

REALNETWORKS INC
Form 10-K/A
May 31, 2007

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

**Amendment No. 1
Form 10-K/A**

(Mark One)

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

For the Fiscal Year Ended December 31, 2006

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

(State of incorporation)

91-1628146

(I.R.S. Employer Identification Number)

2601 Elliott Avenue, Suite 1000

Seattle, Washington

(Address of principal executive offices)

98121

(Zip Code)

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

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 LLC

Preferred Share Purchase Rights

The NASDAQ Stock Market LLC

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

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

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

Indicate by check mark 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.

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

Large accelerated filer Accelerated filer Non-accelerated filer

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

The aggregate market value of the Common Stock held by non-affiliates of the registrant was \$1,137,327,118 on June 30, 2006, based on the closing price of the Common Stock on that date, as reported on the Nasdaq Global Select Market.⁽¹⁾

The number of shares of the registrant's Common Stock outstanding as of May 15, 2007 was 154,328,479.

DOCUMENTS INCORPORATED BY REFERENCE

Portions of the registrant's Proxy Statement relating to the registrant's 2007 Annual Meeting of Shareholders to be held on or about June 25, 2007 are incorporated by reference into Part III of this Report.

- (1) Excludes shares held of record on that date by directors, executive officers and 10% shareholders of the registrant. Exclusion of such shares should not be construed to indicate that any such person directly or indirectly possesses the power to direct or cause the direction of the management of the policies of the registrant.

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EXPLANATORY NOTE

RealNetworks, Inc. (also referred to as the Company, we, or our) is filing this Amendment No. 1 (the Amendment No. 1) to our Form 10-K for the fiscal year ended December 31, 2006 (the Form 10-K), originally filed with the Securities and Exchange Commission on March 1, 2007, for the purpose of:

amending the cover page to indicate that our preferred share purchase rights are registered pursuant to Section 12(b) of the Securities Exchange Act of 1934, as amended,

amending the cover page to indicate that shares of our common stock and our preferred share purchase rights are registered on the NASDAQ Stock Market LLC,

correcting a typographical error in the date of the Report of Independent Registered Public Accounting Firm relating to management s assessment of internal control over financial reporting appearing in Item 9A of the Form 10-K to reflect the report date of February 26, 2007,

revising the cover page and Items 10, 11, 12, 13 and 14 of Part III to reflect the date of our 2007 annual meeting of shareholders will be June 25, 2007, and

revising Items 10, 11, 13 and 14 of Part III to conform the description of the sections of the Proxy Statement for RealNetworks Annual Meeting of Shareholders scheduled to be held on or around June 25, 2007 incorporated by reference into these Items to what appears in such Proxy Statement filed with the Securities and Exchange Commission on May 15, 2007.

We are also updating the signature page, the Exhibit Index in Item 15 of Part IV and appearing after the signature page and Exhibits 23.1, 31.1, 31.2, 32.1 and 32.2.

Pursuant to Rule 12b-15 under the Securities Exchange Act of 1934, as amended, the complete text of Item 8 of Part II, as amended, and Items 10, 11, 12, 13 and 14 of Part III, as amended, is set forth below. The information set forth in our financial statements and the footnotes thereto in this Amendment No. 1 has not been modified or updated in any way from the information in our financial statements and the related footnotes included in the Form 10-K. This Amendment No. 1 speaks as of the original filing date of the Form 10-K and reflects only the changes to the cover page, Item 8 of Part II, Items 10, 11, 12, 13 and 14 of Part III and Item 15 of Part IV discussed above. No other information included in the Form 10-K, including the information set forth in Part I, has been modified or updated in any way.

Table of Contents**PART II.****Item 8. Financial Statements and Supplementary Data****REALNETWORKS, INC. AND SUBSIDIARIES****CONSOLIDATED BALANCE SHEETS****(In thousands, except per share data)**

	December 31,	
	2006	2005
ASSETS		
Current assets:		
Cash and cash equivalents	\$ 525,232	\$ 651,971
Short-term investments	153,688	129,356
Trade accounts receivable, net of allowances for doubtful accounts and sales returns of \$2,490 in 2006 and \$2,973 in 2005	65,751	16,721
Deferred costs, current portion	1,643	
Deferred tax assets, net, current portion	891	54,204
Prepaid expenses and other current assets	21,990	11,933
Total current assets	769,195	864,185
Equipment, software, and leasehold improvements, at cost:		
Equipment and software	83,587	56,402
Leasehold improvements	29,665	27,964
Total equipment, software, and leasehold improvements	113,252	84,366
Less accumulated depreciation and amortization	65,509	51,228
Net equipment, software, and leasehold improvements	47,743	33,138
Restricted cash equivalents	17,300	17,300
Equity investments	22,649	46,163
Other assets	5,148	2,397
Deferred tax assets, net, non-current portion	27,150	19,147
Other intangible assets, net of accumulated amortization of \$16,637 in 2006 and \$9,850 in 2005	105,109	7,337
Goodwill	309,122	123,330
Total assets	\$ 1,303,416	\$ 1,112,997

