

GRAVITY Co., Ltd.  
Form 20-F  
June 30, 2009

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**As filed with the Securities and Exchange Commission on June 30, 2009**

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

**FORM 20-F**

(Mark One)

- REGISTRATION STATEMENT PURSUANT TO SECTION 12(b) OR (g) OF THE SECURITIES EXCHANGE ACT OF 1934**
  - or**
- ANNUAL REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934**  
**For the fiscal year ended December 31, 2008**
  - or**
- TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934**
  - or**
- SHELL COMPANY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934**

**Commission file number: 000-51138  
GRAVITY CO., LTD.**

*(Exact name of registrant as specified in its charter)*

**N/A**

*(Translation of registrant's name into English)*

**The Republic of Korea**

*(Jurisdiction of incorporation or organization)*

Nuritkum Square Business Tower 15F, 1605 Sangam-Dong, Mapo-Gu, Seoul 121-270, Korea  
*(Address of principal executive offices)*

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*Chief Financial Officer*

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Telephone: 82-2-2132-7000

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*(Name, Telephone, E-mail and/or Facsimile number and Address of Company Contact Person)*

Securities registered or to be registered pursuant to Section 12(b) of the Act:

Title of Each Class	Name of Each Exchange on Which Registered
Common stock, par value Won 500 per share* American depositary shares, each representing one-fourth of a share of common stock	Nasdaq Global Market

\* Not for trading, but only in connection with the listing of American depositary shares on the Nasdaq Global Market pursuant to the requirements of the Securities and Exchange Commission.

**Securities registered or to be registered pursuant to Section 12(g) of the Act: None**

**Securities for which there is a reporting obligation pursuant to Section 15(d) of the Act: None**

Indicate the number of outstanding shares of each of the issuer's classes of capital or common stock as of the close of the period covered by the annual report: Shares, par value Won 500: 6,948,900

Indicated by check mark if the registrant is a well-known seasoned issuer, as defined in Rule 405 of the Securities Act. Yes  No

If this report is an annual or transition report, indicate by check mark if the registrant is not required to file reports pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934. 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 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  No

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 which basis of accounting the registrant has used to prepare the financial statements included in this filing:

U.S. GAAP  International Financial Reporting Standards as used by the International Accounting Standards Board  Other

If "Other" has been checked in response to the previous question, indicate by check mark which financial statement item the registrant has elected to follow: Item 17  Item 18

If this is an annual report, indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act). Yes  No

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**CERTAIN DEFINED TERMS**

Unless the context otherwise requires, references in this annual report on Form 20-F, or annual report to:

ADRs are to the American depositary receipts that evidence our ADSs;

ADSs are to our American depositary shares, each of which represents one-fourth of a share of our common stock;

Government is to the government of The Republic of Korea;

Gravity, the Company, we, us, our, or our company are to Gravity Co., Ltd. and, except as otherwise indicated or required by context, our subsidiaries;

Korea or the Republic are to The Republic of Korea;

China or the PRC are to the People's Republic of China (excluding Taiwan, Hong Kong and Macau);

Taiwan or the ROC are to Taiwan, the Republic of China;

US\$, U.S. dollars, US dollars, or Dollars are to the currency of the United States of America;

Won, Korean Won, ~~₩~~ or W, are to the currency of The Republic of Korea;

Chinese Yuan or CNY are to the currency of China;

Japanese Yen or JPY are to the currency of Japan;

NT dollar is to the currency of Taiwan; and

Thai Baht or THB are to the currency of Thailand.

For your convenience, this annual report contains translations of certain Won amounts into U.S. dollars at the noon buying rate as quoted by the Federal Reserve Bank of New York for Won in effect on April 30, 2009, which was Won 1,277.00 to US\$1.00. No assurance is given that any Won or dollar amounts could have been, or could be converted into dollars or Won as the case may be at such rate, or any other rate, or at all.

Discrepancies in tables between totals and sums of the amounts listed are due to rounding.

**FORWARD-LOOKING STATEMENTS**

This annual report for the year ended December 31, 2008 contains forward-looking statements, as defined in Section 27A of the U.S. Securities Act of 1933, as amended, or the Securities Act, and Section 21E of the U.S. Securities Exchange Act of 1934, as amended, or the Exchange Act. The forward-looking statements are based on our current expectations, assumptions, estimates and projections about us and our industry, and are subject to various risks and uncertainties. Generally, these forward-looking statements can be identified by the use of forward-looking terminology such as anticipate, believe, considering, depends, estimate, expect, intend, plan, planning

predict, project, continue and variations of these words, similar expressions, or that certain events, actions or results will, may, might, should, would or could occur, be taken or be achieved.

Forward-looking statements include, but are not limited to, the following:

future prices of and demand for our products;

future earnings and cash flow;

estimated development and commercial launch schedule of our games in development;

our ability to attract new customers and retain existing customers;

the expected growth of the Korean and worldwide online gaming industry;

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the effect that economic, political or social conditions in Korea have on the revenue generated from our online game product and our results of operations;

the effect that the current global financial crisis and global economic recession will or may have on our business prospects, financial condition and results of operations; and

our future business development and prospects, results of operations and financial condition.

We caution you not to place undue reliance on any forward-looking statement each of which involves risks and uncertainties. Although we believe that the assumptions on which our forward-looking statements are based are reasonable, any of those assumptions could prove to be inaccurate, and as a result, the forward-looking statements based on those assumptions could be incorrect. All forward-looking statements are based on our management's current expectation, assumptions, estimates and projections of future events and are subject to a number of factors that could cause actual results to differ materially from those described in the forward-looking statements. Risks and uncertainties associated with our business include, but are not limited to, risks related to changes in the regulatory environment; technology changes; potential litigation and governmental actions; changes in the competitive environment; changes in customer preference and popular culture and trends, including the online gaming culture; political changes; recent global economic events including, but not limited to, the significant downturn in the global economic and financial markets and the tightening of the global credit markets, changes in business and economic conditions, fluctuations in foreign exchange rates, fluctuations in prices of our products, decreasing consumer confidence and slowing of economic growth generally, and other risks and uncertainties that are more fully described under the heading "Risk Factors" in this annual report, and elsewhere in this annual report. In light of these and other uncertainties, you should not conclude that we will necessarily achieve any plans and objectives or projected financial results referred to in any of the forward-looking statements. We undertake no obligation to update or revise any forward-looking statement to reflect future events or circumstances.

**Table of Contents****PART I****ITEM 1. IDENTITY OF DIRECTORS, SENIOR MANAGEMENT AND ADVISERS**

Not applicable.

**ITEM 2. OFFER STATISTICS AND EXPECTED TIMETABLE**

Not applicable.

**ITEM 3. KEY INFORMATION****ITEM 3.A. Selected Financial Data**

You should read the selected financial data below in conjunction with the financial statements and the related notes included elsewhere in this annual report. The selected financial data as of and for the years ended December 31, 2006, 2007 and 2008 are derived from our audited financial statements and related notes thereto are included elsewhere in this annual report. Our historical results do not necessarily indicate results expected for any future periods. Our financial statements are prepared in accordance with accounting principles generally accepted in the United States of America, or U.S. GAAP.

**As of and for the Years Ended December 31,**  
**2004            2005            2006            2007            2008            2008(1)**  
**(In millions of Won and thousands of US\$, except share and per share data,**  
**operating data and percentage)**  
**(Unaudited)**

**Statement of operations**

## Revenues:

Online games subscription revenue	₩ 16,253	₩ 11,249	₩ 8,420	₩ 9,405	₩ 12,576	US \$ 9,848
Online games royalties and license fees	45,101	37,375	26,123	24,698	30,110	23,579
Mobile games	376	1,664	3,840	4,063	6,882	5,389
Character merchandising, animation and other revenue	2,696	3,096	2,580	2,063	3,602	2,821
Total revenues	64,426	53,384	40,963	40,229	53,170	41,637
Cost of revenues	10,116	16,038	17,746	19,479	27,772	21,748
Gross profit	54,310	37,346	23,217	20,750	25,398	19,889
Operating expenses:						
Selling, general and administrative	13,660	30,795	27,555	29,030	23,489	18,394
Research and development	2,029	9,219	9,239	5,761	2,145	1,680

Impairment losses on investments				8,619		
Litigation charges		4,648				
Proceeds from a former chairman due to fraud		(4,947)				
Gain in disposal of assets held for sale		(1,081)				
Operating income (loss)	38,621	(2,668)	(12,197)	(22,660)	(236)	(185)
Other income (expense), net	(4,879)	(787)	2,265	3,441	6,030	4,722
Income (loss) before income tax expenses, minority interest, and equity in loss of related joint venture and partnership	33,742	(3,455)	(9,932)	(19,219)	5,794	4,537
Income tax expenses (benefit)	5,406	(817)	12,069	2,916	3,379	2,646
Income (loss) before minority interest and equity in loss of related joint venture and partnership	28,336	(2,638)	(22,001)	(22,135)	2,415	1,891

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	As of and for the Years Ended December 31,						
2004	2005	2006	2007	2008	2008(1)		
(In millions of Won and thousands of US\$, except share and per share data, operating data and percentage)							(Unaudited)
Minority interest	(17)	(2)	7	40	69	54	
Equity in loss of related joint venture and partnership	296	394	1,106	1,026	5,119	4,009	
Income (loss) before cumulative effect of change in accounting principle	28,057	(3,030)	(23,114)	(23,201)	(2,773)	(2,172)	
Cumulative effect of change in accounting principle, net of tax			849				
Net income (loss)	₩ 28,057	₩ (3,030)	₩ (22,265)	₩ (23,201)	₩ (2,773)	US \$ (2,172)	
Earnings (loss) per share:							
Before cumulative effect of change in accounting principle	₩ 5,056	₩ (445)	₩ (3,326)	₩ (3,339)	₩ (399)	US \$ (0.31)	
Cumulative effect of change in accounting principle(2)			122				
Basic and diluted per share	₩ 5,056	₩ (445)	₩ (3,204)	₩ (3,339)	₩ (399)	US \$ (0.31)	
Basic and diluted per ADS		(111)	(801)	(835)	(100)	(0.08)	
Weighted average number of shares outstanding (basic and diluted)	5,548,900	6,803,147	6,948,900	6,948,900	6,948,900	6,948,900	
<b>Balance sheet data:</b>							

Cash and cash equivalents	₩	16,405	₩	25,874	₩	35,314	₩	53,588	₩	53,168	US \$	41,635
Total current assets		46,868		109,428		88,203		72,667		72,550		56,813
Property and equipment, net		14,760		11,863		8,472		7,195		5,226		4,092
Total assets		68,644		144,857		122,561		96,921		95,935		75,125
Total current liabilities		12,221		19,448		16,192		10,106		8,397		6,575
Total liabilities		18,209		24,073		24,419		21,377		19,327		15,134
Total shareholders equity		50,435		120,762		98,113		75,476		76,471		59,884
<b>Selected operating data and financial ratios:</b>												
Gross profit margin(3)		84.3%		70.0%		56.7%		51.6%		47.8%		47.8%
Operating profit margin(4)		59.9		(5.0)		(29.8)		(56.3)		(0.4)		(0.4)
Net profit margin(5)		43.5		(5.7)		(54.4)		(57.7)		(5.2)		(5.2)

*Notes:*

- (1) For convenience only, the Won amounts are expressed in U.S. dollars at the rate of Won 1,277.0 to US\$1.00, the noon buying rate as quoted by the Federal Reserve Bank of New York in effect on April 30, 2009.
- (2) FAS 123(R) was adopted in 2006.
- (3) Gross profit margin for each period is calculated by dividing gross profit by total revenues for each such period.
- (4) Operating profit margin for each period is calculated by dividing operating income (loss) by total revenues for each such period.
- (5) Net profit margin for each period is calculated by dividing net income (loss) by total revenues for each such period.

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The following table sets forth information concerning the noon buying rate for the years 2004 through 2008 and for each month during the previous six months through June 26, 2009, expressed in Won per US dollar.

<b>Period</b>	<b>At End of Period</b>	<b>Average Rate(1)</b>	<b>High</b>	<b>Low</b>
2004	₩ 1,035.1	₩ 1,139.3	₩ 1,195.1	₩ 1,035.1
2005	1,010.0	1,023.2	1,059.8	997.0
2006	930.0	950.1	1,002.9	913.7
2007	935.8	928.0	950.2	903.2
2008	1,262.0	1,098.7	1,507.9	935.2
December 2009	1,262.0	1,361.6	1,479.0	1,257.4
January	1,380.0	1,354.4	1,391.5	1,292.3
February	1,532.8	1,439.6	1,532.8	1,368.7
March	1,372.3	1,449.6	1,570.1	1,334.8
April	1,277.0	1,332.1	1,378.3	1,277.0
May	1,249.0	1,254.4	1,277.0	1,232.9
June (through June 26, 2009)	1,278.3	1,257.7	1,285.1	1,232.1

Source: Federal Reserve Bank of New York

*Note:*

- (1) The average rates for the annual periods were calculated based on the average noon buying rate on the last day of each month during the period. The average rates for the monthly periods were calculated based on the average noon buying rate of each day of the month.

**ITEM 3.B. Capitalization and Indebtedness**

Not applicable.

**ITEM 3.C. Reasons for the Offer and Use of Proceeds**

Not applicable.

