REALNETWORKS INC
Form 10-Q
August 08, 2013

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

FORM 10-Q

(Mark One)

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

For the Quarterly Period Ended June 30, 2013

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)
2601 Elliott Avenue, Suite 1000 Seattle, Washington	98121
(Address of principal executive offices)	(Zip Code)

(206) 674-2700
(Registrant's telephone number, including area code)

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

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

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	ý
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 ý

The number of shares of the registrant's Common Stock outstanding as of July 31, 2013 was 35,666,571.

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PART I. FINANCIAL INFORMATION
Item 1. Financial Statements
REALNETWORKS, INC. AND SUBSIDIARIES
UNAUDITED CONDENSED CONSOLIDATED BALANCE SHEETS
(In thousands, except per share data)

	June 30, 2013	December 31, 2012
ASSETS		
Current assets:		
Cash and cash equivalents	$129,210	$163,198
Short-term investments	107,536	108,216
Trade accounts receivable, net of allowances	25,700	30,754
Deferred costs, current portion	485	825
Deferred tax assets, current	3,845	2,869
Prepaid expenses and other current assets	9,452	17,002
Total current assets	276,228	322,864
Equipment, software, and leasehold improvements, at cost:		
Equipment and software	94,231	98,041
Leasehold improvements	22,740	22,767
Total equipment, software, and leasehold improvements, at cost	116,971	120,808
Less accumulated depreciation and amortization	92,342	91,492
Net equipment, software, and leasehold improvements	24,629	29,316
Restricted cash equivalents and investments	10,000	10,000
Equity method investment	15,344	19,204
Available for sale securities	36,156	34,334
Other assets	3,262	3,153
Deferred costs, non-current portion	1,300	531
Deferred tax assets, net, non-current portion	1,534	4,911
Other intangible assets, net	9,783	3,275
Goodwill	15,984	6,309
Total assets	$394,220	$433,897
LIABILITIES AND SHAREHOLDERS’ EQUITY		
Current liabilities:		
Accounts payable	$18,600	$19,013
Accrued and other current liabilities	47,972	57,530
Deferred revenue, current portion	7,987	8,675
Total current liabilities	74,559	85,218
Deferred revenue, non-current portion	191	169
Deferred rent	441	2,250
Deferred tax liabilities, net, non-current portion	3,194	432
Other long-term liabilities	492	3,100
Total liabilities	78,877	91,169
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 35,658 shares in 2013 and 35,324 shares in 2012	36	35

Additional paid-in capital	607,140	603,770
Accumulated other comprehensive loss	(27,151)	(26,540)
Retained deficit	(264,682)	(234,537)
Total shareholders’ equity	315,343	342,728
Total liabilities and shareholders’ equity	$394,220	$433,897

See accompanying notes to unaudited condensed consolidated financial statements.

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

	Quarters Ended June 30,		Six Months Ended June 30,	
	2013	2012	2013	2012
Net revenue (A)	$49,850	$65,526	$106,643	$132,490
Cost of revenue (B)	19,519	25,962	40,025	53,389
Gross profit	30,331	39,564	66,618	79,101
Sale of patents and other technology assets, net of costs (See Note 1)	—	117,933	—	116,353
Operating expenses:				
Research and development	14,993	16,028	30,244	33,846
Sales and marketing	19,269	22,694	40,403	46,490
General and administrative	8,691	13,068	18,637	26,344
Restructuring and other charges	816	1,539	2,198	3,148
Lease exit and related charges	3,066	—	3,066	—
Total operating expenses	46,835	53,329	94,548	109,828
Operating income (loss)	(16,504)	104,168	(27,930)	85,626
Other income (expenses):				
Interest income, net	179	225	826	869
Gain (loss) on sale of equity and other investments, net	—	3,078	—	3,078
Equity in net loss of Rhapsody investment	(1,347)	(2,114)	(3,580)	(2,482)
Other income (expense), net	(137)	(49)	(28)	1,426
Total other income (expenses), net	(1,305)	1,140	(2,782)	2,891
Income (loss) before income taxes	(17,809)	105,308	(30,712)	88,517
Income tax expense (benefit)	662	24,311	(567)	24,535
Net income (loss)	$(18,471)	$80,997	$(30,145)	$63,982
Basic net income (loss) per share	$(0.52)	$2.33	$(0.85)	$1.85
Diluted net income (loss) per share	$(0.52)	$2.32	$(0.85)	$1.83
Shares used to compute basic net income (loss) per share	35,455	34,752	35,399	34,620
Shares used to compute diluted net income (loss) per share	35,455	34,900	35,399	34,914
Comprehensive income (loss):				
Unrealized investment holding gains (losses)	$(1,622)	$(12,061)	$1,015	$(3,567)
Foreign currency translation adjustments, net of reclassification adjustments	(388)	(1,852)	(1,626)	(2,236)
Total other comprehensive income (loss)	(2,010)	(13,913)	(611)	(5,803)
Net income (loss)	(18,471)	80,997	(30,145)	63,982
Comprehensive income (loss)	$(20,481)	$67,084	$(30,756)	$58,179
(A) Components of net revenue:				
License fees	$10,162	$14,224	$22,991	$29,180
Service revenue	39,688	51,302	83,652	103,310
	$49,850	$65,526	$106,643	$132,490
(B) Components of cost of revenue:				
License fees	$2,161	$2,645	$4,315	$5,917
Service revenue	17,358	23,317	35,710	47,472
	$19,519	$25,962	$40,025	$53,389

See accompanying notes to unaudited condensed consolidated financial statements.

