ended 2013, compared with 2012. The increase was primarily due to increased revenue from intellectual property licensing of $4.7 million. Additionally we saw increased revenue generated from our SaaS offerings of $2.6 million, due in part to increased lower margin music on demand revenue of $9.4 million, offset by declines in our other SaaS offerings of $6.8 million. These increases were partially offset by a decline in professional services revenue of $1.4 million.

Revenue in the rest of world decreased by $3.1 million, or 10%, in the year-ended 2014, compared with 2013. The decrease was primarily due to lower overall revenue within our RealPlayer Group from sales of RealPlayer Plus of $2.3 million, lower revenue from our SaaS business of $1.3 million, lower subscription revenue of $1.2 million and lower revenue from the distribution of third party software products of $0.9 million. In addition, revenue generated from our Games business was $0.4 million lower. These decreases were slightly offset, however, by an increase in revenue from sales of our intellectual property license of $2.8 million.

Revenue in the rest of world decreased by $12.9 million, or 29%, in the year-ended 2013, compared with 2012. The decrease was primarily due to lower revenue within our RealPlayer Group from licensing and subscriptions revenue of $4.3 million and $2.3 million, respectively, in addition to lower revenue generated from our SaaS offerings of $2.2 million.

Liquidity and Capital Resources

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

	December 31,	
	2014	2013
Working capital	$136,429	$191,522
Cash, cash equivalents, and short-term investments	161,706	226,155
Restricted cash and investments	3,000	3,000

The decrease in 2014 working capital from December 31, 2013, which includes cash, cash equivalents short term investments, was primarily due to cash used in our operations of $60.2 million.

The following summarizes cash flow activity (in thousands):

	Years Ended December 31,		
	2014	2013	2012
Cash provided by (used in) operating activities	$(60,244)	$(49,879)	$(33,313)
Cash provided by (used in) investing activities	15,561	39,242	87,135
Cash provided by (used in) financing activities	(637)	(1,435)	2,807

Cash used in operating activities consisted of net income (loss) adjusted for certain non-cash items such as depreciation and amortization, as well as the effect of changes in certain operating assets and liabilities.

Cash used in operating activities was $10.4 million more in 2014 than in 2013. This increase in cash used was primarily due to the decline in revenue of $50.0 million which was offset, in part, by the decrease in operating expenses of $ 38.3 million.

The higher amount of cash used in operating activities for 2013 compared to 2012 was primarily due to the decline in revenues of $52.6 million for 2013 compared with the prior year, which was partially offset by a decline in cost of revenue of $24.6 million for 2013. We also had a net decrease in cash of $3.6 million for the year ended December 31, 2013 related to changes in certain operating assets and liabilities, compared with a net decrease in cash of $11.7 million for the year ended December 31, 2012 related to changes in certain operating assets and liabilities.

For the year ended December 31, 2014, cash provided by investing activities of $15.6 million was mainly from sales and maturities, net of purchases, of short-term investments totaling $16.5 million. In addition, cash proceeds from the sale of available for sale securities of $2.8 million in 2014 mainly offset purchases of equipment, software and leasehold improvements of $2.5 million.

For the year ended December 31, 2013, cash provided by investing activities of $39.2 million was due to the net cash proceeds of $29.2 million received from the sale of our remaining shares of common stock in LoEn. Further contributing to the total cash provided was sales and maturities, net of purchases, of short-term investments of $33.3 million. Offsetting these cash proceeds was cash used for the acquisition of businesses, net of cash acquired, of $22.5 million.

For the year ended December 31, 2012, cash provided by investing activities of $87.1 million was due to the net cash proceeds of $116.4 million received from the sale of certain patents and other technology assets to Intel Corporation in the second quarter, and cash proceeds of $7.3 million related to the sale of certain equity and other investments, offset in part by purchases of equipment, software and leasehold improvements totaling $7.2 million, and purchases, net of sales and maturities, of short-term investments of $29.5 million.

Financing activities for the year ended December 31, 2014 used cash totaling $0.6 million which was mainly due to tax payments from shares withheld upon vesting of restricted stock and the payment of contingent consideration related to acquisitions of businesses, partially offset by proceeds received from the issuance of common stock.