**ITEM 3.D. Risk Factors****RISKS RELATING TO OUR BUSINESS**

*We currently depend on one online game product, Ragnarok Online, for most of our revenues which may have a limited lifespan.*



Most of our revenues have been and are currently derived from a single online game product, Ragnarok Online, which was commercially introduced in August 2002 and currently commercially offered in 38 countries and markets. We derived Won 38,949 million (US\$30,500 thousand) in revenues from Ragnarok Online in 2008 and Won 31,114 million in revenues from Ragnarok Online in 2007, representing approximately 73.3% and 77.3% of our total revenues in 2008 and 2007, respectively.

Ragnarok Online has been in the market for nearly seven years and has reached maturity in most of our principal markets. The life cycle of an online game generally lasts from four to seven years and reaches its peak popularity within the first two years of its introduction, after which, usage gradually stabilizes and begins to decrease over time. The number of users of Ragnarok Online worldwide reached its peak in the first quarter of 2005 and has continued to decline since such time. Our failure to maintain, improve, update or enhance Ragnarok Online in a timely manner or successfully introduce it in attractive new markets is likely to lead to a continual decline in

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Ragnarok Online's user base and subscription revenues and royalties. This could lead to a decline in our overall revenues, which would materially and adversely affect our business, financial condition and results of operations.

***If we are unable to consistently and timely develop, acquire, license, launch, market or operate commercially successful online games in addition to Ragnarok Online, our business, financial condition and results of operations may be materially and adversely affected.***

In order to grow our revenues and net income, we must develop, acquire, license, launch, market or operate commercially successful online games in addition to Ragnarok Online that will retain our existing users and attract new users. In addition to Ragnarok Online, we currently offer three other massively multiplayer online role playing games, Requiem, Emil Chronicle Online and R.O.S.E. Online and one casual online game, Pucca Racing. We are currently conducting open beta testing of a massively multiplayer online role playing game sequel to Ragnarok Online, Ragnarok Online II, and are in the process of developing a new massively multiplayer online game, Ice Age Online, with a third-party developer.

None of our other online games to date have proven to be as commercially successful as Ragnarok Online. We stopped offering, in September 2008, two casual online games, Love Forty and TV Boyz, which were offered on STYLIA, our casual online game portal site, which we no longer operate. We also stopped offering a massively multiplayer online role playing game, Time N Tales, in March 2009 as the games did not prove to be popular to users. We also stopped developing two other casual online games, W Baseball and Bodycheck Online, in May 2008 as the results of our open beta testing indicated that the two games would not be popular. In addition, we have experienced significant delays in and cost overruns related to the launch of some of our online games. For example, although we have been conducting open beta testing of Ragnarok Online II since May 2007 and had indicated our plan to release Ragnarok Online II at various times over the past few years, the launch of this game has been significantly delayed on a number of occasions for a variety of reasons, including as a result of technical difficulties and corrective actions taken in response to market feedback during the testing and development phase. While no assurance can be given that we will be able to meet our current anticipated launch date, we currently intend to launch Ragnarok Online II in the first half of 2010. Due to the continued delay in the launch of Ragnarok Online II, certain licensees of Ragnarok Online II have delayed remitting royalty payments otherwise payable for Ragnarok Online. Any continued delay in the launch schedule of Ragnarok Online II could result in financial losses, including termination of certain license agreements, which could damage our reputation and have a material adverse effect on our business, prospects, financial condition and results of operation.

In addition, no assurance can be given that when launched, Ragnarok Online II will gain market acceptance and popularity. The success of Ragnarok Online II will be subject to many factors, including the quality, uniqueness and playability of the game and the launch by our competitors of other games that may gain more market acceptance than Ragnarok Online II. See ITEM 3.D. RISK FACTORS RISKS RELATING TO OUR BUSINESS As we introduce new games, we face the risk that a significant number of users of our existing games may migrate to our new games without any net gains in the overall user base or overall improvement to our total revenues.

***As we introduce new games, we face the risk that a significant number of users of our existing games may migrate to our new games without any net gains in the overall user base or overall improvement to our total revenues.***

We expect that as we introduce new games, a certain number of our existing users will migrate from our old games to the new games. If the level of migration by our users from our existing games to such new games is significantly higher than our expectations, and the net gains in new users is significantly lower than our expectations, then our growth and profitability could be materially and adversely affected.

In particular, there is a high degree of uncertainty about the potential impact of the commercial launch of Ragnarok Online II on the user base of Ragnarok Online. While we believe that the game environment and the overall game experience of Ragnarok Online II will be meaningfully different from those of Ragnarok Online, we cannot assure you that the overall user base will grow and that the net migration away from Ragnarok Online will not be significant and detrimental to our total revenues.

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***We depend on our overseas licensees for a substantial portion of our revenues and rely on them to distribute, market and operate our games, and comply with applicable laws and government regulations.***

In markets other than Korea, the United States, Canada, Australia, New Zealand, Russia, CIS countries, France and Belgium, in which we or our subsidiaries directly publish our games, we license our games to overseas operators or distributors for license fees and royalty payments based on a percentage of revenues generated from our games in such markets. Overseas license fees and royalty payments represented 73.7% of our total revenues in 2008 and 72.4% of our total revenue in 2007. In particular, we are heavily dependent on two licensees for a significant portion of our revenues. In 2008, 50.2% of our total revenues was derived from GungHo Online Entertainment, Inc., or GungHo, our licensee in Japan, which became our majority shareholder in April 2008, and 3.5% of our total revenues was from Soft-World International Corporation, our licensee in Taiwan and Hong Kong. Deterioration in our relationships with licensees or material changes in the terms of our licenses with such licensees will likely have a material adverse effect on our business, prospects, financial condition and results of operations. In addition, as we are heavily dependent on certain licensees, deterioration or any adverse developments in the operations, including changes in senior management, of our overseas licensees may materially and adversely affect our business, financial condition and results of operations.

Further, our overseas licensees generally have the exclusive right to distribute our games in their respective markets for a term of two or three years and may also operate or publish other online games developed or offered by our competitors under the license arrangements, while we may not be able to easily terminate the license agreements as the agreements do not specify particular financial or performance criteria that need to be met by our licensees. If our overseas licensees devote greater time and resources to marketing their proprietary games or those of our competitors than ours, we may not be able to terminate our license agreements or enter into a new license agreement with a different licensee. Also a failure to satisfy our obligation to provide technical and other consulting services to the licensees under the license agreement may negatively affect user satisfaction and loyalty and hinder our licensees efforts to gain market share, which may lead the licensees to focus their attention on our competitors' games or request modifications to our licensing agreements, and which may, in certain circumstances, result in our licensees terminating their relationship with us.

Our overseas licensees are responsible for remitting royalty payments to us based on a percentage of sales from our games after deducting certain expenses. Some licensees may be allowed to deduct certain expenses before calculating royalty payments depending on the terms of the applicable contract. Failure by our licensees to maintain a stable and efficient billing, recording, distribution and payment collection network in these markets may result in inaccurate recording of sales or insufficient collection of payments from these markets and may materially and adversely affect our financial condition and results of operations. In addition, although we have, pursuant to our license agreements, audit rights to the database of our licensees to ensure that proper payment amounts are being recorded and remitted, such activities can be disruptive and time consuming and as a result we have not, to date, exercised such rights. Certain of our licensees in the past have failed to accurately report amounts due to us and have diverted certain payables to one of our former chairmen, in contravention of our license agreements. Although we have taken a number of steps to improve our internal controls and compliance procedures to prevent inaccurate reporting and illicit diversion of payments, we cannot ensure that such incidents will not occur again. Any future occurrence of such incidents may materially and adversely affect our business, financial condition and results of operations.

Furthermore, our overseas licensees are responsible for complying with local laws, including obtaining and maintaining the requisite government licenses and permits. Failure by our overseas licensees to do so may have a material adverse effect on our business, financial condition and results of operations.

***GungHo, the publisher of our games in Japan, our largest market in terms of revenues, is our majority shareholder, which gives them control of our board of directors.***

Since April 1, 2008, GungHo has been our largest shareholder and beneficially owns, as of the date hereof, 59.3% of our common shares. As a result, GungHo is able to exert significant control over all matters requiring shareholder approval, including the election of directors and approval of significant corporate transactions, including acquisitions, divestitures, strategic relationships and other matters, and may also exert significant control

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over decisions related to the listing of our American depository shares on the NASDAQ Global market. In addition, as GungHo is also an online game developer, there may be conflicts of interest. For instance, GungHo may utilize our time and resources towards efforts which benefits itself and its shareholders to the detriment of our other shareholders. GungHo may also compete directly or indirectly against us for users and customers or increased market share for its games. Furthermore, four of our registered Directors, Mr. Toshiro Ohno, Mr. Kazuki Morishita, Mr. Yoshinori Kitamura and Mr. Kazuya Sakai currently serve as Executive Officer and Executive General Manager, President and Chief Executive Officer, Director and Executive General Manager, Director and Chief Financial Officer, respectively, of GungHo, and there may be conflicts of interest in the decisions made by our Board of Directors and senior management. See ITEM 7.B. RELATED PARTY TRANSACTIONS Relationship with GungHo.

***We operate in a highly competitive industry and compete against many large companies.***

Increased competition in the online game industry in our markets from existing and potential competition could make it difficult for us to retain existing users and attract new users, and could reduce the number of hours users spend playing our current or future games or cause us and our licensees to reduce the fees charged to play our current or future games. In some of the countries in which our games are distributed, such as Korea, Japan and Taiwan, growth of the market for online games has continued to slow while competition remains strong. If we are unable to compete effectively in our principal markets, our business, financial condition and results of operations could be materially and adversely affected. Many companies worldwide are dedicated to developing and/or operating online games and compete across various markets and regions. We expect more companies to enter the online game industry and a wider range of online games to be introduced in our current and future markets. Our competitors in the massively multiplayer online role playing game industry vary in size from small companies to very large companies with dominant market share such as NCsoft of Korea and Shanda of China. We also compete with online casual game and game portal companies such as NHN, Nexon, CJ Internet and Neowiz Games, all from Korea. In addition, we may face stronger competition from companies that produce package games, such as Activision Blizzard, Electronic Arts, Nintendo and Sony Computer Entertainment, some of which have already successfully entered the online gaming market and many of which have announced their intention to expand their game services and offerings over the Internet. For example, World of Warcraft, Activision Blizzard's online game, was released in 2004 and has been one of the most popular games in the world. Electronic Arts co-developed with Neowiz Games and launched FIFA Online 2, a sports online game based on its best-selling package sports game franchise FIFA series in Korea in 2006 and beta testing is conducted in China and South East Asian countries. Many of our competitors have significantly greater financial, marketing and game development resources than we have. As a result, we may not be able to devote adequate resources to develop, acquire or license new games, undertake extensive marketing campaigns, adopt aggressive pricing policies or adequately compensate our game developers or third-party game developers to the same degree as many of our competitors.

As the online game industry in many of our markets is rapidly evolving, our current or future competitors may more effectively adapt to the changing competitive landscape and market conditions and compete more successfully than us. In particular, online game products are becoming more similar to each other, thus becoming commoditized and undifferentiated. In this environment, larger companies with relative economies of scale have a clear advantage over smaller companies like ours, as they are able to develop games in a more cost efficient manner, diversify their risks with a broader category of games and genres and increase their chances of having widely popular games. In addition, any of our competitors may offer products and services that have significant performance, price, creativity or other advantages over those offered by us. These products and services may weaken the market strength of our brand name and achieve greater market acceptance than ours. In addition, any of our current or future competitors may be acquired by, receive investments from or enter into strategic relationships with larger, more well established and better-financed companies and therefore may be able to obtain significantly greater financial, marketing and game licensing and development resources than we can. See ITEM 4.B. BUSINESS OVERVIEW COMPETITION.



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***Our investments in joint ventures or partnerships related to development of new online games may not be successful.***

Since 2004 we have made investments in joint ventures and entered into partnership arrangements with third-parties to invest in online game. In many cases, as we do not have significant investment or other control over such entities, the success of such joint ventures and partnership arrangements is heavily dependent on third parties and their investment decisions. In 2005, we entered into a limited liability partnership agreement to invest an aggregate amount of ¥1,000 million in Online Game Revolution Fund No. 1, a limited liability partnership which purpose was to invest in online games. In 2005, 2006 and 2008, we made contributions of ¥100 million, ¥150 million and ¥642 million, respectively, to the partnership. While as of December 31, 2008, we have a 16.39% interest in the partnership as a limited partner, we cannot significantly influence the partnership's operation and financial or investment policies. We account for our partnership interest under equity method of accounting. We recorded our partnership interest as an equity loss equal to ₩978 million, ₩1,026 million and ₩5,119 million in 2006, 2007 and 2008, respectively. We also invested \$9 million in May 2006 for the purchase of Series D preferred shares of Perpetual Entertainment, Inc., a game development company, which subsequently went into liquidation proceeding in October 2007 due to its poor financial condition. We determined that our investment in Perpetual Entertainment, Inc. will not be recoverable and recognized the total investment amount as impairment losses on investments in 2007.

If our partners or our investments in such joint ventures and partnerships are unable to manage their investments and develop promising online games, such joint ventures and partnerships will be unable to attain their investment objectives, which may materially and adversely affect the value of our investments and commitments and will likely have a material adverse affect on our business, financial condition and results of operation.