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

	Six Months Ended June 30, 2013	2012
Cash flows from operating activities:		
Net income (loss)	$(30,145)	$63,982
Adjustments to reconcile net income (loss) to net cash provided by (used in) operating activities:		
Depreciation and amortization	9,874	8,162
Stock-based compensation	4,058	4,065
Equity in net loss of Rhapsody	3,580	2,482
Deferred income taxes, net	(1,668)	22,496
Gain on sale of patent and other technology assets, net of costs	—	(116,353)
Gain on sale of equity and other investments, net	—	(3,078)
Realized translation gain	(35)	(1,611)
Other	51	(79)
Net change in certain operating assets and liabilities:		
Trade accounts receivable	5,355	2,691
Prepaid expenses and other assets	6,749	(1,144)
Accounts payable	(92)	4,013
Accrued and other liabilities	(10,612)	(3,067)
Net cash provided by (used in) operating activities	(12,885)	(17,441)
Cash flows from investing activities:		
Purchases of equipment, software, and leasehold improvements	(3,181)	(4,989)
Proceeds from sale of patents and other technology assets, net of costs	—	116,353
Proceeds from sale of equity and other investments	—	4,165
Purchases of short-term investments	(70,647)	(18,637)
Proceeds from sales and maturities of short-term investments	71,327	13,970
Decrease (increase) in restricted cash equivalents and investments, net	—	(5)
Acquisitions of businesses, net of cash acquired	(16,107)	—
Net cash provided by (used in) investing activities	(18,608)	110,857
Cash flows from financing activities:		
Proceeds from issuance of common stock (stock options and stock purchase plan)	392	1,221
Tax payments from shares withheld upon vesting of restricted stock	(800)	(884)
Payment of contingent consideration	(828)	—
Net cash provided by (used in) financing activities	(1,236)	337
Effect of exchange rate changes on cash and cash equivalents	(1,259)	(546)
Net increase (decrease) in cash and cash equivalents	(33,988)	93,207
Cash and cash equivalents, beginning of period	163,198	106,333
Cash and cash equivalents, end of period	$129,210	$199,540
Supplemental disclosure of cash flow information:		
Cash received from income tax refunds	$8,100	$149
Cash paid for income taxes	$2,147	$1,575
Non-cash investing activities:		
Increase (decrease) in accrued purchases of equipment, software, and leasehold improvements	$483	$1,189

See accompanying notes to unaudited condensed consolidated financial statements.

REALNETWORKS, INC. AND SUBSIDIARIES
NOTES TO UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS
Quarters and Six Months Ended June 30, 2013 and 2012
Note 1. Description of Business and Summary of Significant Accounting Policies
Description of Business. RealNetworks, Inc. and subsidiaries is a leading global provider of network-delivered digital media applications and services that make it easy to manage, play and share digital media. The Company also develops and markets software products and services that enable the creation, distribution and consumption of digital media, including audio and video.
Inherent in our business are various risks and uncertainties, including a limited history of certain of our product and service offerings. RealNetworks' success will depend on the acceptance of our technology, products and services and the ability to generate related revenue.
In this Quarterly Report on Form 10-Q for the quarter ended June 30, 2013 (10-Q or Report), RealNetworks, Inc. and Subsidiaries is referred to as “RealNetworks”, the “Company”, “we”, “us”, or “our”.
Basis of Presentation. The unaudited condensed consolidated financial statements include the accounts of RealNetworks and its wholly-owned subsidiaries. Intercompany balances and transactions have been eliminated in consolidation.
The unaudited condensed consolidated financial statements reflect all adjustments, consisting only of normal, recurring adjustments that, in the opinion of the Company’s management, are necessary for a fair presentation of the results of operations for the periods presented. Operating results for the quarter and six months ended June 30, 2013 are not necessarily indicative of the results that may be expected for any subsequent period or for the year ending December 31, 2013. Certain information and disclosures normally included in financial statements prepared in conformity with accounting principles generally accepted in the United States of America (GAAP) have been condensed or omitted pursuant to the rules and regulations of the Securities and Exchange Commission (SEC). These unaudited condensed consolidated financial statements should be read in conjunction with the audited consolidated financial statements and related notes included in our Annual Report on Form 10-K for the year ended December 31, 2012 (the 10-K).
Use of Estimates. The preparation of financial statements in conformity with GAAP requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities, disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates. In addition, current economic conditions may require the use of additional estimates, and certain estimates we make are subject to a greater degree of uncertainty as a result of the current economic conditions.
Reportable Segments. In the first quarter of 2013 we reorganized the management of our businesses and as a result, we changed our reportable segments. See Note 17, Segment Information, for details.
Accumulated Other Comprehensive Income (Loss). The components of accumulated other comprehensive income (loss), net of any applicable tax, were as follows (in thousands):

	June 30, 2013	December 31, 2012
Unrealized gains on investments, net of tax effects of $(129) and $(846) at June 30, 2013 and December 31, 2012, respectively	$27,700	$26,685
Foreign currency translation adjustments	(54,851)	(53,225)
Accumulated other comprehensive income (loss)	$(27,151)	$(26,540)

In the three months ended March 31, 2012 we liquidated the investment in certain of our foreign entities and recorded a net pre-tax gain of $1.6 million in Other income (expense), net, in the consolidated statement of operations upon the reclassification of the same amount of cumulative foreign exchange translation adjustment from accumulated other comprehensive income (loss) on the balance sheet. The reclassification adjustment had no related income tax expense or benefit. There were no reclassification adjustments or related tax effects related to foreign exchange translation amounts in the three months ended June 30, 2012.

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There were no material reclassification adjustments or related tax effects related to foreign exchange translation amounts in the six months ended June 30, 2013.

In the three months ended June 30, 2012 we realized a pre-tax gain of $2.1 million in the consolidated statement of operations, within Gain (loss) on sale of equity and other investments, net, related to the sale of a portion of the equity shares we hold in LoEn Entertainment, Inc., with the same amounts reclassified from accumulated other comprehensive income (loss) on the balance sheet. The reclassification adjustment had no related income tax expense or benefit. There were no reclassification adjustments or related tax effects related to unrealized gains on investments in the three months ended March 31, 2012, or in the six months ended June 30, 2013.