LIABILITIES AND SHAREHOLDERS EQUITY

Current liabilities:		
Accounts payable	\$ 52,097	\$ 11,397
Accrued and other liabilities	104,328	112,340
Deferred revenue, current portion	24,137	25,021
Accrued loss on excess office facilities, current portion	4,508	4,623
Total current liabilities	185,070	153,381

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Deferred revenue, non-current portion	3,440	276
Accrued loss on excess office facilities, non-current portion	9,993	13,393
Deferred rent	4,331	4,018
Deferred tax liabilities, net, non-current portion	27,076	
Convertible debt	100,000	100,000
Other long-term liabilities	3,740	196
Total liabilities	333,650	271,264
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 1,000,000 shares; issued and outstanding 163,278 shares in 2006 and 166,037 shares in 2005	162	166
Additional paid-in capital	791,108	805,067
Deferred stock-based compensation		(19)
Accumulated other comprehensive income	23,485	26,724
Retained earnings	155,011	9,795
Total shareholders' equity	969,766	841,733
Total liabilities and shareholders' equity	\$ 1,303,416	\$ 1,112,997

See accompanying notes to consolidated financial statements.

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

	Years Ended December 31,		
	2006	2005	2004
Net revenue ^(A)	\$ 395,261	\$ 325,059	\$ 266,719
Cost of revenue ^(B)	124,108	98,249	92,207
Loss on content agreement			4,938
Gross profit	271,153	226,810	169,574
Operating expenses:			
Research and development	77,386	70,731	52,066
Sales and marketing	165,602	130,515	96,779
General and administrative	57,332	50,697	31,538
Loss on excess office facilities	738		866
Subtotal operating expenses	301,058	251,943	181,249
Antitrust litigation (benefit) expenses, net	(220,410)	(422,500)	11,048
Total operating expenses (benefit)	80,648	(170,557)	192,297
Operating income (loss)	190,505	397,367	(22,723)
Other income (expenses):			
Interest income, net	37,622	14,511	4,452
Gain on sale of equity investments	2,286	19,330	
Equity in net income (loss) of investments	326	(1,068)	(4,351)
Impairment of equity investments	(3,116)	(266)	(450)
Other income (expenses)	130	(331)	597
Other income, net	37,248	32,176	248
Income (loss) before income taxes	227,753	429,543	(22,475)
Income taxes	(82,537)	(117,198)	(522)
Net income (loss)	\$ 145,216	\$ 312,345	\$ (22,997)

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Basic net income (loss) per share	\$ 0.90	\$ 1.84	\$ (0.14)
Diluted net income (loss) per share	\$ 0.81	\$ 1.70	\$ (0.14)
Shares used to compute basic net income (loss) per share	160,973	169,986	168,907
Shares used to compute diluted net income (loss) per share	179,281	184,161	168,907
Comprehensive income (loss):			
Net income (loss)	\$ 145,216	\$ 312,345	\$ (22,997)
Unrealized gain (loss) on investments:			
Unrealized holding (losses) gains, net of tax	(14,399)	17,864	7,557
Adjustments for gains reclassified to net income (loss)		(4,052)	(53)
Foreign currency translation gains (losses)	11,160	(1,677)	(99)
Comprehensive income (loss)	\$ 141,977	\$ 324,480	\$ (15,592)
(A) Components of net revenue:			
License fees	\$ 90,684	\$ 80,785	\$ 71,706
Service revenue	304,577	244,274	195,013
	\$ 395,261	\$ 325,059	\$ 266,719
(B) Components of cost of revenue:			
License fees	\$ 37,089	\$ 33,770	\$ 28,206
Service revenue	87,019	64,479	64,001
	\$ 124,108	\$ 98,249	\$ 92,207

See accompanying notes to consolidated financial statements.