***We have experienced frequent turnover among our senior management team and key employees. Some of our senior managers and key employees have limited experience in our industry, which could materially and negatively affect our business prospects.***

Some members of senior management and other key employees have worked with us and in our industry for a relatively short period of time. Their unfamiliarity with many aspects of the business operations may adversely affect our business, prospects, financial condition and results of operation. Despite our efforts to stabilize the composition of our senior management, we cannot provide any assurance that we will be successful. Our business prospects must be considered in light of the risks and difficulties we have encountered in the recruiting and retaining qualified senior management. Our inability to successfully address these risks and difficulties could materially harm our business prospects, financial condition and results of operations.

***If we fail to hire and retain skilled and experienced game developers or other key personnel to design and develop new online games and additional game features, we may be unable to achieve our business objectives.***

In order to meet our business objectives and maintain our competitiveness, we need to attract and retain qualified employees, including skilled and experienced online game developers. We compete to attract and retain key personnel with other companies in the online game industry as well as in the broader entertainment, media and Internet industries, many of which offer superior compensation arrangements and career opportunities. In addition, our ability to train and integrate new employees into our operations may not meet the changing demands of our business. We cannot assure you that we will be able to attract and retain qualified game developers or other key personnel, and successfully train and integrate them to achieve our business objectives, which could materially harm our business prospects. For example, during the development of Ragnarok Online II, we lost some online game developers and hired new online game developers, which negatively affected our ability to launch Ragnarok Online II in a timely fashion.





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***Undetected programming errors or flaws in our games could harm our reputation or decrease market acceptance of our games, which would materially and adversely affect our business prospects, reputation, financial condition and results of operations.***

Our current and future games may contain programming errors or flaws, which may become apparent only after their release. In addition, our online games are developed using programs and engines developed by and licensed from third party vendors, which may include programming errors or flaws over which we have little or no control. If our users have negative experiences with our games related to or caused by undetected programming errors or flaws, they may be less inclined to continue subscriptions for our games or recommend our games to other potential users.

While we have not experienced any material disruptions to our business from such errors or flaws in our games or in the programs and engines that we use to develop our games, these risks are inherent to our industry and, if realized, could severely harm our reputation, cause our users to cease playing our games, divert our resources or delay market acceptance of our games, any of which could materially and adversely affect our business, financial condition and results of operations.

***Unexpected network interruptions, security breaches or computer virus attacks could harm our business and reputation.***

Failure to maintain satisfactory performance, reliability, security and availability of our network infrastructure, whether maintained by us or by our licensees, may cause significant harm to our reputation and negatively impact our ability to attract and maintain users. Major risks relating to our network infrastructure include:

any breakdowns or system failures, including from fire, flood, earthquake, typhoon or other natural disasters, power loss or telecommunications failure, resulting in a sustained shutdown of all or a material portion of our servers;

any disruption or failure in the national or international backbone telecommunications network, which would prevent users in certain countries in which our games are distributed from logging onto or playing our games for which the game servers are located in other countries; and

any security breach caused by hacking, loss or corruption of data or malfunctions of software, hardware or other computer equipment, and the inadvertent transmission of computer viruses.

*Hacking* involves efforts to gain unauthorized access to information or systems or to cause intentional malfunctions or loss or corruption of data, software, hardware or other computer equipment. Hackers, if successful, could misappropriate proprietary information or cause disruptions in our service. We may have to spend significant capital and human resources to rectify any damage to our system. In addition, we cannot ensure that any measures we take against computer hacking will be effective. A well-publicized computer security breach could significantly damage our reputation and materially and adversely affect our business.

We have been subject to denial of service attacks that have caused portions of our network to be inaccessible for limited periods of time but did not cause material losses or damages. Although we take a number of measures to ensure that our systems are secure and unaffected by security breaches, including ensuring that our servers are hosted at physically secure sites, limiting access to server ports, and using firewalls, passwords, and encryption technology, we cannot ensure that any measures we take against computer hacking will be effective.

In addition, computer viruses may cause delays or other service interruptions on our systems and expose us to a material risk of loss or litigation and possible liability. We may be required to expend significant capital and other

resources to protect our websites against the threat of such computer viruses and alleviate any problems. Moreover, if a computer virus affecting our system is highly publicized, our reputation could be materially damaged and our visitor traffic may decrease.

Any of the foregoing factors could reduce our users' satisfaction, harm our business and reputation and have a material adverse effect on our financial condition and results of operations.

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***Electronic embezzlement could lessen the popularity of our online games and adversely affect our reputation and our results of operations.***

Despite security measures, some of our employees or licensees employees with high-level security access to our network, or other employees who hack into or otherwise gain unauthorized access to certain sectors of our network, may succeed in breaching internal security systems and engage in electronic embezzlement by creating or diverting game money used in our online games and engaging in a public or private sale of the game money for their personal financial benefit. For example, from October 2005 to March 2006, a Ragnarok Online game master at GungHo hacked into his superior's account which enabled the game master to create game money. The game master sold game money for cash in an aggregate of JPY 58 million, which caused price inflation in the game and disrupted the balance of game play among the different players in Japan. GungHo dismissed the game master and implemented disciplinary action for high level executives. Although we have internal security procedures in place designed to prevent electronic embezzlement, we cannot assure you that we or our overseas licensees will be successful in preventing all electronic embezzlement. We have taken a number of procedures to prevent electronic embezzlement, including installing security programs specialized to prevent counterfeiting and modification of program files, but cannot assure you such procedures will be sufficient to prevent new methods to engage in electronic embezzlement. Incidents of electronic embezzlement may negatively impact the reputation of our games, which may materially and adversely affect our business, financial condition and results of operations.

***Cheating by users of online games could lessen the popularity of our online games and adversely affect our reputation and our results of operations.***

In the past, we have experienced numerous incidents where users were able to modify the published rules of our online games. Although these users did not gain unauthorized access to our systems, they were able to modify the rules of our online games during game play in a manner that allowed them to cheat and disadvantage our other online game users, for example, by utilizing auto-run programs that enabled the games to be continuously and automatically played without user participation, which allowed the users to accrue in-game points quickly, causing many other players to stop using the game and shortening the game's lifecycle. Such unauthorized manipulation of our games may negatively impact the image and users' perception of our games and damage our reputation. Although we have taken a number of steps to deter our users from cheating when playing our online games, including spot checks, monitoring of game play by game masters to check for suspicious activity, we cannot assure you that we or our licensees will be successful or timely in taking the corrective steps necessary to prevent users from modifying the terms of our online games.

***Unauthorized use of our intellectual property by third parties, and the expenses incurred in protecting our intellectual property rights, may adversely affect our business.***

Our intellectual property such as copyrights, service marks, trademarks and trade secrets are critical to our business. Unauthorized use of the intellectual property used in our business, whether owned by us or licensed to us, may materially and adversely affect our business and reputation. We rely on trademark and copyright law, trade secret protection and confidentiality agreements with our employees, customers, business partners and others to protect our intellectual property rights. Despite certain precautions taken by us, it may be possible for third parties to obtain and use our intellectual property without authorization.

Since the commercialization of Ragnarok Online in August 2002, we have discovered that the server-end software of Ragnarok Online has been consistently and unlawfully released in most of the countries and markets in which Ragnarok Online is offered. This enables unauthorized parties to set up local server networks to operate Ragnarok Online, which may result in the diversion of a significant number of paying users. We designate certain employees to be responsible for detecting such illegal servers. In Korea, we report offenders to the relevant enforcement authority

for possible prosecution relating to crimes on the Internet. In markets outside of Korea, we cooperate with and rely on our licensees to seek enforcement actions against operators of illegal servers. We may incur considerable costs in the future in order to remedy software piracy of our sever software and to enforce our rights against the operators of unauthorized server networks.

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The validity, enforceability, enforcement mechanisms and scope of protection of intellectual property in Internet-related industries are uncertain and evolving. In particular, the laws and enforcement regimes of Korea, Japan, Taiwan, Thailand, China and certain other countries in which our games are distributed are uncertain or may not protect intellectual property rights to the same extent as do the laws and enforcement procedures of the United States. Moreover, litigation may be necessary in the future to enforce our intellectual property rights. Such litigation could result in substantial costs and diversion of our resources, disruption of our business, and have a material adverse effect on our business, prospects, financial condition and results of operations.

***We may be subject to claims with respect to the infringement of intellectual property rights of others, which could result in substantial costs and diversion of our financial and management resources.***

We cannot be certain that our online games do not or will not infringe upon patents, copyrights or other intellectual property rights held by third parties. We may become subject to legal proceedings and claims from time to time relating to the intellectual property of others. If we are found to have violated the intellectual property rights of others, we may be enjoined from using such intellectual property, and we may be required to pay penalties, fines and pay for unauthorized use of such intellectual property and we may need to incur additional license fees or be forced to develop alternative technology or obtain other licenses. We may incur substantial expenses in defending against these third party infringement claims, regardless of their merit. In addition, certain of our employees were recruited from other online game developers, including current and potential competitors. To the extent these employees have been and are involved in the development of our games that are similar to the games they helped develop at their former employers, we may become subject to claims that we or such employees have improperly used or disclosed trade secrets or other proprietary information. Although we are not aware of any pending or threatened claims of this type, if any such claims were to arise in the future, litigation or other dispute resolution procedures might be necessary to retain our ability to offer our current and future games, which could result in substantial costs and diversion of our financial and management resources.

Successful infringement or licensing claims against us may result in substantial monetary damages, which may materially disrupt the conduct of our business and have a material adverse effect on our reputation, business, financial condition and results of operations.

***We may not be able to successfully implement our growth and profit improvement strategies.***

We are pursuing a number of growth and profit improvement strategies, including the following:

- distributing games developed in-house;
- publishing games acquired from or developed by third parties through licensing arrangements;
- offering our games in countries where we currently have little or no presence;
- optimizing our marketing and research and development expenditures;
- cross-selling our popular online games through other lines of businesses, such as mobile games, animation and character merchandising; and
- pursuing joint ventures with game development companies.

We cannot assure you that we will be successful in implementing any of these strategies. Certain of our strategies relate to new services or products, such as game business related to internet protocol television, for which there are no

established markets, or in which we lack experience and expertise. If we are unable to successfully implement our growth and profit improvement strategies, our revenues, profitability and competitiveness may be materially and adversely affected.

***We have limited business insurance coverage and any business interruption could have a material adverse effect on our business.***

While we carry insurance coverage against certain risks, such as fire, flood and earthquake, in respect of our principal assets, including offices and equipment, as well as directors and officers liability insurance, we do not

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separately maintain casualty and liability insurance against litigation, risks or disruptions related to our business. The occurrence of any natural disaster, fire, power loss, telecommunications failure, break-ins, sabotage, computer viruses, intentional acts of Internet vandalism, human error or other similar events may damage our facilities or network servers and disrupt the operation of our business. As we do not carry sufficient natural disaster or business interruption insurance to compensate us for all types or amounts of loss that could arise, any damage or disruption from such events might result in our incurring substantial costs and the diversion of our resources, and have a material adverse effect on our business, financial condition and results of operation. See ITEM 4.B. BUSINESS OVERVIEW INSURANCE.

### ***Slow growth or contractions in the Internet café industry in Korea may affect our ability to target a core group of users.***

According to the 2008 report issued by the Korean Game Industry Agency, the growth in the number of Internet cafés in Korea started to stabilize from 2000. According to the report, the number of Internet cafés slightly decreased for a short period of time due to certain legal developments such as the Enforcement Decree of the Building Act, which placed limitation on the space for Internet cafés, the School Health Act, which prohibited the entry of certain facilities into the school environment clean-up zone and from the Mandatory Registration of Businesses Supplying Games which was enforced by the government to regulate speculative gambling places. While we believe that there was no significant change in the number of Internet cafés in active operation in 2008 compared with the previous several years, as the Korean government enforces its regulations to tighten control over businesses that provide Internet and computer game facilities, the number of Internet cafés is expected to gradually decrease in the long term. Internet cafés have traditionally been the largest consumer and served as a medium of the game industry in Korea and any future reduction in the number of Internet cafés may shrink the size of the overall game market in Korea and adversely affect our ability to target a core group of potential users who prefer playing online games, in particular, massively multiplayer online role playing games, at Internet cafés.

### ***The high cost to access the Internet in certain markets may impede our entry into such markets.***

Our growth potential in many of the markets in which our games are currently distributed or which we intend to enter, such as Southeast Asia and CIS countries, may be limited as the penetration rates for personal computers in such markets are relatively low and the cost of Internet access relative to the per capita income is higher when compared to some of our principal markets such as Korea and Japan. If we are unable to successfully enter and develop new markets for our games, our growth and profit improvement strategies, our revenues, profitability and competitiveness may be materially and adversely affected.

### ***Occurrence of widespread public health problems could adversely affect our business and results of operations.***

During 2003, some online game operators in China experienced declining growth of their online game revenues which they believe resulted from the closure of Internet cafés in Beijing and elsewhere to prevent the spread of SARS, or severe acute respiratory syndrome. In April 2009, a new strain of influenza A virus subtype H1N1, commonly referred to as swine flu, was first discovered in Mexico and quickly spread to other parts of the world. A renewed outbreak of SARS or another widespread public health problem, such as swine flu or avian influenza, in China or in other countries may prevent our customers from accessing Internet cafés and may adversely affect our business and operating results.

A worldwide health crisis from any known or unknown causes and the response and the reaction from the health authorities of each country may impact our operations in a number of ways, including, among other things:

quarantines or closures of some of our offices which would severely disrupt our operations;



the sickness or death of our officers and key employees; and

closure of Internet cafés and other public areas where people access the Internet.

Any of the foregoing events or other unforeseen consequences of public health problems could adversely affect our business, financial condition and results of operations.