For the three months ended June 30, 2013 we recorded income tax expense of $0.9 million and for the six months ended June 30, 2013 we recorded an income tax benefit of $0.7 million related to unrealized gains (losses) on investment securities, and recognized the corresponding amount as an increase or decrease to accumulated other comprehensive income.

2012 Sale of Patents and Other Technology Assets to Intel Corporation. In the second quarter of 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 Corporation (Intel). The entire $120.0 million of cash proceeds we received, net of certain direct costs incurred, was recorded as a gain on our statement of operations in the quarter ending June 30, 2012, since the patent assets and other technology had a net book value of zero. The gain recognized of $116.4 million in the six months ended June 30, 2012 was net of related direct costs for the sale transaction totaling $3.6 million incurred in the first and second quarters of 2012.

Note 2. Recent Accounting Pronouncements

There have been no recent accounting pronouncements or changes in accounting pronouncements during the six months ended June 30, 2013 to be implemented that are of significance or potential significance to RealNetworks.

Note 3. Stock-Based Compensation

Total stock-based compensation expense recognized in our consolidated statements of operations includes amounts related to stock options, restricted stock units, and employee stock purchase plans and was as follows (in thousands):

	Quarters Ended June 30,		Six Months Ended June 30,	
	2013	2012	2013	2012
Total stock-based compensation expense	$2,020	$1,722	$4,058	$4,065

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

	Quarters Ended June 30,		Six Months Ended June 30,	
	2013	2012	2013	2012
Expected dividend yield	0 %	0 %	0 %	0 %
Risk-free interest rate	0.52 %	0.55 %	0.55 %	0.65 %
Expected life (years)	5.4	3.8	4.3	3.8
Volatility	48 %	58 %	48 %	58 %

The total stock-based compensation amounts for 2013 and 2012 disclosed above are recorded in their respective line items within operating expenses in the consolidated statement of operations. No stock-based compensation was capitalized as part of the cost of an asset as of June 30, 2013 or December 31, 2012. As of June 30, 2013, we had $7.1 million of total unrecognized compensation cost, net of estimated forfeitures, related to stock awards. The unrecognized compensation cost is expected to be recognized over a weighted-average period of approximately 3 years.

Note 4. Rhapsody Joint Venture

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RealNetworks initially formed in 2007 a joint venture with MTV Networks, a division of Viacom International Inc. (MTVN), to own and operate a business-to-consumer digital audio music service known as Rhapsody. Prior to March 31, 2010, we held a 51% interest in Rhapsody and MTVN owned the remaining 49%. On March 31, 2010, restructuring transactions involving Rhapsody were completed, and as a result, effective March 31, 2010 RealNetworks owned approximately 47% of Rhapsody. Subsequent to the restructuring transaction, we account for our investment in Rhapsody using the equity method of accounting for investments.

As of June 30, 2013 we owned approximately 45% of the issued and outstanding stock of Rhapsody.

RealNetworks continues to provide certain operational transition services to Rhapsody. These transition services are expected to be completed in 2013, and are discussed further in Footnote 18, Related Party Transactions.

We recorded our share of losses of Rhapsody of $1.3 million and $3.6 million for the quarter and six months ended June 30, 2013, respectively. Our share of losses of Rhapsody for the quarter and six months ended June 30, 2012 were $2.1 million and $2.5 million, respectively.

The carrying value of our Rhapsody investment was $15.3 million as of June 30, 2013.

Summarized financial information for Rhapsody, which represents 100% of their financial information (in thousands):

	Quarters Ended June 30,		Six Months Ended June 30,	
	2013	2012	2013	2012
Net revenue	$34,679	$37,809	$68,641	$72,979
Gross profit	8,767	9,879	16,612	19,491
Net loss	(4,375)	(4,537)	(9,191)	(5,607)

Note 5. Fair Value Measurements

We measure certain financial assets at fair value on a recurring basis, including cash equivalents, short-term investments, and equity investments of publicly traded companies. The fair value of these financial assets was determined based on three levels of inputs:

- Level 1: Quoted prices in active markets for identical assets or liabilities
- Level 2: Directly or indirectly observed inputs for the asset or liability, including quoted prices for similar assets or liabilities in active markets and quoted prices for identical or similar assets or liabilities in markets that are not active
- Level 3: Significant unobservable inputs that reflect our own estimates of assumptions that market participants would use

Items Measured at Fair Value on a Recurring Basis

The following table presents information about our financial assets that have been measured at fair value on a recurring basis as of June 30, 2013 and December 31, 2012, and indicates the fair value hierarchy of the valuation inputs utilized to determine such fair value (in thousands).

	Fair Value Measurements as of June 30, 2013			
	Total	Level 1	Level 2	Level 3
Cash equivalents:				
Money market funds	$12,788	$2	$12,786	$—
Corporate notes and bonds	63,490	—	63,490	—
Short-term investments:				
Corporate notes and bonds	73,135	—	73,135	—
U.S. government agency securities	34,401	34,276	125	—
Restricted cash equivalents and investments	10,000	—	10,000	—
Equity investments in publicly traded securities	36,156	36,156	—	—
Total	$229,970	$70,434	$159,536	$—

	Fair Value Measurements as of December 31, 2012			
	Total	Level 1	Level 2	Level 3
Cash equivalents:				
Money market funds	$10,680	$—	$10,680	$—
Corporate notes and bonds	81,235	—	81,235	—
Short-term investments:				
Corporate notes and bonds	65,502	—	65,502	—
U.S. government agency securities	42,714	42,113	601	—
Restricted cash equivalents and investments	10,000	—	10,000	—
Equity investments in publicly traded securities	34,334	34,334	—	—
Total	$244,465	$76,447	$168,018	$—

Our equity investments in publicly traded companies consist of J-Stream Inc., a Japanese media services company, and LoEn Entertainment, Inc., a Korean digital music distribution company. These equity investments are accounted for as available for sale. The aggregate cost basis of these securities totaled $8.6 million as of June 30, 2013 and $8.6 million at December 31, 2012.