Financing activities for the year ended December 31, 2013 used cash primarily from tax payments from shares withheld upon the vesting of employee restricted stock, in addition to payment of contingent consideration relating to a previous acquisition. This was partially offset by the proceeds from the exercise of employee stock options and proceeds from sales of common stock under the employee stock purchase plan.

Financing activities for the year ended December 31, 2012, provided cash from the proceeds from the exercise of employee stock options and proceeds from sales of common stock under the employee stock purchase plan, offset partially by tax payments from shares withheld upon the vesting of employee restricted stock.

We currently have no planned significant capital expenditures for 2015 other than those in the ordinary course of business.

Our principal future cash commitments include office leases. 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.

In the future, we may seek to raise additional funds through public or private equity financing, or through other sources such as future credit facilities. The sale of additional equity securities could result in dilution to our shareholders. In addition, in the future, we may enter into cash or stock acquisition transactions or other strategic transactions that could reduce cash available to fund our operations or result in dilution to shareholders.

Our cash equivalents and short-term investments consist of investment-grade 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 primarily in five functional currencies: the U.S. dollar, the Korean won, the Japanese yen, the British pound and the euro. We currently do not hedge the majority of our foreign currency exposures and are therefore subject to the risk of exchange rate fluctuations. 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.

As of December 31, 2014, approximately $27.1 million of the $161.7 million of cash, cash equivalents, and short-term investments was held by our foreign subsidiaries. If these funds are needed for our operations in the U.S., we may be required to accrue and pay U.S. taxes to repatriate these funds. However, our intent is to permanently reinvest these funds outside of the U.S. and our current plans do not demonstrate a need to repatriate them to fund our U.S. operations. Additionally, the Company currently has significant net operating losses and other tax attributes that could be used to offset most potential U.S. income tax that could result if these amounts were distributed to the U.S. We utilize a variety of tax planning and financing strategies in an effort to ensure that our worldwide cash is available in the locations in which it is needed. We do not expect restrictions or potential taxes on repatriation of amounts held outside of the U.S to have a material effect on our overall liquidity, financial condition or results of operations.

As of December 31, 2014, we have not provided for U.S. federal and state income taxes on approximately $13.9 million of undistributed earnings of our foreign subsidiaries, since such earnings are considered permanently reinvested outside the U.S. or may be remitted tax-free to the U.S. If these amounts were distributed to the U.S, in the future 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 timing of such future distributions, the availability of foreign tax credits, and the complexity of the computation if such earnings were not deemed to be permanently reinvested. If future events, including material changes in estimates of cash, working capital, and long-term investment requirements necessitate that these earnings be repatriated, an additional provision for U.S. income and foreign withholding taxes, net of foreign tax credits, may be necessary.

Contractual Obligations

Please refer to Note 16, Commitments and Contingencies, for details on our contractual obligations, which consist of operating leases for office facilities. For income tax liabilities for uncertain tax positions we cannot make a reasonably reliable estimate of the amount and period of any related future payments. As of December 31, 2014 we had $3.5

million of gross unrecognized tax benefits for uncertain tax positions.
Off-Balance Sheet Arrangements
We have operating lease obligations for office facility leases with future cash commitments that are not required to be recorded on our consolidated balance sheet. Accordingly, these operating lease obligations constitute off-balance sheet

arrangements. In addition, since we do not maintain accruals associated with certain guarantees, as discussed in Note 17, Guarantees, those guarantee obligations also constitute off-balance sheet arrangements.

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;
- Estimating recoverability of deferred costs;
- Estimating allowances for doubtful accounts and sales returns;
- Valuation of equity method investments;
- Valuation of definite-lived assets;
- Valuation of goodwill and indefinite-lived intangible assets;
- Stock-based compensation; and
- Accounting for income taxes.

Revenue Recognition. We recognize revenue when persuasive evidence of an arrangement exists, delivery has occurred, the sales price is fixed or determinable, and collection is probable. Physical products are considered delivered to the customer once they have been shipped and title and risk of loss have been transferred. For online sales, the products or services are considered delivered at the time the product or services are made available, digitally, to the end user.

We recognize revenue on a gross or net basis. In most arrangements, we contract directly with end user customers, and are the primary obligor. In such arrangements, we recognize revenue on a gross basis. In some cases, we utilize third-party distributors who are the primary obligor to sell products or services directly to end user customers. In such instances, we recognize revenue on a net basis.