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***Some of our minority shareholders have been very active in making demands and requests on our management and our management may be required to expend substantial time, effort and resources to respond to such demands and requests.***

Certain of our minority shareholders in and outside of Korea have made various demands on our management, including with respect to our corporate governance practices. For example, certain of our minority shareholders formed a committee in March 2006 named the Gravity Committee for the Fair Treatment of Minority Shareholders, or the Minority Shareholders Committee. The committee has since made a number of requests, including a request to inspect our financial documents and review decisions made by our management concerning transactions entered into with certain parties, and to pursue legal action if the committee views such transactions to have been entered into improperly. In the future, our management may be required to expend substantial time, effort and resources to respond to such requests from our minority shareholders, including the Minority Shareholders Committee, which may negatively impact the ability of our management to address business challenges and operational requirements facing us, and adversely affect our business, financial condition and results of operations.

***We may be required to take significant actions that are contrary to our business objectives in order to avoid being deemed an investment company as defined under the Investment Company Act of 1940, as amended.***

Generally, the Investment Company Act of 1940, or the 1940 Act, provides that a company is not an investment company and is not required to register under the 1940 Act as an investment company if:

the company is primarily engaged, directly or through a wholly-owned subsidiary or subsidiaries, in a business or businesses other than that of investing, reinvesting or trading in securities; and

40% or less of the value of the company's assets (exclusive of cash items and U.S. government securities) is represented by investment securities as defined by the 1940 Act.

We believe that we are engaged primarily and directly in the businesses of providing online game services, and that less than 40% of the fair market value of our assets (exclusive of our cash items) is represented by investment securities. Consequently, we believe that we are not an investment company as that term is defined under the 1940 Act. For this purpose, we treat a bank deposit that may be withdrawn earlier than on its maturity date upon demand without penalty against the principal amount of the deposit as cash items rather than securities. In the future we may be required to take actions to avoid the requirement to register as an investment company, such as shifting a significant portion of our short-term investment portfolio into low-yielding bank deposits or other short-term securities which are not considered to be securities due to their liquidity and certain other characteristics. These types of investments may reduce the amount of interest on other income that we could otherwise generate from our investment activities. In addition, we may need to acquire additional income or loss generating assets that we might not otherwise have acquired or forego opportunities to acquire minority interests in companies that could be important to our strategy.

The 1940 Act also contains regulations with respect to investment companies, including restrictions on their capital structure, operations, transactions with affiliates and other matters which would be incompatible with our operations. If we were to be deemed an investment company in the future, we would effectively be precluded from making public offerings in the United States. In addition to disciplinary actions, such as SEC enforcement actions seeking monetary damages, we could also be subject to administrative or legal proceedings and any contracts to which we are a party that violate the 1940 Act or the rules thereunder might be rendered unenforceable or subject to rescission.

***Our status as a passive foreign investment company in 2008 and potentially other years could result in adverse U.S. tax consequences for you.***

In light of the nature of our business activities and our holding of a significant amount of cash, short-term investments and other passive assets after our initial public offering, we may have been since our initial public offering a passive foreign investment company for U.S. federal income tax purposes. In particular, due to the deterioration of the trading price of our ADSs, we believe that we were a PFIC in 2008 and there is a significant risk

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that we will continue to be a passive foreign investment company in 2009. If we are a passive foreign investment company for any taxable year during which you hold our ADSs or common shares, you could be subject to adverse U.S. federal income tax consequences. You are urged to consult your tax advisors concerning the U.S. federal income tax consequences of holding our ADSs or common shares if we are considered a passive foreign investment company in any taxable year. See ITEM 10.E. TAXATION U.S. FEDERAL INCOME TAX CONSIDERATIONS Passive foreign investment companies.

***We have identified a material weakness in our internal controls over financial reporting. If we fail to achieve and maintain an effective system of internal controls over financial reporting, we may be unable to accurately report our financial results or do so on a timely basis or reduce our ability to prevent or detect fraud, and investor confidence and the market price of our ADSs may be adversely affected.***

In connection with the audit of our financial statements prepared under U.S. GAAP for the year ended December 31, 2008, we have identified a material weakness (as defined under both the U.S. Securities and Exchange Commission, or SEC, Management's Report on Internal Control Over Financial Reporting, and Standards of the Public Company Accounting Oversight Board (United States)) in our system of internal control over financial reporting. In addition, our management assessed the effectiveness of our internal controls over financial reporting and disclosure controls and procedures as of December 31, 2008 pursuant to Section 404 of the Sarbanes-Oxley Act of 2002, or Sarbanes-Oxley Act, and related SEC rules, respectively and concluded that our internal control over financial reporting and disclosure controls and procedures were not effective as of December 31, 2008. Management has identified the following material weakness in our internal control over financial reporting as of December 31, 2008:

*Lack of controls over equity method investment.* We did not design or maintain effective internal control over the accuracy of the accounting for the equity method investment. Specifically, we did not maintain effective control for the proper identification of and accounting for GAAP differences between local GAAP and U.S. GAAP related to our equity method investment.

This material weakness resulted in a material audit adjustment to the equity method investment and related income/loss accounts. Additionally this material weakness could result in misstatements of any of our financial statements and other material weaknesses that are not prevented or detected, which could result in a material misstatement of our annual consolidated financial statements. After considering this material weakness, among other matters, our Chief Executive Officer and Chief Financial Officer have also concluded, most recently as of December 31, 2008, that our disclosure controls and procedures were not effective to provide reasonable assurance that information required to be disclosed in the reports we file and submit under the Exchange Act is recorded, processed, summarized and reported as and when required.

Furthermore, we are subject to the Sarbanes-Oxley Act, which requires us to, among other things, maintain an effective system of internal controls over financial reporting, and requires our management to provide a certification on the effectiveness of our internal controls on an annual basis. Additionally, our independent registered public accounting firm must provide an audit opinion on the effectiveness of our internal control over financial reporting.

If we fail to create an effective system of internal controls over financial reporting, we may be unable to accurately report our financial results in a timely manner or prevent errors or fraud, and investor confidence and the market price of our ADSs may be adversely affected. See ITEM 15. CONTROLS AND PROCEDURES for additional discussion concerning our material weakness.

***Rapid technological developments and changes in market environment may limit our ability to recover game development, acquisition or licensing costs and adversely affect our financial condition and results of operations due to impairment loss.***

The online game industry is subject to rapid technological developments and changes in market environment, which could render our online games under development and commercialized games obsolete or unattractive to users. Any resulting failure to recover capitalized development, acquisition or licensing costs and the recognition of impairment loss for such costs may materially and adversely affect our financial condition and results of operations.

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**RISKS RELATING TO OUR REGULATORY ENVIRONMENT**

*Our online operations and businesses are subject to regulation in certain of the countries in which our games are distributed, such as Korea, China, Taiwan, Japan and Thailand, the changes of which are difficult to predict, and the uncertainties in interpretation and enforcement of rules in such counties may limit the protections available to us.*

The regulatory and legal regimes in many of the countries in which our games are distributed have yet to establish a sophisticated set of laws, rules or regulations designed to regulate the online game industry. However, in many of our principal markets, such as Korea, China, Taiwan and Thailand, legislators and regulators have implemented or indicated their intention to implement laws and regulations with respect to issues such as user privacy, defamation, pricing, advertising, taxation, promotions, financial market regulation, consumer protection, content regulation, quality of products and services, and intellectual property ownership and infringement that may directly or indirectly impact our activities. The impact of such laws and regulations on our business and results of operations is difficult to predict as many such laws and regulations are constantly changing. However, as we might unintentionally violate such laws or such laws may be modified and new laws may be enacted in the future, any such developments, or developments stemming from enactment or modification of other laws, could increase the costs of regulatory compliance, force changes in business practices or otherwise have a material adverse effect on our business, financial condition and results of operations. Further, if the cost of regulatory compliance increases for our licensees as a result of regulatory changes, our licensees may seek to reduce royalties and license fees payable to us, which may materially and adversely affect our business, results of operations and financial condition.

***Korea***

A draft amendment to the National Health Promotion Act was submitted to the National Assembly in February 2009. The draft amendment, among others, propose to designate certain public facilities including Internet cafés as non-smoking areas. If the draft amendment is adopted in the extra session of the National Assembly, it will cause significant changes in the operation of Internet cafés, which currently operate both smoking sections and non-smoking sections. The number of Internet cafés in Korea is already gradually decreasing and the enactment of the proposed amendment may have a further effect in reducing the number of Internet cafés operated by small business owners and have a materially adversely affect on our business, financial condition and results of operation. See ITEM 3.D. RISK FACTORS RISKS RELATING TO OUR BUSINESS Slow growth or contractions in the Internet café industry in Korea may affect our ability to target a core group of potential users. See also ITEM 4.B. BUSINESS OVERVIEW LAWS AND REGULATIONS Korea for detailed discussion regarding Korean laws that affect our operations.

***China***

The Chinese government, through various regulatory authorities, heavily regulates the Internet sector, which includes the online game industry. In addition, there are uncertainties in the interpretation and application of existing Chinese laws, regulations and policies regarding the activities of Internet companies and businesses in China. Any violations of current and future laws and regulations could materially and adversely affect our and our Chinese licensee s business, financial condition and results of operations. See ITEM 4.B. BUSINESS OVERVIEW LAWS AND REGULATIONS China for detailed discussion regarding Chinese laws that affect our operations.

***Taiwan***

In Taiwan, the game industry and online game companies are subject to various laws and regulations on different aspects, including, among others, consumer protection, rating system for protection of children and juveniles, Internet cafés, intellectual property and privacy protection.

Currently there is no national laws specifically regulating the operation of Internet cafés in Taiwan. However, several municipalities and counties of Taiwan, such as Taipei City, Taipei County, Taoyuan County, Tainan City and Nantou County, have promulgated ordinances imposing restrictions on Internet cafés. In order to have Internet cafés regulated under a national legislation rather than by different municipalities and counties ordinances, the ROC

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MOEA as well as some legislators propose to regulate all Internet cafés located in Taiwan under a national legislation to be enacted. It is unclear, however, whether or when the above proposals will be passed by the Legislative Yuan and what restrictions will be imposed on Internet cafés. If the future laws and regulations have an impact on the Internet cafés, the growth of the Internet cafés industry in Taiwan may be affected and adversely affect our business, financial condition and result of operations. See ITEM 4.B. BUSINESS OVERVIEW LAWS AND REGULATIONS Taiwan for detailed discussion regarding Taiwanese laws that affect our operations.

***Japan***

See ITEM 4.B. BUSINESS OVERVIEW LAWS AND REGULATIONS Japan for detailed discussion regarding Japanese laws that affect our operations.

***Thailand***

Although there is no specific law or regulation that directly governs the online game industry in Thailand, new legislation was passed in June 2008 to impose certain restrictions to control operators of game shops (i.e., places where people can play games, including Internet cafés that provide game services) and limit access to game shops by users under 18 years of age. These restrictions include limitations on the business days and hours, location and building structure of game shops as well as the daily playing time of games and curfew hours for users under 18 years of age to enter game shops and Internet cafés. These restrictions, however, will be prescribed in further detail in ministerial regulations of the Ministry of Culture. Pending the prescription of the ministerial regulations by the Ministry of Culture, similar restrictions under the rules of the Ministry of Interior and provincial authorities are still in force. See ITEM 4.B. BUSINESS OVERVIEW LAWS AND REGULATIONS Thailand for detailed discussion regarding Thai laws that affect our operations.

***United States***

See ITEM 4.B. BUSINESS OVERVIEW LAWS AND REGULATIONS United States for detailed discussion regarding U.S. laws that affect our operations.

***Our online games may be subject to governmental restrictions or ratings systems, which could delay or prohibit the release of new games or reduce the existing and potential scope of our user base.***

Legislation is periodically introduced in many of the countries in which our games are distributed to establish a system for protecting consumers from the influence of graphic violence and sexually explicit materials contained in various types of games. For instance, Korean law requires online game companies to obtain ratings classifications and implement procedures to restrict access of online games to certain age groups. Similar mandatory ratings systems and other regulations affecting the content and distribution of our games have been adopted or are under review in Taiwan, China, the United States and other markets for our online games. For instance, in May 2009, the Ministry of Industry and Information Technology of the PRC promulgated a regulation requiring that effective as of July 1, 2009, all computers sold in China shall be preinstalled with the latest available version of Green Dam-Youth Escort, a software aimed at filtering out unhealthy content in text and graphics from the Internet, which, according to the official Website of the software, may be used to control the time on Internet, prohibit access to computer games and filter out unhealthy Websites. In the future, we may be required to modify our game content or features or alter our marketing strategies to comply with new governmental regulations or ratings assigned to our current or future games, which could delay or prohibit the release of new games or upgrades and reduce the existing and potential scope of our user base. Moreover, uncertainties regarding governmental restrictions or ratings systems applicable to our business could give rise to market confusion, thereby materially and adversely affecting our business, financial condition and results of operations.





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***Restrictions and controls on currency exchange in Korea and in certain countries in which our games are distributed may limit our ability to effectively utilize revenues generated in Won to fund our business activities outside Korea or expenditures denominated in foreign currencies, and may limit our ability to receive and remit revenues effectively.***

The existing and any future restrictions on currency exchange in Korea, including Korean exchange control regulations, may restrict our ability to convert Won into foreign currencies under certain emergency circumstances, such as natural calamities, wars, conflicts of arms or grave and sudden changes in domestic or foreign economic circumstances, difficulties in Korea's international balance of payments and international finance and obstacles in carrying out currency policies, exchange rate policies and other Korean macroeconomic policies. Such restrictions may limit our ability to effectively utilize revenues generated in Won to fund our business activities outside Korea or expenditures denominated in foreign currencies.