Items Measured at Fair Value on a Non-recurring Basis

Certain of our assets and liabilities are measured at estimated fair value on a non-recurring basis, using Level 3 inputs. These instruments are subject to fair value adjustments only in certain circumstances (for example, when there is evidence of impairment). During the six months ended June 30, 2013 and 2012, we did not record any impairments on those assets required to be measured at fair value on a non-recurring basis.

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

Cash and cash equivalents, short-term investments, and restricted cash equivalents and investments as of June 30, 2013, consisted of the following (in thousands):

	Amortized Cost	Estimated Fair Value
Cash and cash equivalents:		
Cash	$52,932	$52,932
Money market mutual funds	12,788	12,788
Corporate notes and bonds	63,490	63,490
Total cash and cash equivalents	129,210	129,210
Short-term investments:		
Corporate notes and bonds	73,143	73,135
U.S. government agency securities	34,390	34,401
Total short-term investments	107,533	107,536
Total cash, cash equivalents and short-term investments	$236,743	$236,746
Restricted cash equivalents and investments	$10,000	$10,000

Cash and cash equivalents, short-term investments, and restricted cash equivalents and investments as of December 31, 2012 consisted of the following (in thousands):

	Amortized Cost	Estimated Fair Value
Cash and cash equivalents:		
Cash	$71,283	$71,283
Money market mutual funds	10,680	10,680
Corporate notes and bonds	81,237	81,235
Total cash and cash equivalents	163,200	163,198

Short-term investments:		
Corporate notes and bonds	65,426	65,502
U.S. Government agency securities	42,693	42,714
Total short-term investments	108,119	108,216
Total cash, cash equivalents, and short-term investments	$271,319	$271,414
Restricted cash equivalents and investments	$10,000	$10,000

Restricted cash equivalents and investments amounts as of June 30, 2013, and December 31, 2012 relate to cash and investments pledged as collateral against letters of credit in connection with lease agreements.

Realized gains or losses on sales of short-term investment securities for the quarters and six months ended June 30, 2013 and 2012 were not significant. Gross unrealized gains and gross unrealized losses on short-term investment securities as of June 30, 2013 and December 31, 2012 were not significant.

Investments with remaining contractual maturities of five years or less are classified as short-term because the investments are marketable and highly liquid and we have the ability to utilize them for current operations. Contractual maturities of short-term investments as of June 30, 2013 (in thousands):

	Estimated Fair Value
Within one year	$82,261
Between one year and five years	25,275
Total short-term investments	$107,536

Note 7. Allowance for Doubtful Accounts Receivable and Sales Returns

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

	Allowance For Doubtful Accounts Receivable	Sales Returns
Balances, December 31, 2012	$1,010	$653
Addition (reduction) to allowance	42	(10)
Amounts written off	(48)	(16)
Foreign currency translation	(17)	—
Balances, June 30, 2013	$987	$627

One customer accounted for 12% of trade accounts receivable and one other customer accounted for 11% of trade accounts receivable, as of June 30, 2013. No one customer accounted for more than 10% of trade accounts receivable as of December 31, 2012.

One customer accounted for approximately 13%, or $6.5 million, and 14% or $15.1 million, of consolidated revenue during the quarter and six months ended June 30, 2013, respectively. The revenue from this customer is reflected in our RealPlayer Group and Games segments. One customer accounted for approximately 11%, or $5.6 million, of consolidated revenue during the quarter ended June 30, 2013, in our Mobile Entertainment segment. No one customer accounted for more than 10% of consolidated revenue during the quarter and six months ended June 30, 2012.

Note 8. Other Intangible Assets

Other intangible assets (in thousands):

	Gross Amount	Accumulated Amortization	Net
Customer relationships	$30,441	$27,775	$2,666
Developed technology	25,876	23,439	2,437
Patents, trademarks and tradenames	7,869	3,369	4,500
Service contracts and other	5,500	5,320	180
Total other intangible assets, June 30, 2013	$69,686	$59,903	$9,783

In the quarter ended June 30, 2013, we acquired 100% of the voting interests in Slingo, Inc., a social casino games company based in the U.S., for total cash consideration of $15.6 million. The tangible and intangible assets and liabilities recognized are reported within the Games segment. The identifiable intangible assets associated with the acquisition totaled $8.0 million. Of this total, $4.5 million is related to tradenames and trademarks determined to have indefinite useful lives and will be evaluated annually in our fourth quarter for impairment, or more frequently, if circumstances indicate an impairment may exist. The remaining $3.5 million includes developed game technology and existing customer relationships with finite lives, and will be amortized over their useful lives. We recorded a net deferred tax liability of $2.7 million related to the intangible assets acquired. Goodwill totaling $9.8 million was recorded, representing the intangible assets that do not qualify for separate recognition for accounting purposes, primarily related to the assembled workforce and expected synergies in the rapidly growing social casino games market. The goodwill is not deductible for income tax purposes. For the six months ended June 30, 2013, the amount of revenue and income (loss) before income taxes from this acquired business was not significant.

Note 9. Goodwill

Changes in goodwill (in thousands):

Balance, December 31, 2012	$6,309
Increases due to current year acquisitions	10,026
Effects of foreign currency translation	(351)
Balance, June 30, 2013	$15,984

Goodwill by segment (in thousands):

	June 30, 2013
RealPlayer Group	$580
Mobile Entertainment	688
Games	14,716
Total goodwill	$15,984

See Note 8, Other Intangible Assets for details on our acquisition of Slingo, a social casino games business, in the quarter ended June 30, 2013.