In our direct to consumer operations, we derive revenue primarily through (1) subscriptions of SuperPass within our RealPlayer Group segment and subscriptions sold by our Games segment, (2) sales of content downloads, software and licenses offered by our RealPlayer Group, Mobile Entertainment, and Games segments and (3) the sale of advertising and the distribution of third-party products on our websites and in our games.

Consumer subscription products are paid in advance, typically for monthly, quarterly or annual duration. Subscription revenue is recognized ratably over the related subscription time period. Revenue from sales of content downloads, software and licenses is recognized at the time the product is made available, digitally, to the end user. Revenue generated from advertising on our websites and from advertising and the distribution of third-party products included in our products is recognized as revenue at the time of delivery.

We also generate revenue through business-to-business channels by providing services within our Mobile Entertainment segment enabling mobile carriers to deliver audio and video content to their customers and by selling software licenses and products and related support and other services. Revenue generated from services provided to mobile carriers that enable the delivery of audio and video content to their customers is recognized as the services are provided. Setup fees to build these services are recognized ratably upon launch of the service over the remaining expected term of the service.

Non-software revenue arrangements containing multiple elements are divided into separate units of accounting, after being evaluated for specific criteria. If the criteria for separation are met, revenue is allocated to the individual units using the relative price method. If the criteria are not met, the elements are treated as one unit of accounting and revenue recognition is delayed until all elements have been delivered. In the case of revenue arrangements containing software, elements are divided into separate units of accounting only when vendor-specific objective evidence has been established. In cases where vendor-specific objective evidence has not been established, undelivered elements are combined into one unit of accounting and are not recognized in revenue until all elements have been delivered.

Estimating Music Publishing Rights and Music Royalty Accruals. We have made estimates of amounts that may be owed related to music royalties for our historical domestic and international music services. Material differences may impact 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 have delivered. 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. 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 have based 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.

During the quarter ended March 31, 2014, certain accrued royalty liabilities of $10.6 million associated with our historical music business, which had originally been recorded based on statutory rates, were extinguished. Our remaining accrued royalty liability as of December 31, 2014 totaled $2.9 million.

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

Assessing the recoverability of deferred project costs is based on significant assumptions and estimates, including future revenue and cost of sales. Significant or sustained decreases in revenue or increases in cost of sales in future periods could result in impairments of deferred project costs. We cannot accurately predict the amount and timing of any such impairments. Should the value of deferred project costs become impaired, we would record the appropriate charge, which could have a material adverse effect on our financial condition or results of operations.

Estimating Allowances for Doubtful Accounts and Sales Returns. We make estimates of the uncollectible portion 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 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 are made and used in connection with establishing allowances for doubtful accounts and sales returns. 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 or actual future experience was different from the judgments and estimates.

Valuation of Equity Method Investments. We use the equity method of accounting for investments in circumstances where we have the ability to exert significant influence, but not control, over an investee or joint venture. We initially record our investment based on a fair value analysis of the investment.

We record our percentage interest in the investee's recorded income or loss and changes in the investee's capital under this method, which will increase or decrease the reported value of our investment. We record investee losses up to the aggregate amount of the investment. As further described in Note 4, because of the $10.0 million liquidation preference on the preferred stock we hold in Rhapsody, under the equity method of accounting we do not record any share of Rhapsody losses that would reduce our carrying value of Rhapsody, which is impacted by Rhapsody equity transactions, below $10.0 million, unless Rhapsody's book value is reduced below $10.0 million.

We evaluate impairment of an investment valued under the equity method if events and circumstances warrant. An impairment charge would be recorded if a decline in value of an equity investment below its carrying amount were determined to be other than temporary. In determining if a decline is other than temporary, we consider factors such as the length of time and extent to which the fair value of the investment has been less than the carrying amount of the investee or joint venture, the near-term and longer-term operating and financial prospects of the investee or joint venture and our intent and ability to hold the investment for a period of time sufficient to allow for any anticipated recovery.

Valuation of Definite-Lived Assets. Definite-lived assets consist primarily of property, plant and equipment, as well as amortizable intangible assets acquired in business combinations. Definite-lived assets are amortized on a straight line basis over their estimated useful lives. We review definite-lived assets for impairment whenever events or changes in circumstances indicate the carrying amount of such assets may not be recoverable. Recoverability of these assets is measured by comparison of their carrying amount to future undiscounted cash flows the assets are expected to generate. If definite-lived assets are considered to be impaired, the impairment to be recognized equals the amount by which the carrying value of the assets exceeds their fair market value.