In addition, the governments in certain markets in which our games are distributed, including Thailand, Taiwan and China, impose controls on the convertibility of local currency into foreign currencies and, in some cases, the remittance of currency outside their countries. Under current foreign exchange control regulations of certain markets, shortages in the availability of foreign currency may restrict the ability of our overseas licensees to pay license fees and royalties, most of which are paid in U.S. dollars, to us. Restrictions on our ability to receive license fees, royalties and other payments from our licensees would adversely affect our financial condition and liquidity.

***Adverse changes in the withholding tax rates in the countries from which we receive license fees and royalties could adversely affect our net income.***

We may be subject to income withholding in countries where we derive revenues. Such withholding is made by our overseas licensees at the current withholding rates in such countries. To the extent Korea has a tax treaty with any such country, the withholding rate prescribed by such tax treaty will apply. Under the Corporation Tax Law of Korea, we are entitled to and recognize a capped tax credit computed based on the amount of income withheld overseas when filing our income tax return in Korea. Accordingly, the amount of taxes withheld overseas may be offset against taxes payable in Korea.

The tax rates on royalties pursuant to tax treaties that Korea entered into have not changed recently other than with regards to the limited tax rates in Thailand. While this tax rate change is not adverse for us, any adverse changes in tax treaties between Korea and the countries from which we receive license fees and royalties, such as with the rate of withholding tax in the countries in which our games are distributed or in Korean tax law enabling us to recognize tax credits for taxes withheld overseas, could adversely affect our net income.

**RISKS RELATING TO OUR MARKET ENVIRONMENT**

***Our businesses may be adversely affected by developments affecting the economies of the countries in which our games are distributed.***

Our future performance will depend in large part on the economic growth of our principal markets. Our top geographic markets in terms of revenues were Japan, Korea, the United States and Canada, Taiwan and Hong Kong, and Russia, representing 50.8%, 26.3%, 6.8%, 4.3% and 2.0%, respectively, of our total revenues in 2008. Accordingly, our business, prospects, financial condition and results of operations are subject to the economic, political, legal and regulatory conditions and developments in these countries. Adverse developments in such markets may have an adverse effect on the number of our subscribers and our results of operations, which could have a material adverse effect on our business.

Deterioration in global economic conditions since the second half of 2007, as well as the recent global downturn, have weakened the economies of the countries in which our games are distributed. Many countries for the foreseeable future may continue to experience economic slowdowns and recessionary pressures, including difficulty in securing credit in the global financial markets and decreased consumer confidence and discretionary spending. While the recent global economic developments did not yet have a material adverse effect on us, continuing deterioration or delayed recovery in global economic conditions could materially and adversely affect our business, financial condition and results of operations.

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***Fluctuations in exchange rates could result in foreign currency exchange losses.***

In most of the countries in which our games are distributed, the revenues generated by our licensees are denominated in local currencies, which include the U.S. dollar, Japanese Yen, Euro, NT dollar, the Thai Baht and Chinese Yuan. In 2008, approximately 73.7% of our revenues were denominated in foreign currencies, primarily in the U.S. dollar and Japanese Yen. As the revenues denominated in local currencies, other than the U.S. dollar, Japanese Yen and Euro, are converted into the U.S. dollar for remittance of monthly royalty payments to us, any depreciation of the local currencies against the U.S. dollar will result in reduced license fees and monthly royalty payments in U.S. dollar terms and may materially and adversely affect our financial condition and results of operations.

While we receive monthly royalty revenues from our overseas licensees in foreign currencies, substantially all of our costs are denominated in Won. Our financial statements are also prepared and presented in Won. We receive monthly royalty payments from our overseas licensees based on a percentage of revenues confirmed and recorded at the end of each month applying the foreign exchange rate applicable on such date. While, in 2008, we enjoyed increased royalty revenues due to the weakening of the Korean Won against the Japanese Yen by approximately 36% from 2007 to 2008, appreciation of the Won against the Japanese Yen or other foreign currencies will result in foreign currency losses that may materially and adversely affect our financial condition and results of operations. See ITEM 5.A.

OPERATING RESULTS OVERVIEW Foreign currency effects.

As of December 31, 2008, we have not entered into any outstanding foreign currency forward exchange contract. We may enter into hedging transactions in the future to mitigate our exposure to foreign currency exchange risks, but we may not be able to do so in a timely or cost-effective manner, or at all.

***Increased tensions with North Korea could adversely affect us and the price of our ADSs.***

Relations between Korea and North Korea have been tense over most of Korea's history and the Demilitarized Zone between the two countries is the most fortified border in the world. In October 2004, the United States and Korea agreed to a phased downsizing of the number of American troops stationed in Korea from 37,500 to 25,000 by the end of 2008, as part of worldwide U.S. troop realignment plans. However, in April 2008, the presidents of the U.S. and Korea reached an agreement to maintain the current U.S. troop level of 28,500, halting the planned withdrawal of 3,500 more U.S. troops.

The level of tension between Korea and North Korea has fluctuated and may increase or change abruptly as a result of current and future events, including ongoing contacts at the highest levels of the governments of Korea, North Korea and the United States. North Korea, Korea, the United States, China, Japan and Russia entered an accord in February 2007, whereby North Korea would begin to disable its nuclear facilities in return for fuel oil and aid. After several months of alleged non-compliance by North Korea and other related disputes among the parties, North Korea shut down its sole functioning nuclear reactor in Yongbyon and allowed the inspection team of the International Atomic Energy Agency to visit North Korea to monitor the shutdown and sealing of the facilities in July 2007. At the six-party talks in Beijing in October 2007, North Korea agreed to disable its nuclear facility at Yongbyon by the end of the year in a process overseen by a U.S.-led international team and to disclose all of its nuclear programs in return for one million tons of heavy fuel oil and lifting of sanctions by the United States. North Korea complied with disabling its nuclear facility at Yongbyon and the United States and other parties initiated delivery of the heavy fuel oil. However, North Korea failed to address an alleged plutonium-based program, uranium-enrichment program and other nuclear proliferation activities in Syria and North Korea missed the December 31, 2007 deadline to disclose the entirety of its nuclear programs.

In April 2008, North Korea and the United States agreed to draft two separate declarations, a public one that would address the plutonium-based program, and another classified one that would include the issues of uranium-enrichment

program and proliferation. After breakdowns in negotiations, in September 2008, North Korea announced it was preparing to restore and restart its nuclear facility in Yongbyon. In October 2008, the United States agreed to remove North Korea from its list of countries that sponsor terrorism after North Korea agreed to again allow international inspectors access to declared nuclear sites in North Korea and to resume disabling its nuclear facility in Yongbyon. More recently, in January 2009, North Korea nullified all political and military agreements with South Korea. In March 2009, in response to two-week long joint military exercises between the

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United States and South Korea, North Korea placed its military in combat ready mode and stated that it would not guarantee the safety of civilian aircraft that approached its airspace during the duration of the joint military exercises. In April 2009, North Korea launched a long-range rocket over the Pacific Ocean and in May 2009, it announced that it had conducted a second nuclear test and tested short-range missiles. United Nations Security Council unanimously passed a resolution in June 2009 that condemned North Korea for its actions and decided to tighten sanctions against North Korea.

We cannot assure you that recent events will not lead to an escalation of tension with North Korea. Any further increase in geopolitical tensions, resulting from testing of long-range nuclear missiles, continuing nuclear programs by North Korea, transition of power in leadership in North Korea, a break-down in existing contacts or an outbreak in military hostilities could adversely affect our business, prospects, financial condition and results of operations and could lead to a decline in the market value of our ADSs.

***Disruptions in Taiwan's political environment could seriously harm our business and operations in Taiwan.***

In 2008 and 2007, we derived 4.3% and 5.9%, respectively, of our total revenues from our licensee in Taiwan and Hong Kong. The Chinese government asserts sovereignty over mainland China and Taiwan and does not recognize the legitimacy of the government of Taiwan. The Chinese government has indicated that it may use military force to gain control over Taiwan if Taiwan declares independence or a foreign power interferes in Taiwan's internal affairs. In response, the Taiwanese government promulgated the Referendum Law on December 31, 2003, last amended on May 27, 2009, allowing referenda on a range of issues to be proposed and voted upon. The law allows a referendum on key constitutional issues in the event that Taiwan faces military attack from a foreign power and its sovereignty is threatened.

In March 2008, a new president in Taiwan was elected, President Ma Ying-jeou, who has supported the cultivation of better relations with mainland China. For instance, from July 2008, Taiwan has lifted the ban on Chinese persons visiting in Taiwan with certain limitations. In December 2008, Taiwan re-established regular direct transportation links with mainland China that had been shut since 1949, including regularly scheduled commercial flights and shipping and mail. Further, Taiwanese government is considering partially unwinding the restrictions on the investment in Taiwan by Chinese companies and person and several new regulations in connection therewith have been passed or drafted. Although recent trends may be beneficial to Taiwan's economy, the history between Taiwan and mainland China has been marked with uncertainties. Deteriorations in the relationship between Taiwan and China and other factors affecting Taiwan's political environment may materially and adversely affect our Taiwanese licensee's business and our results of operations.

**RISKS RELATING TO OUR AMERICAN DEPOSITARY SHARES**

***The public shareholders of our ADSs may have more difficulty protecting their interests than they would as shareholders of a U.S. corporation.***

Our corporate affairs are governed by our articles of incorporation and by the laws and regulations governing Korean corporations. The rights and responsibilities of our shareholders and members of our Board of Directors under Korean law may be different from those that apply to shareholders and directors of a U.S. corporation. For example, minority shareholder rights afforded under Korean law often require the minority shareholder to meet minimum shareholding requirements in order to exercise certain rights. Under applicable Korean law, a shareholder must own at least (i) one percent of the total issued shares to bring a shareholders' derivative lawsuit, (ii) three percent to demand an extraordinary meeting of shareholders, demand removal of directors or inspect the books and related documents of a company, (iii) ten percent to apply to the court for dissolution if there is gross improper management or a deadlock in corporate affairs likely to result in a significant and irreparable injury to the company or to apply to the court for a

reorganization in the case of an insolvency and (iv) 20 percent to block a small-scale share exchange that may be approved only by a board resolution. In addition, while the facts and circumstances of each case will differ, the duty of care required of a director under Korean law may not be the same as the fiduciary duty of a director of a U.S. corporation. Although the business judgment rule concept exists in Korea, there is insufficient case law or precedent to provide guidance to the management and shareholders as to how it should be

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applied or interpreted. Holders of our ADSs may have more difficulty protecting their interests against actions of our management, members of our Board of Directors or controlling shareholders than they would as shareholders of a U.S. corporation.

***Any dividends paid on our common shares will be in Won and fluctuations in the exchange rate between the Won and the U.S. dollar may affect the amount received by you.***

If and when we declare cash dividends, the dividends will be paid to the depositary for the ADSs in Won and then converted by the depositary into U.S. dollars in connection with the deposit agreement. Fluctuations in the exchange rate between the Won and the U.S. dollar will affect, among other things, the U.S. dollar amounts you will receive from the depositary as dividends. Holders of ADSs may not receive dividends if the depositary does not believe it is reasonable or practicable to do so. In addition, the depositary may collect certain fees and expenses, at the sole discretion of the depositary, by billing the holders of ADSs for such charges or by deducting such charges from one or more cash dividends or other cash distributions from us to be distributed to the holders of ADSs.

***Your ability to deposit or withdraw common shares underlying the ADSs into and from the depositary facility may be limited, which may adversely affect the value of your investment.***

Under the terms of our deposit agreement, holders of our common shares may deposit such shares with the depositary's custodian in Korea and obtain ADSs, and holders of our ADSs may surrender the ADSs to the depositary and receive our common shares. However, to the extent that a deposit of common shares exceeds the difference between:

the aggregate number of common shares we have consented to be deposited for the issuance of ADSs (including deposits in connection with offerings of ADSs and stock dividends or other distributions relating to ADSs); and

the number of common shares on deposit with the custodian for the benefit of the depositary at the time of such proposed deposit,

such common shares will not be accepted for deposit unless (i) our consent with respect to such deposit has been obtained or (ii) such consent is no longer required under Korean laws and regulations or under the terms of the deposit agreement.

Under the terms of the deposit agreement, no consent is required if the common shares are obtained through a dividend, free distribution, rights offering or reclassification of such shares. Under the terms of the deposit agreement, we have consented to any deposit to the extent that, after the deposit, the aggregate number of deposited common shares does not exceed 3,552,229 common shares or any greater number of common shares we determine from time to time (i.e., as a result of a subsequent offering, stock dividend or rights offer), unless the deposit is prohibited by applicable laws or violates our articles of incorporation; provided, however, that in the case of any subsequent offer by us or our affiliates, the limit on the number of common shares on deposit shall not apply to such offer and the number of common shares issued, delivered or sold pursuant to the offer (including common shares in the form of ADSs) shall be eligible for deposit under the deposit agreement, except to the extent such deposit is prohibited by applicable laws or violates our articles of incorporation or, in the case of any subsequent offer by us or our affiliates, we determine with the depositary to limit the number of common shares so offered that would be eligible for deposit under the deposit agreement in order to maintain liquidity of the shares in Korea as may be requested by the relevant Korean authorities. We might not consent to the deposit of any additional common shares. As a result, if a holder surrenders ADSs and withdraws common shares, the holder may not be able to subsequently deposit the common shares to obtain ADSs.