Note 10. Accrued and Other Current Liabilities

Accrued and other current liabilities (in thousands):

	June 30, 2013	December 31, 2012
Royalties and other fulfillment costs	$17,697	$19,435
Employee compensation, commissions and benefits	10,379	13,368
Sales, VAT and other taxes payable	8,353	10,959
Deferred tax liabilities—current	432	3,894
Accrued lease exit and related charges	4,209	2,463
Other	6,902	7,411

Total accrued and other current liabilities	$47,972	$57,530

Note 11. Restructuring Charges

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Restructuring and other charges in 2013 and 2012 consist of costs associated with the ongoing reorganization of our business operations and focus on aligning our operating expenses with our revenue profile. The expense amounts in both years relate primarily to severance costs due to workforce reductions.

In the third quarter of 2012 we announced we would be eliminating approximately 160 positions worldwide. This action has been concluded as of the end of the second quarter of 2013. For the quarter and six months ended June 30, 2013 we recorded $0.8 million and $2.2 million, respectively, of restructuring charges for employee separation costs related to this action and for other actions taken in 2013.

Details of restructuring charges for the six months ended June 30, 2013 and 2012 are in the table below. The amount accrued at June 30, 2013 for employee separation includes costs for those employees who were separated in the quarter ended June 30, 2013 and are expected to be paid out in the quarter ended September 30, 2013. The amount accrued for contract assignment is expected to be paid out by the end of 2013.

For details on costs associated with the termination of our Seattle headquarters lease see Note 12, Lease exit and related charges.

Restructuring charges by type of cost (in thousands):

	Employee Separation Costs	Asset Disposal Expense and Other	Total
Costs incurred and charged to expense for the six months ended June 30, 2013	$1,818	380	$2,198
Costs incurred and charged to expense for the six months ended June 30, 2012	$3,148	—	$3,148

Changes to the accrued restructuring cost liability (in thousands):

	By Type of Cost		
	Employee Separation Costs	Contract Assignment Costs	Total
Accrued liability as of December 31, 2012	$731	$1,700	$2,431
Costs incurred and charged to expense for the six months ended June 30, 2013	1,818	—	1,818
Cash payments	(2,348)	—	(2,348)
Accrued liability as of June 30, 2013	$201	$1,700	$1,901

Note 12. Lease Exit and Related Charges

As a result of the reduction in use of RealNetworks' office space, primarily in our corporate headquarters in Seattle, Washington, and certain other locations, losses have been recognized representing rent and contractual operating expenses over the remaining life of the leases, and related write-downs of leasehold improvements to their estimated fair value.

In the second quarter of 2013, we entered into a new lease in a new location for our Seattle headquarters and concurrently entered into an amendment to our current headquarters office lease that provides for an early termination of such lease.

The new Seattle building lease is for an initial term of 11 years and is estimated to commence on August 15, 2013. We have the option to extend the lease for two additional five-year terms, with certain increases in base rent.

The amendment to our current headquarters office lease provides for an early termination of such lease effective in three stages, with the termination of a majority of the premises taking place on August 31, 2013, and the final stage being complete by December 31, 2013. Prior to the execution of the amendment, the lease had been scheduled to expire in September 2014. In

connection with the early termination of the lease, we will pay the landlord termination fees totaling approximately $6.6 million in 2013. In the second quarter of 2013, we paid the landlord $3.2 million in termination fees.
Changes to accrued lease exit and related charges (in thousands):

Accrued loss December 31, 2012	$4,213	
Additions and adjustments to the lease exit charges accrual, including sublease income estimate revision	1,275	
Less amounts paid, net of sublease amounts	(1,279	)
Accrued loss June 30, 2013 (included in Accrued and other current liabilities)	$4,209	

Note 13. Income Taxes

As of June 30, 2013, there have been no material changes to RealNetworks' uncertain tax positions disclosures as provided in Note 14 of the 10-K. We do not anticipate that our total unrecognized tax benefits will significantly change within the next twelve months.

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.

Note 14. Earnings (Loss) Per Share

Basic net income (loss) per share (EPS) is computed by dividing net income (loss) by the weighted average number of common shares outstanding during the period. Diluted EPS is computed by dividing net income (loss) by the weighted average number of common and dilutive potential common shares outstanding during the period. Basic and diluted EPS (in thousands, except per share amounts):

	Quarters Ended June 30,			Six Months Ended June 30,		
	2013		2012	2013		2012
Net income (loss) available to common shareholders	$(18,471	)	$80,997	$(30,145	)	$63,982
Weighted average common shares outstanding used to compute basic EPS	35,455		34,752	35,399		34,620
Dilutive effect of stock based awards	—		148	—		294
Weighted average common shares outstanding used to compute diluted EPS	35,455		34,900	35,399		34,914
Basic EPS	$(0.52	)	$2.33	$(0.85	)	$1.85
Diluted EPS	$(0.52	)	$2.32	$(0.85	)	$1.83

During the quarter and six months ended June 30, 2013, respectively, 4.3 million and 4.3 million of potentially issuable shares from stock awards were excluded from the calculation of diluted EPS because of their antidilutive effect.

During the quarter and six months ended June 30, 2012, respectively, 5.7 million and 5.8 million of potentially issuable shares from stock awards were excluded from the calculation of diluted EPS because of their antidilutive effect.

Note 15. Commitments and Contingencies

Commitments. See Note 12, Lease exit and related charges, for details on office lease commitments.

Litigation. On July 3, 2012, a lawsuit was filed against us by VoiceAge Corporation in the Supreme Court of the State of New York. VoiceAge asserts that we have breached our payment obligations under the terms of a patent license agreement between us and VoiceAge in respect of distribution of specified codec technology and is seeking a material amount of damages. We have removed the proceedings to New York federal court. Discovery commenced on January 4, 2013 and closed on May 15, 2013. In June 2013, VoiceAge submitted a motion for summary judgment; the Supreme Court of the State of New York denied the motion for summary judgment on August 5, 2013. We dispute VoiceAge's allegations and the magnitude of the claimed damages, and, because we are in the early stages of this litigation and due to the uncertainties inherent in this matter, we are unable to estimate the range of possible loss that could result from this litigation.