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

	Years Ended December 31,		
	2006	2005	2004
Cash flows from operating activities:			
Net income (loss)	\$ 145,216	\$ 312,345	\$ (22,997)
Adjustments to reconcile net income (loss) to net cash provided by operating activities:			
Depreciation and amortization	20,980	16,243	14,643
Stock-based compensation	18,151	128	695
Deferred income taxes	54,986	107,208	
Impairment of equity investments	3,116	266	450
Loss on disposal of property, software, and leasehold improvements	276		
Excess tax benefit from stock option exercises	(39,183)		
Accrued loss on excess office facilities	(3,515)	(6,244)	(4,799)
Gain on sale of equity investments	(2,286)	(19,330)	(561)
Equity in net (income) loss of investments	(326)	1,068	4,351
Accrued loss on content agreement		(2,917)	2,917
Other	97	804	1,592
Changes in certain assets and liabilities, net of acquisitions:			
Trade accounts receivable	(7,962)	(1,479)	(3,314)
Prepaid expenses and other current assets	(3,126)	(3,409)	1,258
Accounts payable	4,276	44	3,577
Accrued and other liabilities	(21,800)	59,826	12,810
Deferred revenue	2,020	(3,800)	(3,599)
 Net cash provided by operating activities	 170,920	 460,753	 7,023
 Cash flows from investing activities:			
Purchases of equipment, software, and leasehold improvements	(13,808)	(13,782)	(10,018)
Purchases of short-term investments	(204,841)	(153,491)	(293,560)
Sales and maturities of short-term investments	180,973	168,358	324,512
Purchases of intangible and other assets		(1,125)	(4,839)
Decrease (increase) in restricted cash equivalents		2,851	(198)
Proceeds from sale of equity investments	2,286	19,530	572
Purchases of cost based investments	(834)	(647)	
Cash used in acquisitions, net of cash acquired	(257,841)	(14,705)	(10,477)
 Net cash (used in) provided by investing activities	 (294,065)	 6,989	 5,992
 Cash flows from financing activities:			
	54,929	20,361	8,489

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Net proceeds from sales of common stock under employee stock purchase plan and exercise of stock options			
Repayment of long-term note payable		(648)	
Excess tax benefit from stock option exercises	39,183		
Repurchase of common stock	(98,876)	(54,321)	
Net cash (used in) provided by financing activities	(4,764)	(34,608)	8,489
Effect of exchange rate changes on cash	1,170	(589)	(106)
Net (decrease) increase in cash and cash equivalents	(126,739)	432,545	21,398
Cash and cash equivalents, beginning of year	651,971	219,426	198,028
Cash and cash equivalents, end of year	\$ 525,232	\$ 651,971	\$ 219,426
Supplemental disclosure of cash flow information:			
Cash paid during the year for income taxes	\$ 16,487	\$ 149	\$ 415
Supplemental disclosure of non-cash investing and financing activities:			
Accrued acquisition consideration	\$ 2,000	\$	\$
Payable for repurchase of common stock	\$	\$ 5,116	\$
Common stock and options to purchase common stock issued in business combinations	\$	\$	\$ 20,901

See accompanying notes to consolidated financial statements.

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REALNETWORKS, INC. AND SUBSIDIARIES
CONSOLIDATED STATEMENTS OF SHAREHOLDERS' EQUITY
(In thousands)

	Common Shares	Common Stock Amount	Additional Paid-In Capital	Notes Receivable from Shareholders	Deferred Stock-Based Compensation	Accumulated Other Comprehensive Income	Retained Earnings (Deficit)	Total Shareholders' Equity
Balances, December 31, 2003	164,197	\$ 164	\$ 639,369	\$ (58)	\$ (620)	\$ 7,184	\$ (279,553)	\$ 366,486
Common stock issued for:								
Exercise of stock options and employee stock purchase plan	3,423	4	8,485					8,489
Business combination	3,007	3	20,898		(222)			20,679
Notes receivable retired	(8)		(41)	48				7
Amortization of deferred stock compensation					695			695
Shares issued for director payments	7		41					41
Unrealized gain on investments, net of income tax						7,557		7,557
Adjustments for gains reclassified to net loss						(53)		(53)
Translation adjustment						(99)		(99)
Net loss							(22,997)	(22,997)
Balances, December 31, 2004	170,626	171	668,752	(10)	(147)	14,589	(302,550)	380,805
Common stock issued for exercise of stock options and employee stock purchase plan	4,056 (8,642)	3 (8)	20,358 (54,313)					20,361 (54,321)

Common shares repurchased				
Notes receivable retired	(18)	(26)	10	(16)
Amortization of deferred stock compensation				128
Shares issued for director payments	15	91		91
Unrealized gain on investments, net of income tax				17,864
Adjustments for gains reclassified to net income				17,864