The impairment analysis of definite-lived assets is based upon estimates and assumptions relating to our future revenue, cash flows, operating expenses, costs of capital and capital purchases. These estimates and assumptions are complex and subject to a significant degree of judgment with respect to certain factors including, but not limited to, the cash flows of our long-term operating plans, market and interest rate risk, and risk-commensurate discount rates and cost of capital. Significant or sustained declines in future revenue or cash flows, or adverse changes in our business climate, among other factors, and their resulting impact on the estimates and assumptions relating to the value of our definite-lived assets could result in the need to perform an impairment analysis in future periods which could result in a significant impairment. While we believe our estimates and assumptions are reasonable, due to their complexity and subjectivity, these estimates and assumptions could vary from period to period. Changes in these estimates and assumptions could materially affect the estimate of future undiscounted cash flows and related fair market values of these assets and result in significant impairments, which could have a material adverse effect on our financial condition or results of operations.

As of December 31, 2014, we had $9 million in total carrying value of definite-lived assets related to our Mobile Entertainment group. In accordance with our policy as described above, we reviewed these assets for impairment as of December 31, 2014. Our estimate of the fair value of this asset group exceeds the carrying amount and, therefore, no impairment is indicated as of December 31, 2014. However, it is reasonably possible that the estimate of the fair value of the Mobile Entertainment group may change in the near term should we experience adverse changes in our estimates and assumptions, which could result in impairments of those assets. For further discussion, please see the risk factor entitled, "Any impairment to our goodwill, indefinite-lived intangible assets or definite-lived assets could result in a significant charge to our earnings" under Item 1A Risk Factors.

Valuation of Goodwill and Indefinite-Lived Intangible Assets. We test goodwill for impairment on an annual basis, in our fourth quarter, or more frequently if circumstances indicate reporting unit carrying values may exceed their fair values. Circumstances that may indicate a reporting unit's carrying value exceeds its fair value include, but are not limited to: 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.

When evaluating goodwill for impairment, based upon our annual test or due to changes in circumstances described above, we first perform a qualitative assessment to determine if the fair value of a reporting unit is more likely than not less than the reporting unit's carrying amount including goodwill. If this assessment indicates it is more likely than not, we then compare the carrying value of the reporting unit to the estimated fair value of the reporting unit. If the carrying value of the reporting unit exceeds the estimated fair value, we then calculate the implied estimated fair value of goodwill for the reporting unit and compare it to the carrying amount of goodwill for the reporting unit. If the carrying amount of goodwill exceeds the implied estimated fair value, an impairment charge to current operations is recorded to reduce the carrying value to implied estimated value.

Significant judgments and estimates are required in determining the reporting units and assessing the fair value of the reporting units. These estimates and assumptions are complex and subject to a significant degree of judgment with respect to certain factors including, but not limited to, the cash flows of long-term operating plans, market and interest rate risk, and risk-commensurate discount rates and cost of capital.

We evaluate indefinite-lived intangible assets (primarily tradenames and trademarks) for impairment on an annual basis, in the fourth quarter, or more frequently if an event occurs or changes in circumstances indicate that impairment may exist. When evaluating indefinite-lived intangible assets for impairment, we may first perform a qualitative assessment to determine if the fair value of the intangible assets is more likely than not greater than its carrying amount. If we do not perform a qualitative assessment or if the fair value of the intangible assets is not more likely than not greater than its carrying amount, we estimate the fair value of the intangible assets. If the carrying amount of the intangible assets exceeds the estimated fair value, an impairment charge is recorded to reduce the carrying value to the estimated fair value. Significant judgments and estimates are required in assessing the fair value of the indefinite-lived intangible assets. These estimates and assumptions are complex and subject to a significant degree of judgment with respect to certain factors including, but not limited to, the cash flows of long-term operating plans, market and interest rate risk, and risk-commensurate discount rates and cost of capital.

Stock-Based Compensation. Stock-based compensation cost is estimated at the grant date based on the award's fair value and is recognized as expense over the requisite service period, which is the vesting period. For stock options, the fair value is calculated using the Black-Scholes option-pricing model or other appropriate valuation models such as Monte Carlo simulation. The valuation models require various highly judgmental assumptions including volatility in our common stock price and expected option life. If any of the assumptions used in the valuation models change significantly, stock-based compensation expense for new awards may differ materially in the future from the amounts recorded in our consolidated statement of operations. For all awards, 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 forfeitures.