On October 28, 2011 and November 1, 2011, respectively, two lawsuits were filed by Callertone Innovations, LLC in the U.S. District Court for the District of Delaware. The first lawsuit was against T-Mobile USA, Inc. and the second lawsuit was against MetroPCS Wireless, Inc. and MetroPCS Communications, Inc., which we collectively refer to as MetroPCS. The lawsuits allege that T-Mobile and MetroPCS, respectively, infringe Callertone's patents by providing ringback tone services. We agreed to indemnify each of T-Mobile and MetroPCS against the claims based on an indemnity that is claimed to be owed by us. The respective complaint was served on T-Mobile on January 16, 2012 and on MetroPCS on January 14, 2012. We filed our answers to each complaint on April 9, 2012. In each matter, we dispute the plaintiff's allegations regarding both the validity of its patents and its claims of infringement against T-Mobile and MetroPCS, respectively. A claims construction hearing is scheduled for September 6, 2013. Because we are in the early stages of this litigation and due to the uncertainties inherent in these matters, we are unable to estimate the range of possible loss that could result from this litigation.

On April 25, 2007, a lawsuit was filed by Greenville Communications, LLC in Greenville, Mississippi against a number of cell phone carriers, including our partners T-Mobile USA, Inc. and Alltel Corporation, alleging that they infringe its patents by providing ringback tone services. We agreed to indemnify T-Mobile and Alltel against the claims based on an indemnity that is claimed to be owed by us. On August 27, 2007, our motion to transfer this matter to the U.S. District Court for the District of New Jersey was granted. The parties briefed claims construction, but the case was subsequently stayed pending reexamination of the patents at issue. On December 10, 2009, the U.S. Patent and Trademark Office issued notice of its intent to issue reexamination certificates for the patents in suit. The District Court lifted the stay on the litigation on January 29, 2010 and discovery resumed. On September 28, 2011, the District Court held a claims construction hearing, and on May 10, 2012, the District Court issued a non-infringement judgment that was favorable to us and the other defendants. On December 4, 2012, Greenville appealed the claims construction order and the judgment, and the defendants filed a reply brief on January 28, 2013. On May 17, 2013, the U.S. Court of Appeals for the Federal Circuit affirmed the judgment of non-infringement of the District Court. Greenville has filed a petition for re-hearing with the U.S. Court of Appeals. Due to the uncertainties inherent in this matter, we are unable to estimate the range of possible loss that could result from this litigation.

From time to time we are, and expect to continue to be, subject to legal proceedings, governmental investigations and claims in the ordinary course of business, including employment claims, contract-related claims, and claims of alleged infringement of third-party patents, trademarks and other intellectual property rights. These claims, including those described above, even if not meritorious, could force us to spend significant financial and managerial resources. We are not aware of any other legal proceedings or claims that we believe will have, individually or taken together, a material adverse effect on our business, prospects, financial condition or results of operations. However, we may incur substantial expenses in defending against third-party claims. In addition, 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. In the event of a determination adverse to us, we may incur substantial monetary liability, and/or be required to change our business practices. Either of these could have a material adverse effect on our consolidated financial statements.

Note 16. Guarantees

In the ordinary course of business, RealNetworks is subject to potential obligations for standard indemnification and warranty provisions that are contained within many of our customer license and service agreements, as described below.

Warranty provisions contained within our customer license and service agreements are generally consistent with those prevalent in our industry. The duration of our product warranties generally does not exceed 90 days following delivery of our products. Nearly all of our carrier contracts obligate us to indemnify our carrier customer for certain liabilities that may be incurred by them.

We do not maintain accruals for warranty-related obligations as we do not have a history of incurring such losses. We have, however, received claims for indemnification from certain of our carrier customers. See Note 15, Commitments and Contingencies, for a discussion of these indemnification claims.

As discussed in Note 1, Description of Business and Summary of Significant Accounting Policies, we sold certain patents and other technology assets to Intel in the second quarter of 2012. We have specific obligations to indemnify

Intel for breaches of the representations and warranties that we made and covenants that we agreed to in the asset purchase agreement executed in connection with the transaction, and for certain potential future intellectual property infringement claims brought by third parties against Intel. The amount of any potential liabilities related to our indemnification obligations will not be determined until a claim has been made, but we are obligated to indemnify Intel up to the amount of the gross purchase price that we received in the sale.

Note 17. Segment Information

In the first quarter of 2013 we reorganized the management of our businesses and as a result, we now report the following three segments: (1) RealPlayer Group, which includes sales of our RealPlayer media player software and related products, such as the distribution of third party software products, advertising on RealPlayer websites, and sales of RealPlayer Plus software licenses to consumers, sales of intellectual property licenses, and consumer subscriptions such as SuperPass; (2) Mobile Entertainment, which includes our SaaS services, systems integration, and professional services to mobile carriers, and sales of technology licenses of our software products such as Helix; and (3) Games, which includes all our games-related businesses, including sales of games licenses, online games subscription services, advertising on games sites and social network sites, microtransactions from online and social games, and sales of mobile games.

In addition, we now also allocate certain corporate expenses which are directly attributable to supporting the business to our reportable segments, rather than retaining those expenses in our corporate segment. These 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 retained in aggregate in our corporate segment. All restructuring and lease exit and related charges are included in the corporate segment. In 2012, the sale of patent and other technology assets, net of costs, was included in the corporate segment. The historical financial information presented has been recast to reflect the new segments and the new corporate expense presentation.