*You may not be able to exercise preemptive rights or participate in rights offerings and as a result, you may experience dilution in your ownership percentage in us.*

The Korean Commercial Code and our articles of incorporation require us to offer shareholders the right to subscribe for new common shares in proportion to their existing ownership percentages whenever new common

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shares are issued, except under certain circumstances as provided in our articles of incorporation. See ITEM 10.B. ARTICLES OF INCORPORATION Preemptive rights and issuance of additional shares.

Such exceptions include offering of new shares:

through a general public offering;

to the members of the employee stock ownership association;

upon exercise of a stock option;

in the form of depositary receipts;

to induce foreign direct investment necessary for business in accordance with the Foreign Investment Promotion Act of Korea;

for the purpose of raising funds on an emergency basis;

to certain companies under an alliance arrangement with us; or

by a public offering or to cause underwriters to underwrite new shares for the purpose of listing them on any stock exchange.

Accordingly, if we issue new shares to non-shareholders based on such exceptions, existing holders of ADSs will be diluted. If none of the above exemptions is available under Korean law, we may be required to grant subscription rights when issuing additional common shares. However, under U.S. law, we would not be able to make those rights available in the United States unless we register the securities to which the rights relate or an exemption from the registration requirements of the Securities Act is available. Under the deposit agreement governing the ADSs, if we offer rights to subscribe for additional common shares, the depositary under the deposit agreement, after consultation with us, may make such rights available to you or dispose of such rights on behalf of you and make the net proceeds available to you or, if the depositary is unable to take such actions, it may allow the rights to lapse with no consideration to be received by you. The depositary is generally not required to make available any rights under any circumstances. We are under no obligation to file a registration statement under the Securities Act to enable you to exercise preemptive rights in respect of the common shares underlying the ADSs, and we cannot assure you that any registration statement would be filed or that an exemption from the registration requirement under the Securities Act would be available. Accordingly, you may not be entitled to exercise preemptive rights and may thereby suffer dilution of your interests in the Company.

***You will not be treated as our shareholder and you will not have shareholder rights such as the voting rights applicable to a holder of common shares.***

As an ADS holder, we are not obligated to and we will not treat you as one of our shareholders and therefore, you will not have the rights of a shareholder. Korean law and our articles of incorporation govern the rights applicable to our shareholder. The depositary will be treated as the shareholder of the common shares underlying your ADSs. As a holder of ADSs, you will have ADS holder rights, which is governed by deposit agreement among us, the depositary and you, as an ADS holder. Upon receipt of the necessary voting materials, you may instruct the depositary to vote the number of shares your ADSs represent. The depositary will notify you of shareholders' meetings and arrange to deliver our voting materials to you only when we deliver them to the depositary with sufficient time under the terms of the deposit agreement. If there is a delay or loss of the proxy materials, we cannot ensure that you will receive voting

materials or otherwise learn of an upcoming shareholders meeting to ensure that you may instruct the depositary to vote your shares. In addition, the depositary and its agents are not responsible for failing to carry out voting instructions or for the manner of carrying out voting instructions.

***You would not be able to exercise dissent and appraisal rights unless you have withdrawn the underlying common shares from the depositary facility and become a holder of our common stock.***

In some limited circumstances, including the transfer of the whole or any significant part of our business, our acquisition of a part of the business of any other company having a material effect on our business, or our merger or consolidation with another company, dissenting shareholders have the right to require us to purchase their shares

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under Korean law. However, if you hold our ADSs, you will not be able to exercise such dissent and appraisal rights unless you have withdrawn the underlying common shares from the depositary facility and become our direct shareholder prior to the record date for the shareholders' meeting at which the relevant transaction is to be approved.

***We may amend the deposit agreement and the American Depositary Receipts without your consent for any reason and, if you disagree, your option will be limited to selling the ADSs or withdrawing the underlying securities.***

We may agree with the depositary to amend the deposit agreement and the ADRs without your consent for any reason. If an amendment adds or increases fees or charges, except for taxes and other governmental charges or expenses of the depositary, for registration fees, facsimile costs, delivery charges or similar items, or prejudices a substantial right of ADS holders, it will not become effective for outstanding ADRs until 30 days after the depositary notifies ADS holders of the amendment. At the time an amendment becomes effective, you are considered, by continuing to hold your ADSs, to agree to the amendment and to be bound by the ADRs and the deposit agreement as amended. If you do not agree with an amendment to the deposit agreement or the ADRs, your option is limited to selling the ADSs or withdrawing the underlying securities. No assurance can be given that the sale of ADSs would be made at a price satisfactory to you in such circumstances. In addition, the common shares underlying the ADSs are not listed on any stock exchange in Korea. Your ability to sell the underlying common shares following withdrawal and the liquidity of the common shares may be limited.

***You may be subject to Korean withholding tax.***

Under Korean tax law, if you are a U.S. investor, you may be subject to Korean withholding taxes on capital gains and dividends with respect of the ADSs unless an exemption or a reduction under the income tax treaty between the United States and Korea is available. Under the Korea-United States tax treaty, capital gains realized by holders that are residents of the United States eligible for treaty benefits will not be subject to Korean taxation upon the disposition of the ADSs. However, under the Korea-United States tax treaty, the following holders are not eligible for such tax treaty benefits: (i) in case the holder is a United States corporation, if by reason of any special measures, the tax imposed on such holder by the United States with respect to such capital gains is substantially less than the tax generally imposed by the United States on corporate profits, and 25% or more of the holder's capital is held of record or is otherwise determined, after consultation between competent authorities of the United States and Korea, to be owned directly or indirectly by one or more persons who are not individual residents of the United States and (ii) in case the holder is an individual, if such holder maintains a fixed base in Korea for a period or periods aggregating 183 days or more during the taxable year and the holder's ADSs or common shares giving rise to capital gains are effectively connected with such fixed base or such holder is present in Korea for a period or periods of 183 days or more during the taxable year.

***You may have difficulty bringing an original action or enforcing any judgment obtained outside Korea against us and our directors and officers who are not U.S. persons.***

We are organized under the laws of Korea, and most of our directors and officers reside outside of the United States. While we have a wholly-owned subsidiary in the United States, most of our assets and the assets of such persons are located outside of the United States. As a result, it may not be possible for you to effect service of process within the United States upon these persons or to enforce against them or us court judgments obtained in the United States that are predicated upon the civil liability provisions of the federal securities laws of the United States or of the securities laws of any state of the United States. There is doubt as to the enforceability in Korea, either in original actions or in actions for enforcement of judgments of United States courts, of civil liabilities predicated on the federal securities laws of the United States or the securities laws of any state of the United States.

***The transfer, sale or availability for sale of substantial amounts of our ADSs could adversely affect their market price.***

GungHo beneficially owns 59.3% of our common shares. Ramius LLC beneficially owns approximately 9.6%, and Moon Capital Master Fund Ltd. and Moon Capital Leveraged Master Fund Ltd. beneficially own, collectively, 8.5% of our common shares. If any of our major shareholders, including GungHo, Ramius LLC, Moon Capital

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Master Fund Ltd. and Moon Capital Leveraged Master Fund Ltd., decides to sell or transfer substantial amounts of our common shares into the form of ADSs in the public market or if there is a perception of their intent to sell, the market price of our ADSs could be materially and adversely affected and could materially impair our future ability to raise capital through offerings of our ADSs.

### **ITEM 4. INFORMATION ON THE COMPANY**

#### **ITEM 4.A. History and Development of the Company**

We were incorporated as a company with limited liability under Korean law on April 4, 2000 under the legal name of Gravity Co., Ltd. Following our initial public offering of 8,000,000 ADSs, each representing one-fourth of one share of our common stock, par value Won 500 per share on February 8, 2005, our ADSs were listed on the NASDAQ Stock Market s the NASDAQ Global Market under the symbol GRVY.

In March 2003, we established Gravity Interactive, LLC, our wholly-owned subsidiary in the United States. The name of Gravity Interactive, LLC was changed on January 1, 2006 to Gravity Interactive, Inc., or Gravity Interactive. In January 2004, we acquired 50% of the voting shares of Gravity Entertainment Corporation, or Gravity Entertainment, formerly RO Production Co., Ltd., our subsidiary in Japan. In October 2004, we obtained from GungHo, then the other 50% shareholder of RO Production Co., Ltd., their ownership interest in RO Production Co., Ltd., which made Gravity Entertainment our wholly-owned subsidiary. RO Production Co., Ltd. changed its corporate name to Gravity Entertainment on February 5, 2005. In April and May 2005, we acquired an aggregate of 88.15% equity interest in TriggerSoft Corporation, or TriggerSoft, which developed our R.O.S.E. Online game. TriggerSoft went into liquidation proceedings in Korea in May 2007 and the liquidation was completed in October 2007. In November and December 2005, we acquired an aggregate of 96.11% of the total shares of NeoCyon, Inc., or NeoCyon, which provides mobile multimedia services in Korea. In August 2006, we founded Gravity EU SASU, or Gravity EU, a wholly-owned subsidiary based in France, and in September 2006, we acquired 100% of the voting shares of Gravity CIS, Inc. formerly Mados, Inc., from Cybermedia International, Inc., a former subsidiary of NeoCyon. On November 21, 2007, the name of Gravity CIS, Inc. was changed to Gravity CIS Co., Ltd., or Gravity CIS. In May 2007, we established Gravity Middle East & Africa FZ-LLC, or Gravity Middle East & Africa, a wholly-owned subsidiary in Dubai. Gravity Middle East & Africa has been in the process of liquidation since September 2008. In October 2007, we founded Gravity RUS Co., Ltd., or Gravity RUS, a Russia-based subsidiary, and acquired 99.99% of the voting shares, and transferred 100% of the voting shares of Gravity CIS to Gravity RUS in December 2007. In October 2007, we formed L5 Games Inc., or L5 Games, a game development studio in the U.S., which is a wholly-owned subsidiary of Gravity Interactive. L5 Games has been in the process of liquidation since August 2008. On April 1, 2008, GungHo acquired shares of our common stock, after which it became our largest shareholder, beneficially owning approximately 52.4% of our common shares. GungHo subsequently purchased our ADSs and beneficially owns approximately 59.3% of our common shares as of May 31, 2009.

Our registered office is located at Nuritkum Square Business Tower 15F, 1605 Sangam-Dong, Mapo-Gu, Seoul, Korea 121-270. Our telephone number is (822) 2132-7000. Our main website is at <http://www.gravity.co.kr>. Our address for service of process in the United States is Gravity Interactive, 4499 Glencoe Avenue, Marina Del Rey, California 90292.

#### **ITEM 4.B. Business Overview**

##### **OVERVIEW**

We are a leading developer and publisher of online games in Japan, Brazil, the Philippines, Indonesia, Singapore, Malaysia, Thailand, Russia and Taiwan based on the number of peak concurrent users, or PCU, as compiled from

various statistical data available from public sources in such countries. We are based in Korea and we currently offer five online games worldwide and have two online games in development. Our principal product, Ragnarok Online, is commercially offered in Korea and 37 other countries and markets. Requiem is commercially offered in Korea, the United States, Canada and 15 other countries. Emil Chronicle Online is commercially offered in Korea, Thailand, Hong Kong and Taiwan. R.O.S.E. Online is commercially offered in the United States, Canada and Mexico. Pucca Racing is commercially offered in Korea and Thailand. We also offer a number of mobile games

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and license the merchandizing rights of character-related products based on our online games. We intend to diversify our online game offering by developing online games internally as well as publishing additional online games developed by third parties.

In Korea, we directly manage all aspects of game operations, such as marketing, operation, billing and customer service. For certain countries and markets, our subsidiaries directly manage such game operations. Gravity Interactive, our wholly-owned subsidiary, is responsible for all aspects of game operations in the United States, Canada, Australia and New Zealand and Gravity CIS and Gravity EU, our subsidiaries, are responsible for game operations in Russia and CIS countries and in France and Belgium, respectively. In the countries we and our subsidiaries manage game operations, game revenues are generated through subscription fees.

In the rest of the countries in which our games are offered, our overseas licensees are responsible for all aspects of game operations in their respective markets in close cooperation with us. Our license agreements have an initial term of two or three years and are subject to renewal every year once the initial term expires. We rely on the initial license fees and the ongoing royalties from our overseas licensees for a significant portion of our revenues. The ongoing royalties are based on a percentage of revenues generated by our overseas licensees from the subscriptions to our games in their respective markets.

The following table sets forth a summary of our consolidated statement of operations showing revenues from our online games (by type of revenue and geographic market), mobile games, and character merchandising and other revenue as a percentage of total revenues for the periods indicated.