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 income tax expense and 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 the current and deferred 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.

Each reporting period we must periodically assess the likelihood that our deferred tax assets will be recovered from future sources of 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. In certain instances, changes in the valuation allowance may be allocated directly to the related components of shareholders' equity on the consolidated balance sheet. 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.

As of December 31, 2014, $27.1 million of the $161.7 million of cash, cash equivalents, and short-term investments was held by our foreign subsidiaries.

As of December 31, 2014, we have not provided for U.S. federal and state income taxes on approximately $13.9 million of undistributed earnings of our foreign subsidiaries, since such earnings are considered indefinitely reinvested outside the U.S. or may be remitted tax-free to the U.S. If these amounts were distributed to the U.S., in the form of dividends or otherwise, RealNetworks could be subject to additional U.S. income and foreign withholding taxes. It is not practicable to determine the foreign withholding and U.S. federal income tax liability or benefit on such earnings due to the timing of such future distributions, the availability of foreign tax credits, and the complexity of the computation if such earnings were not deemed to be permanently reinvested. If future events, including material changes in estimates of cash, working capital, and long-term investment requirements necessitate that these earnings be distributed, an additional provision for U.S. income and foreign withholding taxes, net of foreign tax credits, may be necessary.

Recently Issued Accounting Standards

See Note 2, Recent Accounting Pronouncements.

Item 7A. Quantitative and Qualitative Disclosures About Market Risk

The following discussion about our market risk involves forward-looking statements. All statements that do not relate to matters of historical fact should be considered forward-looking statements. Actual results could differ materially from those projected in any 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. Our short-term investments consist of investment grade 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. See Note 5, Fair Value Measurements for additional information. 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, 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 December 31, 2014. Based on our cash, cash equivalents, short-term investments, and restricted cash equivalents as of December 31, 2014, a hypothetical 10% increase/decrease in interest rates would not increase/decrease our annual interest income or cash flows by more than a nominal amount.

Investment Risk. As of December 31, 2014, we had investments in voting capital stock of both publicly traded and privately held technology companies for business and strategic purposes. See Note 1, Description of Business and Summary of Significant Accounting Policies - Valuation of Equity Method Investments, and Management's Discussion and Analysis of Financial Condition and Results of Operations - Critical Accounting Policies and Estimates (Valuation of equity method investments) in this 10-K for details on our accounting treatment for these investments, including the analysis of other-than-temporary impairments.

Foreign Currency Risk. We conduct business internationally in several currencies and thus 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 remeasurement 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. We manage a portion of these risks 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. Some of our unhedged exposures are recorded in our statement of operations on a mark-to-market basis each quarter, so to the extent we continue to experience adverse economic conditions, we may record losses related to such unhedged exposures in future periods that may have a material adverse effect on our financial condition and results of operations.

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

We have cash balances denominated in foreign currencies which are subject to foreign currency fluctuation risk. The majority of our foreign currency denominated cash is held in Korean won and euros. A hypothetical 10% increase or decrease in the Korean won and euro relative to the U.S. dollar as of December 31, 2014 would not result in more than a nominal amount of unrealized gain or loss.

Item 8. Financial Statements and Supplementary Data

REALNETWORKS, INC. AND SUBSIDIARIES

CONSOLIDATED BALANCE SHEETS

(In thousands, except per share data)