RealNetworks reports three reportable segments based on factors such as how we manage our operations and how our Chief Operating Decision Maker reviews results. Our Chief Operating Decision Maker is considered to be the CEO Staff (CEOS), which includes the interim Chief Executive Officer, Chief Financial Officer, President, Executive Vice President, General Counsel and certain Senior Vice Presidents. The CEOS reviews financial information presented on both a consolidated basis and on a business segment basis, accompanied by certain disaggregated information about products and services, geographical regions and corporate expenses for purposes of making decisions and assessing financial performance. The accounting policies used to derive segment results are the same as those described in Note 1, Description of Business and Summary of Significant Accounting Policies, in the 10-K.

Segment results for the quarters and six months ended June 30, 2013 and 2012 (in thousands):

RealPlayer Group

	Quarters Ended June 30,		Six Months Ended June 30,	
	2013	2012	2013	2012
Revenue	$18,383	$22,158	$40,766	$44,239
Cost of revenue	4,409	4,727	9,720	9,291
Gross profit	13,974	17,431	31,046	34,948
Operating expenses	14,001	12,792	30,207	28,767
Operating income (loss)	$(27)	$4,639	$839	$6,181

Mobile Entertainment

	Quarters Ended June 30,		Six Months Ended June 30,	
	2013	2012	2013	2012
Revenue	$18,592	$26,005	$39,087	$51,780
Cost of revenue	11,170	14,875	22,002	30,353
Gross profit	7,422	11,130	17,085	21,427
Operating expenses	8,412	13,851	17,523	28,655
Operating income (loss)	$(990)	$(2,721)	$(438)	$(7,228)

Games

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	Quarters Ended June 30,		Six Months Ended June 30,	
	2013	2012	2013	2012
Revenue	$12,875	$17,363	$26,790	$36,471
Cost of revenue	3,381	5,630	7,181	12,343
Gross profit	9,494	11,733	19,609	24,128
Operating expenses	11,755	13,801	23,607	27,939
Operating income (loss)	$(2,261)	$(2,068)	$(3,998)	$(3,811)

Corporate

	Quarters Ended June 30,		Six Months Ended June 30,	
	2013	2012	2013	2012
Cost of revenue	$559	$730	$1,122	$1,402
Sale of patents and other technology assets, net of costs	—	117,933	—	116,353
Operating expenses	12,667	12,885	23,211	24,467
Operating income (loss)	$(13,226)	$104,318	$(24,333)	$90,484

Our customers consist primarily of consumers and corporations located in the U.S., Europe and various foreign countries. Revenue by geographic region (in thousands):

	Quarters Ended June 30,		Six Months Ended June 30,	
	2013	2012	2013	2012
United States	$21,463	$28,614	$49,486	$60,428
Europe	9,272	14,339	20,528	30,551
Rest of the world	19,115	22,573	36,629	41,511
Total net revenue	$49,850	$65,526	$106,643	$132,490

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

	June 30, 2013	December 31, 2012
United States	$42,264	$27,915
Europe	1,921	2,350
Rest of the world	6,211	8,635
Total long-lived assets	$50,396	$38,900

Note 18. Related Party Transactions

Transactions with Rhapsody. See Note 4, Rhapsody Joint Venture, for details on the 2010 restructuring transaction involving Rhapsody. Subsequent to the restructuring transaction, we are obligated to provide Rhapsody with certain support services. These support services are expected to be completed in 2013. The support services include information technology and limited operational support provided directly to Rhapsody. The amount of these and other support service costs were based on various measures depending on the service provided, including vendor fees, an allocation of fixed costs and time employees spend on providing services to Rhapsody. RealNetworks allocates the cost of providing these support services and records such allocation as a reduction to the related expense in the period for which it was incurred. During the quarter and six months ended June 30, 2013, we charged Rhapsody $0.3 million

and $0.4 million, respectively, for the support services. During the quarter and six months ended June 30, 2012, we charged Rhapsody $0.2 million and $0.5 million, respectively, for the support services.
Transactions with LoEn Entertainment, Inc. In 2008 RealNetworks acquired at market prices common shares of LoEn Entertainment, Inc., whose shares are traded on the Korean Securities Dealers Automated Quotations. We currently own

approximately 9% of the outstanding shares of LoEn. Our investment in LoEn is treated as an equity investment of a public company and is marked-to-market each period with resulting unrealized gains or losses recognized in accumulated other comprehensive income/loss. During the quarter and six months ended June 30, 2013, we recorded revenue from LoEn of $5.6 million and $10.5 million, respectively. During the quarter and six months ended June 30, 2012, we recorded revenue from LoEn of $4.1 million and $8.0 million, respectively. Revenue consisted primarily of sales of application service provider services, which include sales of ringback tones, music on demand, video on demand, and inter carrier messaging services. Associated with these transactions, we also recorded accounts receivable of $2.2 million as of June 30, 2013. Accounts payable and cost of revenue associated with LoEn as of and for the periods ended June 30, 2013 and 2012 were nominal.

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

This Quarterly Report on Form 10-Q and the documents incorporated herein by reference contain forward-looking statements that have been made pursuant to the provisions of the Private Securities Litigation Reform Act of 1995. These forward-looking statements are based on current expectations, estimates, and projections about RealNetworks’ industry, products, management’s beliefs, and certain assumptions made by management. Words such as “anticipates,” “expects,” “intends,” “plans,” “believes,” “seeks,” “estimates,” and similar expressions are intended to identify forward-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 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 of new and enhanced products, services and technologies across our businesses;
- 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 in Item 1A of Part II entitled “Risk Factors.” RealNetworks undertakes no obligation to update publicly any forward-looking statements as a result of new information, future events or otherwise, unless required by law. Readers should, however, carefully review the risk factors included in other reports or documents filed by RealNetworks from time to time with the Securities and Exchange Commission, particularly the Quarterly Reports on Form 10-Q and any Current Reports on Form 8-K.