	2006		Year Ended December 31, 2007		2008		2008(1)	
	(In millions of Won and thousands of US\$, except percentages)							
	(Unaudited)							
Online game revenues(2):								
Subscriptions:								
Korea	₩ 5,650	13.8%	₩ 6,238	15.5%	₩ 7,463	14.0%	US\$ 5,844	
United States/Canada	2,770	6.7	2,608	6.5	3,607	6.8	2,825	
Others			559	1.4	1,506	2.9	1,179	
Royalties and license fees:								
Japan	15,388	37.6	17,849	44.4	23,353	43.9	18,287	
Taiwan/Hong Kong	4,050	9.9	2,345	5.8	2,210	4.1	1,731	
Thailand	2,505	6.1	1,034	2.6	970	1.8	760	
Others	4,180	10.2	3,470	8.6	3,577	6.7	2,801	
Subtotal	26,123	63.8	24,698	61.4	30,110	56.5	23,579	
Mobile game revenues	3,840	9.4	4,063	10.1	6,882	12.9	5,389	
Character merchandising and other revenues	2,580	6.3	2,063	5.1	3,602	6.9	2,821	
Total revenues	₩ 40,963	100.0%	₩ 40,229	100.0%	₩ 53,170	100.0%	US\$ 41,637	



*Notes:*

- (1) For convenience only, the Won amounts are expressed in U.S. dollars at the rate of Won 1,277.0 to US\$1.00, the noon buying rate as quoted by the Federal Reserve Bank of New York in effect on April 30, 2009.
- (2) Online game revenues include revenues from Ragnarok Online, R.O.S.E. Online, Requiem, Emil Chronicle Online, Pucca Racing, Time N Tales and from two games offered through STYLIA, our casual online game portal site. We discontinued offering games through STYLIA in September 2008. We discontinued offering Time N Tales in March 2009.

**Table of Contents****OUR PRODUCTS**

We currently have four product lines: massively multiplayer online role playing games, casual online games, mobile games, and animation and character-based merchandise. Revenues from our principal product, Ragnarok Online, accounted for 73.3% of our total revenues in 2008, compared with 77.3% of our total revenues in 2007. We are seeking to diversify our revenue sources by offering additional massively multiplayer online role playing games, casual online games, and other products and services, including mobile games.

***Massively multiplayer online role playing games***

Massively multiplayer online role playing game is a genre of computer role playing games in which a large number of players interact with one another within a virtual game world.

The following table summarizes the massively multiplayer online role playing games that we currently offer and those games currently in development.

<b>Title</b>	<b>Description</b>	<b>Game Source</b>	<b>Date of Commercial Launch/Testing(2)</b>
Ragnarok Online	Action adventure with 99 levels of skill upgrades, which features two-dimensional characters in three-dimensional backgrounds(1)	Developed in-house	Launched in August 2002
R.O.S.E. Online	Three-dimensional action adventure with seven independent storylines	Originally licensed from third party developer; currently owned by us(3)	Launched in January 2005
Requiem	Three-dimensional action adventure	Developed in-house	Launched in October 2007
Emil Chronicle Online	Three-dimensional action adventure	Licensed from third party developer	Launched in August 2007
Ragnarok Online II	Three-dimensional sequel to Ragnarok Online	Being developed in-house by the Company	Open beta testing since May 2007. Currently expected to launch in the first half of 2010

***Notes:***

- (1) A game with such features is generally referred to in the industry as a 2.5 dimensional game.
- (2) The actual date of commercial launch of games in each country is dependent on a variety of factors, including technical viability and durability, availability of in-house development capability, market conditions, beta testing results and availability of licensing partners in various jurisdictions, among others.

- (3) We acquired an aggregate of 88.15% equity interest in TriggerSoft, which developed R.O.S.E. Online in April and May 2005. TriggerSoft was liquidated in October 2007.

***Ragnarok Online***

Ragnarok Online is commercially offered in Korea and 37 other countries and markets since its commercial launch in August 2002. Ragnarok Online represented 73.3% of our total revenues or Won 38,949 million (US\$30,500 thousand) in 2008, compared with 77.3% of our total revenues or Won 31,114 million in 2007. See ITEM 4.B. BUSINESS OVERVIEW OUR MARKETS Overseas markets.

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The following are revenues generated by Ragnarok Online for the periods indicated:

Revenue Type	Country	Year Ended December 31,			
		2006	2007	2008	2008(1)
		(In millions of Won and thousands of US\$)			
		(Unaudited)			
Online game-subscription revenue	Korea	₩ 5,339	₩ 5,143	₩ 5,971	US\$ 4,676
	United States/Canada <sup>(2)</sup>	2,163	2,103	2,693	2,109
	Others		558	1,198	938
	Subtotal	7,502	7,804	9,862	7,723
Online game-royalties and license fees	Taiwan/Hong Kong	4,050	2,345	1,706	1,336
	Japan	14,099	16,791	23,326	18,266
	Thailand	2,505	981	679	532
	Philippines	1,020	655	699	547
	China	516	613	472	370
	Indonesia	594	358	322	252
	Europe	534	419	446	349
	Singapore/Malaysia	224	109	63	49
	Australia/New Zealand <sup>(2)</sup>	155	1		
	Brazil	749	547	971	760
	India	118	152	26	20
	Chile	20	209	186	146
	Vietnam		130	191	150
Subtotal	24,584	23,310	29,087	22,777	
Total	₩ 32,086	₩ 31,114	₩ 38,949	US\$ 30,500	

*Note:*

- (1) For convenience only, the Won amounts are expressed in U.S. dollars at the rate of Won 1,277.0 to US\$1.00, the noon buying rate as quoted by the Federal Reserve Bank of New York in effect on April 30, 2009.
- (2) The license agreement for Ragnarok Online with Gravity Interactive, Inc. was amended in January 2008 to include Australia and New Zealand as service countries in addition to the existing service countries, the United States and Canada.

The table below provides for the periods indicated, the peak concurrent users and average concurrent users of Ragnarok Online since the first quarter of 2006, in each of our principal markets for Ragnarok Online.

Taiwan/Hong Kong		Thailand		Japan		China		Korea		USA/C
PCU(1)	ACU(2)	PCU	ACU	PCU	ACU	PCU	ACU	PCU	ACU	PCU
132,539	107,141	69,997	52,404	75,302	36,362	28,248	21,909	13,145	6,342	8,338
115,261	90,536	58,502	42,780	80,800	37,208	24,530	19,275	9,627	4,653	8,495
122,978	86,985	116,331	36,361	83,632	35,551	36,290	17,220	9,796	4,837	8,128
80,226	55,216	48,514	28,276	105,350	34,057	13,620	9,673	10,296	5,042	8,033
78,516	45,993	27,491	19,061	78,053	34,504	14,691	8,516	10,338	5,177	6,538
56,663	34,455	19,408	13,673	77,151	35,633	11,986	5,809	8,046	4,721	6,468
39,983	28,097	12,931	8,562	66,441	23,975	10,108	5,541	7,997	4,575	4,604
34,982	24,935	63,445	38,511	60,788	24,018	7,760	3,936	7,854	4,562	4,638
36,429	29,893	63,316	25,942	61,800	24,674	8,609	4,469	6,785	3,219	4,334
34,747	26,364	14,996	9,709	57,348	22,908	7,393	3,856	10,146	3,518	4,288
40,574	27,097	22,850	12,687	57,515	22,401	6,979	3,273	9,192	4,357	3,700

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	<b>Taiwan/Hong Kong</b>		<b>Thailand</b>		<b>Japan</b>		<b>China</b>		<b>Korea</b>		<b>USA/Canada</b>	
	<b>PCU(1)</b>	<b>ACU(2)</b>	<b>PCU</b>	<b>ACU</b>	<b>PCU</b>	<b>ACU</b>	<b>PCU</b>	<b>ACU</b>	<b>PCU</b>	<b>ACU</b>	<b>PCU</b>	<b>ACU</b>
<b>Q3</b>	30,128	21,292	30,455	20,707	59,470	24,109	5,342	2,476	6,306	3,052	4,661	2,311
<b>Q2</b>	27,686	20,351	28,761	22,628	58,171	24,554	5,942	2,861	6,127	3,211	4,908	2,311

*Notes:*

- (1) PCU, or peak concurrent users, represents the highest number of users of Ragnarok Online during the specified time period as recorded on the servers for the various countries.
- (2) ACU, or average concurrent users, represents the average number of concurrent users of Ragnarok Online during the specified time period as recorded on the servers for the various countries.
- (3) We believe that the number of users as measured by PCU or ACU (i) is reflective of our active user base and (ii) is correlated to revenues as revenues from an online game depend on the number of users as well as time spent playing the game. However, PCU and ACU are not measures under accounting principles generally accepted in Korea, or Korean GAAP, or U.S. GAAP and should not be construed as an alternative to operating income or another measure of performance determined in accordance with Korean GAAP or U.S. GAAP. Other companies may determine PCU or ACU differently than we do.

We obtained an exclusive license from Mr. Myoung-Jin Lee to use the storyline and characters from his cartoon titled Ragnarok for the development of Ragnarok Online including for animation and character merchandising. We paid Mr. Lee an initial license fee of Won 40 million and are required to pay royalties based on a percentage of adjusted revenues (net of value-added taxes and certain other expenses) or net income generated from the use of the Ragnarok brand through January 2033.

Ragnarok Online is an action adventure-based massively multiplayer online role playing game that combines cartoon-like characters, community-oriented themes and combat features in a virtual world within which thousands of players can interact with one another. By combining the highly interactive and community-oriented themes and features, such as marriages and organization of guilds, we believe we are able to create user loyalty from our users who favor games that provide social interaction in a virtual setting.

Other key features of Ragnarok Online include the following:

players may assume an ongoing role, or alter-ego, of a particular game character, each with different strengths and weaknesses. In Ragnarok Online, the user starts as a novice and undergoes training in a specialized mapped game zone to become familiar with the game features. Once that stage is completed, the user can choose from six basic characters, each with a distinct combination of different traits;

as each game character advances in challenge levels, the character can enter into a greater range of mapped game zones and develop into a more sophisticated game character in terms of game attributes and special powers;

Ragnarok Online characters may visually express the users' mood and emotions by using emotive icons that appear within a bubble above the characters' heads. We believe that this feature significantly expands the interface for user interaction and elevates the level of social reality of the game;

game features may be traded or sold within the game, and game characters may simulate real-life experiences such as marriage, group fights and joining a guild. In addition, players may communicate with each other through in-game chatting or instant messaging;

special events are held from time to time to stimulate community formations. For example, we periodically host fortress raids whereby players are encouraged to organize themselves into a team to compete against other teams to capture a fortress within a set time; and

the game has no preordained ending and is designed to continuously evolve in terms of plots, mapped game zones and character attributes through enhancements from time to time.

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We believe that the personal computer, or PC, configurations required to run Ragnarok Online are lower than or similar to many other competing massively multiplayer online role playing games, which we believe has facilitated our successful entry into and expansion of Ragnarok Online in many of the developed and developing countries in which Ragnarok Online is distributed. Also, we believe the community based features, such as marriages and organization of guilds, builds user loyalty from our users who favor games that provide social interaction in a virtual setting. We believe that our decision to balance three-dimensional graphics and game functions with prevailing technological standards with a combination of two-dimensional characters, which requires lower PC configurations than three-dimensional massively multiplayer online role playing games has helped to increase the popularity of Ragnarok Online, in particular in certain jurisdictions which does not have access to the more technological updated PC technology as a result of cost and other limitations. The recommended minimum PC configuration for Ragnarok Online is Pentium III 1.6 GHz, 256 MB RAM and 32 MB graphics card. Ragnarok Online can be accessed through a dial-up modem as well as broadband Internet.

***R.O.S.E. Online***

R.O.S.E. Online, which was commercially launched in January 2005, represented 1.4% of our total revenues or Won 766 million (US\$600 thousand) in 2008, compared with 4.4% of our total revenues or Won 1,760 million in 2007.

The following are revenues generated by R.O.S.E. Online for the periods indicated:

Revenue Type	Country	Year Ended December 31,			
		2006	2007	2008	2008(1)
		(In millions of Won and thousands of US\$)			
		(Unaudited)			
Online game-subscription revenue	Korea	₩ 52	₩	₩	US\$
	United States/Canada/Mexico	607	505	444	348
	Subtotal	659	505	444	348
Online game-royalties and license fees	Japan	1,289	1,058	27	21
	Indonesia		72		
	Philippines	250	125		
	China			136	106
	Vietnam			60	47
	Taiwan			99	78
	Subtotal	1,539	1,255	322	252
	Total	₩ 2,198	₩ 1,760	₩ 766	US\$ 600

*Note:*



(1) For convenience only, the Won amounts are expressed in U.S. dollars at the rate of Won 1,277.0 to US\$1.00, the noon buying rate as quoted by the Federal Reserve Bank of New York in effect on April 30, 2009.

R.O.S.E. Online, a three-dimensional game, is the first online game developed by a third party that we published pursuant to an exclusive publishing license agreement. R.O.S.E. Online was developed by TriggerSoft Corporation, or TriggerSoft, in close coordination with our in-house game development team. In May 2005, we acquired control of TriggerSoft to enhance our ability to update and improve R.O.S.E. Online on a more effective and timely basis and gained ownership of R.O.S.E. Online after liquidation of TriggerSoft in 2007.

In the United States, Canada and Mexico, we have been offering commercial service of R.O.S.E. Online since 2005 and all rights for R.O.S.E. Online have been transferred to our wholly-owned subsidiary, Gravity Interactive in June 2007. We no longer offer or license R.O.S.E. Online in other markets.

### ***Requiem***

We commercially launched Requiem in Korea in October 2007. Requiem represented 3.3% of our total revenues or Won 1,743 million (US\$1,365 thousand) in 2008, compared with 1.6% of our total revenues or Won

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644 million in 2007. We commercially offer Requiem directly in Korea and 17 other countries through our subsidiaries and currently only generate subscription revenues.