	December 31, 2014	December 31, 2013
ASSETS		
Current assets:		
Cash and cash equivalents	$103,253	$151,235
Short-term investments	58,453	74,920
Trade accounts receivable, net of allowances	15,257	24,613
Deferred costs, current portion	702	1,601
Deferred tax assets, current portion	652	306
Prepaid expenses and other current assets	8,980	9,124
Total current assets	187,297	261,799
Equipment and software	74,100	86,721
Leasehold improvements	3,590	3,482
Total equipment, software, and leasehold improvements	77,690	90,203
Less accumulated depreciation and amortization	61,442	67,031
Net equipment, software, and leasehold improvements	16,248	23,172
Restricted cash equivalents and investments	3,000	3,000
Equity method investment	10,000	12,473
Available for sale securities	2,676	7,181
Other assets	2,299	2,332
Deferred costs, non-current portion	316	946
Deferred tax assets, net, non-current portion	999	1,409
Other intangible assets, net	10,109	12,993
Goodwill	17,355	17,476
Total assets	$250,299	$342,781
LIABILITIES AND SHAREHOLDERS’ EQUITY		
Current liabilities:		
Accounts payable	$18,653	$19,987
Accrued and other current liabilities	25,286	41,893
Deferred tax liabilities, net, current portion	1,628	899
Deferred revenue, current portion	5,301	7,498
Total current liabilities	50,868	70,277
Deferred revenue, non-current portion	235	166
Deferred rent	1,215	1,318
Deferred tax liabilities, net, non-current portion	702	1,556
Other long-term liabilities	81	483
Total liabilities	53,101	73,800
Commitments and contingencies		
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 250,000 shares; issued and outstanding 36,099 shares in 2014 and 35,833 shares in 2013	36	36
Additional paid-in capital	617,756	610,167

Accumulated other comprehensive loss	(55,252)	(47,695)
Retained deficit	(365,342)	(293,527)
Total shareholders’ equity	197,198	268,981
Total liabilities and shareholders’ equity	$250,299	$342,781

See accompanying notes to consolidated financial statements.

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

	Years Ended December 31,		
	2014	2013	2012
Net revenue (A)	$156,212	$206,196	$258,842
Cost of revenue (B)	76,381	79,091	103,731
Extinguishment of liability (See Note 9)	(10,580)	—	—
Gross profit	90,411	127,105	155,111
Sale of patents and other technology assets, net of costs	—	—	116,353
Operating expenses:			
Research and development	52,765	60,880	63,194
Sales and marketing	66,926	80,011	90,301
General and administrative	34,001	36,643	43,891
Restructuring and other charges	4,992	5,765	15,225
Lease exit and related charges	880	3,089	3,290
Loss on litigation settlements	—	11,525	—
Total operating expenses	159,564	197,913	215,901
Operating income (loss)	(69,153)	(70,808)	55,563
Other income (expenses):			
Interest income, net	556	1,133	1,192
Gain on sale of equity and other investments, net	2,371	21,389	5,072
Equity in net loss of Rhapsody investment	(4,452)	(6,268)	(5,709)
Other income (expense), net	143	467	1,241
Total other income (expenses), net	(1,382)	16,721	1,796
Income (loss) before income taxes	(70,535)	(54,087)	57,359
Income tax expense (benefit)	1,280	4,903	12,518
Net income (loss)	$(71,815)	$(58,990)	$44,841
Basic net income (loss) per share	$(2.00)	$(1.66)	$1.29
Diluted net income (loss) per share	$(2.00)	$(1.66)	$1.28
Shares used to compute basic net income (loss) per share	35,947	35,553	34,873
Shares used to compute diluted net income (loss) per share	35,947	35,553	35,122
Comprehensive income (loss):			
Unrealized investment holding gains (losses), net of reclassification adjustments	$(4,145)	$(20,288)	$(633)
Foreign currency translation adjustments, net of reclassification adjustments	(3,412)	(867)	(1,023)
Total other comprehensive income (loss)	(7,557)	(21,155)	(1,656)
Net income (loss)	(71,815)	(58,990)	44,841
Comprehensive income (loss)	$(79,372)	$(80,145)	$43,185
(A) Components of net revenue:			
License fees	$28,308	$43,709	$56,640
Service revenue	127,904	162,487	202,202
	$156,212	$206,196	$258,842
(B) Components of cost of revenue:			
License fees	$8,012	$8,538	$11,689
Service revenue	68,369	70,553	92,042
	$76,381	$79,091	$103,731

See accompanying notes to consolidated financial statements.

REALNETWORKS, INC. AND SUBSIDIARIES
CONSOLIDATED STATEMENTS OF CASH FLOWS
(In thousands)

	Years Ended December 31,		
	2014	2013	2012
Cash flows from operating activities:			
Net income (loss)	$(71,815)	$(58,990)	$44,841
Adjustments to reconcile net income (loss) to net cash provided by (used in) operating activities:			
Depreciation and amortization	11,959	18,748	16,959
Stock-based compensation	5,204	7,468	8,123
Loss (gain) on asset disposal	—	—	2,509
Equity in net loss of Rhapsody	4,452	6,268	