Overview

In the first quarter of 2013 we reorganized the management of our businesses and as a result, we now report the following 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, such as the distribution of third party software products, advertising on RealPlayer websites, and sales of RealPlayer Plus software licenses to consumers, sales of intellectual property licenses, and consumer subscriptions such as SuperPass. The Mobile Entertainment business primarily includes revenue from SaaS services, systems integration, and professional services to mobile carriers, and sales of technology licenses of our software products such as Helix. The Games business primarily includes revenue from sales of games licenses, online games subscription services, advertising on games sites and social network sites, microtransactions from online and social games, and sales of mobile games.

In addition, we now also 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. The allocation of these costs to the business units will increase accountability for financial and operational performance within each of our reportable segments. RealNetworks' most significant expenses relate to cost of revenue, compensating employees, and selling and marketing our products and services. The historical financial information presented has been recast to reflect the new segments and the new corporate expense presentation.

In the quarter and six months ended June 30, 2013, our consolidated revenue declined by $15.7 million and $25.8 million, respectively, compared to the same periods in 2012. The decline for the quarter was due to a decline of $7.4 million in Mobile Entertainment revenue, a decline of $4.5 million in Games revenue, and a $3.8 million decline in RealPlayer Group revenue. For the year to date period the decline was primarily due to a decline of $12.7 million in Mobile Entertainment revenue and a decline of $9.7 million in Games revenue.

Our SaaS business within Mobile Entertainment continues to be 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. In our Games segment and in the general games market, 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. However, the revenue we currently generate from social games is not a significant portion of our Games revenue.

We are continuing to invest in each of our businesses. For example, 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 will be incremental costs for investment in new products over the next year, which will directly impact our operating income (loss) before taxes.

We continue to focus on aligning our operating expenses with our revenue profile. The actions we initiated in the third quarter of 2012 to eliminate approximately 160 positions worldwide contributed significantly to the $6.5 million and $15.3 million decline in our total operating expenses for the quarter and six months ended June 30, 2013, respectively, compared to the same periods in 2012. In addition, on May 2, 2013, we entered into a new lease in a new location for our Seattle headquarters and concurrently negotiated an early termination to our current headquarters office lease. This action will meaningfully reduce our future annual facilities cost.

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

	Quarters Ended June 30,				Six months ended June 30,			
	2013	2012	$ Change	% Change	2013	2012	$ Change	% Change
Total revenue	$49,850	$65,526	$(15,676)	(24)%	$106,643	$132,490	$(25,847)	(20)%
Cost of revenue	19,519	25,962	(6,443)	(25)%	40,025	53,389	(13,364)	(25)%
Gross profit	30,331	39,564	(9,233)	(23)%	66,618	79,101	(12,483)	(16)%
Gross margin	61%	60%			62%	60%		
Sale of patent assets and other technology assets, net of costs	—	117,933	(117,933)	(100)%	—	116,353	(116,353)	(100)%
Operating expenses	46,835	53,329	(6,494)	(12)%	94,548	109,828	(15,280)	(14)%
Operating income (loss)	$(16,504)	$104,168	$(120,672)	(116)%	$(27,930)	$85,626	$(113,556)	(133)%

In the second quarter of 2013, our total consolidated revenue declined by $15.7 million, compared with the year-earlier period. The reduction in revenue resulted from a decline of $7.4 million in our Mobile Entertainment segment, a decline of $4.5 million in our Games segment, and a $3.8 million decline in RealPlayer Group revenue, due to the factors described above. Gross margin increased to 61% from 60% for the year earlier quarter as a result of a higher proportion of lower margin revenue in the prior year, in addition to lower personnel and related costs in the second quarter of 2013 that resulted from our ongoing expense alignment efforts. Operating expenses decreased by $6.5 million in the quarter ended June 30, 2013, compared with the prior year primarily due to reductions in personnel and related costs that resulted from our ongoing expense alignment efforts. Excluding restructuring and lease exit and related charges, operating expenses decreased by $8.8 million in the quarter ended June 30, 2013, compared to the same period of the prior year.

For the six months ended June 30, 2013, our total consolidated revenue declined by $25.8 million, compared with the year-earlier period. The reduction in revenue primarily resulted from a decline of $12.7 million in our Mobile Entertainment segment and a decline of $9.7 million in our Games segment, due to the factors described above. Gross margin increased to 62% from 60% for the year earlier quarter as a result of a higher proportion of lower margin revenue in the prior year, in addition to lower personnel and related costs in the first half of 2013 that resulted from our ongoing expense alignment efforts. Operating expenses decreased by $15.3 million in the six months ended June 30, 2013, compared with the prior year primarily due to reductions in personnel and related costs that resulted from our ongoing expense alignment efforts. Excluding

restructuring and lease exit and related charges, operating expenses decreased by $17.4 million in the six months ended June 30, 2013, compared to the same period of the prior year.
The 2012 gain from the sale of patents and other technology assets to Intel is net of certain direct expenses incurred for the sale transaction.
See “Segment Operating Results” below for more information and discussion regarding changes in the operating results for each of our reporting segments.
Segment Operating Results
RealPlayer Group
The RealPlayer Group segment primarily generates revenue and incurs costs from sales of RealPlayer and its related products, such as the distribution of third party software products, advertising on RealPlayer websites, and sales of RealPlayer Plus software licenses to consumers, sales of intellectual property licenses, and consumer subscriptions such as SuperPass.
RealPlayer Group segment results of operations were as follows (dollars in thousands):

	Quarters Ended June 30,				Six months ended June 30,			
	2013	2012	$ Change	% Change	2013	2012	$ Change	% Change
Revenue	$18,383	$22,158	$(3,775)	(17)%	$40,766	$44,239	$(3,473)	(8)%
Cost of revenue	4,409	4,727	(318)	(7)%	9,720	9,291	429	5%
Gross profit	13,974	17,431	(3,457)	(20)%	31,046	34,948	(3,902)	(11)%
Gross margin	76%	79%			76%	79%		
Operating expenses	14,001	12,792	1,209	9%	30,207	28,767	1,440	5%