The following are revenues generated by Requiem for the periods indicated:

Revenue Type	Country	Year Ended December 31,			
		2006	2007	2008	2008(1)
		(In millions of Won and thousands of US\$)			
		(Unaudited)			
Online game-subscription revenue	Korea	₩	₩ 644	₩ 964	US\$ 755
	United States/Canada			470	368
	Russia/CIS countries			309	242
	Total	₩	₩ 644	₩ 1,743	US\$ 1,365

*Note:*

- (1) For convenience only, the Won amounts are expressed in U.S. dollars at the rate of Won 1,277.0 to US\$1.00, the noon buying rate as quoted by the Federal Reserve Bank of New York in effect on April 30, 2009.

Unlike Ragnarok Online, which does not emphasize violent themes, we designed Requiem to showcase user-to-user combat. In addition, we used advanced game development engines for enhanced graphics and to support the game's speedy and streamlined action movements. We commercially launched Requiem in the United States, Canada, Armenia, Azerbaijan, Belorussia, Estonia, Georgia, Kazakhstan, Kyrgyzstan, Latvia, Lithuania, Moldova, Russia, Tajikistan, Turkmenistan, Ukraine and Uzbekistan in June 2008.

***Emil Chronicle Online***

We commercially launched Emil Chronicle Online in Korea, Thailand, Hong Kong and Taiwan in August 2007, September 2007, June 2008 and August 2008, respectively. Emil Chronicle Online is the first online game developed by GungHo Online Entertainment, Inc., the publisher of Ragnarok Online in Japan, which is our controlling and majority shareholder. Emil Chronicle Online is an animation style game based on the chronicles of three races: Emils, Titanians and Dominions, that offers various characters and avatars for players to enjoy. We entered into a software licensing agreement with GungHo in December 2005 for the right to publish and distribute Emil Chronicle Online worldwide, except for Japan. In November 2006, we entered into a license and distribution agreement with Infocomm Asia Holdings Pte Ltd., or Infocomm Asia, to distribute Emil Chronicle Online in Singapore, Malaysia, Brunei, Thailand, the Philippines, Indonesia, Vietnam, Australia and New Zealand. In February 2007, we and Infocomm Asia granted the distribution rights of Emil Chronicle Online in Thailand to Onenet Co., Ltd. In July 2008, we amended the agreement with Infocomm Asia to take back Infocomm Asia's distribution rights in countries in which Infocomm Asia had not yet entered into service agreements with sub-licensees. As a result, we took back our distribution rights for the remaining 8 countries and subsequently, in December 2008, entered into license and distribution agreements with Run Up Game Distribution and Development Sdn. Bhd. for distribution of Emil Chronicle Online in Singapore and Malaysia and in February 2009 with PT. Wave Wahana Wisesa for distribution in Indonesia. We entered into license and distribution agreements for Emil Chronicle Online in China with a wholly-owned subsidiary of The9 Limited in

January 2007 and in Taiwan and Hong Kong with GameCyber Technology Ltd. in August 2007. The amount of revenues from Emil Chronicle Online in 2008 represented 1.8% of our total revenues in 2008 and that in 2007 represented less than 1% of our total revenues in 2007.

***Ragnarok Online II***

Ragnarok Online II is a sequel to Ragnarok Online and a massively multiplayer online role playing game expected to have enhanced character and community features. Ragnarok Online II includes pastel-type graphics, advanced character customization and detailed monsters and non-player characters. Ragnarok Online II also adopts cartoonist Mr. Myoung-Jin Lee's original drawings from his comic book Ragnarok and music from Kanno Yoko, a well-respected composer in the animation industry. We currently have 24 designers, 9 programmers and 11 game planners dedicated to the development of Ragnarok Online II. We have been conducting open beta testing of

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Ragnarok Online II since May 2007 and continue to upgrade and develop Ragnarok Online II in response to market feedback received during the testing and development phase. We have entered into license and distribution agreements for Ragnarok Online II with six licensees in ten countries, including Thailand, Japan, Taiwan, Philippines, Singapore, Malaysia, Vietnam, China, Indonesia and Brazil beginning from the end of 2006. While we currently expect to launch the game in the first half of 2010, no assurance can be given that we can meet this anticipated launch date or, if there is any further delay in the launch date, such delay would not result in termination of any of the existing license agreements for Ragnarok Online II. See ITEM 3.D. RISK FACTORS RISKS RELATING TO OUR BUSINESS If we are unable to consistently and timely develop, acquire, license, launch, market or operate commercially successful online games in addition to Ragnarok Online, our business, financial condition and results of operations may be materially and adversely affected.

### ***Time N Tales***

We commercially launched Time N Tales in July 2006 under a publishing agreement entered into with Ndoors Corp., a Korean online game developer, in November 2005. The amount of revenues from Time N Tales in 2008 and 2007 represented less than 1% of our total revenues in 2008 and 2007, respectively. We terminated our agreement with Ndoors Corp in January 2009 and stopped offering Time N Tales in March 2009.

### **Casual online games**

Casual online games can fit in to any genre and have any type of game play. They are targeted at mass audience of casual online gamers and generally distinguished by simple rules and lack of commitment required in contrast to more complex and hardcore massively multiplayer online role playing games. Currently, we commercially offer one casual online game, Pucca Racing. We stopped offering two casual games, Love Forty and TV Boyz through our casual online game portal site, STYLIA, in September 2008.

### ***Pucca Racing***

We commercially launched Pucca Racing in Korea and in Thailand in September 2007 and March 2008, respectively. Pucca Racing was co-developed by us and Vooz Co., Ltd., which originally designed the Pucca characters. We entered into license and distribution agreements for Pucca Racing in Thailand with Ini 3 Digital Co., Ltd. in January 2008, in Taiwan and Hong Kong with M-etel Co., Ltd. in October 2008. The most distinguishing characteristic of the game is its simple game play based on classic bike racing, allowing players of all age groups to freely enjoy the game. Players can apply various control techniques to achieve fast acceleration and lively movements based on performance differences across a wide selection of bikes. Pucca Racing incorporates the use of famous race tracks from countries around the world which we believe makes the game unique and fun to play. The amount of revenues from Pucca Racing in 2008 and 2007 represented less than 1% of our total revenues in each of 2008 and 2007.

### ***STYLIA***

Through STYLIA, a casual online game portal site operated by us, we offered until September 2008, two casual games, Love Forty, an online tennis game, and TV Boyz, a three-dimensional action game. The amount of revenues from these two games in 2008 and 2007 represented less than 1% of our total revenues in each of 2008 and 2007. We terminated our publishing agreement with Sonnori Co., Ltd. in August 2008 and stopped the service of these two games and STYLIA in September 2008.

### **Ice Age Online**

We are also in the process of working with a third-party developer to develop Ice Age Online, our first massively multiplayer online game, which allows interaction among a large number of players within a virtual game world, but without the role playing capability among users present in massively multiplayer online role playing games.

Ice Age Online is expected to be an Adobe Flash based massively multiplayer online game featuring strong social network features that is intended to target children aged from six to twelve. Ice Age Online, when launched is

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expected to offer a virtual world with characters and fields (backgrounds) based on three popular animated motion pictures: Ice Age, Ice Age: The Meltdown and Ice Age: Dawn of the Dinosaurs. We licensed the right to use the theme, characters and storyline from 20th Century Fox Licensing & Merchandising. Ice Age Online is expected to allow players to create new characters within the animation, play various mini-games, make new friends and earn Acorns as in-game currency. With Acorns, players will be able to buy various items and customize their characters and/or My Room, virtual personal space for users. While we currently expect to start open beta testing and commercial launch of Ice Age Online in November 2009 and in mid December 2009, respectively, there may be unanticipated delays to our development schedule and no assurance can be given that we will be able to meet our current schedule.

**Mobile games**

As compared to massively multiplayer online role playing games, mobile games, which are played using mobile phones and other mobile devices, have shorter game playtime and less complex user-game interaction. We believe that mobile games, due to such characteristics, provide less-experienced users with a means to become familiar with both game playing and the game culture without making a substantial commitment in time and resources. As a result, we believe that mobile games allow us to target a broader audience of users, help us to expand the online game culture beyond Internet cafés and users' homes and act as an effective marketing tool to attract new users to our massively multiplayer online role playing games. We develop and distribute our mobile games through our subsidiary in Korea, NeoCyon, Inc.

The following are revenues generated from our mobile business for the periods indicated:

Country	Year Ended December 31,				
	2006	2007	2008	2008	2008(1)
	(In millions of Won and thousands of US\$, except percentages) (Unaudited)				
Korea	₩ 3,722	₩ 3,673	₩ 4,573	66.5%	US\$ 3,581
Japan	59	390	2,309	33.5	1,808
United States/Canada	39				
Others	20				
Total	₩ 3,840	₩ 4,063	₩ 6,882	100.0%	US\$ 5,389

*Note:*

- (1) For convenience only, the Won amounts are expressed in U.S. dollars at the rate of Won 1,277.0 to US\$1.00, the noon buying rate as quoted by the Federal Reserve Bank of New York in effect on April 30, 2009.

***Game-related products and services****Animation*

Gravity Entertainment, our Japanese subsidiary, entered into an agreement with G&G Entertainment Inc. and three other Japanese media and entertainment companies for the production and distribution of 26 half-hour episode

animation series based on the storyline and characters of Ragnarok Online. The series was produced by Gravity Entertainment and broadcast on television in nine countries from 2004 through 2007. We also entered into an agreement to broadcast the series in Thailand in December 2004. The animation series of Ragnarok Online has been sold in DVD and VOD (video on demand) formats in North America since March 2006 and it has also been distributed in Europe. In addition to the potential revenue generated from the sale of broadcasting rights, videos, DVDs and Internet viewing, we believe that our animation products will enhance the brand recognition of Ragnarok Online and facilitate cross-selling of other products. Our revenues from our animation business was Won 255 million (US\$200 thousand) in 2008 and Won 33 million in 2007, which represented less than 1% of our total revenues in 2008 and 2007, respectively.

**Table of Contents***Game character merchandising*

In order to optimize the commercial opportunities presented by the popularity of Ragnarok Online and its characters, we and our licensees have been marketing dolls, stationery and other character-based merchandise, as well as game manuals, monthly magazines and other publications, based on the game. We have entered into arrangements with nine Korean vendors and eleven overseas vendors to license Ragnarok's animation characters in Korea, Japan, the United States, Taiwan, Hong Kong, China, Thailand, the Philippines, Indonesia, Singapore, Malaysia and Brazil. In Japan, we have been conducting game character merchandising by selling game packages, which package our online game software in CD or DVD format for PC users, in connection with game distribution. We also market the merchandise through convenience stores where, such as in China and many Southeast Asian countries, prepaid game cards for our games are sold. We have also entered into arrangements to license Emil Chronicle Online in Korea.

The total amount of license fees from our contracts with Korean vendors was approximately Won 101 million (US\$79 thousand) in 2008, compared with Won 377 million in 2007, and the total amount of license fees from our contracts with overseas vendors was approximately Won 992 million (US\$777 thousand) in 2008, compared with Won 470 million in 2007. We intend to expand our character marketing for our new games as they are launched.

The following are revenues generated from game character merchandising for the periods indicated:

Country	Year Ended December 31,				
	2006	2007	2008	2008	2008(1)
	(In millions of Won and thousands of US\$, except percentages)				
	(Unaudited)				
Korea	₩ 201	₩ 377	₩ 101	9.2%	US\$ 79
Japan	1,075	470	975	89.3	764
Taiwan/Hong Kong	34		17	1.5	13
Others	73				
Total	₩ 1,383	₩ 847	₩ 1,093	100.0%	US\$ 856

*Note:*

- (1) For convenience only, the Won amounts are expressed in U.S. dollars at the rate of Won 1,277.0 to US\$1.00, the noon buying rate as quoted by the Federal Reserve Bank of New York in effect on April 30, 2009.

*Multiplatform and internet protocol television games*

In December 2006, we entered into a licensing agreement with GungHo Online Entertainment, Inc. to develop and distribute Ragnarok DS, a Nintendo DS version of Ragnarok Online. Ragnarok DS was released in Japan and in Korea in December 2008 and June 2009, respectively. We intend to release Ragnarok DS in North America in 2009.

We are also expanding our business by providing our online games on internet protocol television, or IPTV. In September 2008, we entered into a licensing agreement with Iconix Entertainment Co., Ltd. to develop and publish an IPTV game based on Iconix's 3D TV animation series Pororo: The Little Penguin. We expect to launch Pororo Game, an IPTV game in July 2009.



## **OUR MARKETS**

Japan, Korea, the United States and Canada, Taiwan and Hong Kong, and Russia were our biggest geographic markets in 2008 in terms of revenue. Each of these markets is serviced either by us or a distribution company. We directly manage game operations in Korea, and our wholly-owned subsidiaries, Gravity Interactive and Gravity CIS manage game operations in the United States and Canada, and Russia and CIS countries. For Ragnarok Online, GungHo Entertainment Inc. is our licensee for Japan and Soft-World International Corporation is our licensee for Taiwan and Hong Kong. For Emil Chronicle Online, GameCyber Technology Ltd. is our licensee for Taiwan and Hong Kong.

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The following table sets forth a summary of our consolidated statement of operations showing revenues by geographic area for the periods indicated and the percentage represented by such revenues for year ended December 31, 2008.

Countries	Year Ended December 31,				
	2006	2007	2008	2008	2008(1)
	(In millions of Won and thousands of US\$, except percentages)				
	(Unaudited)				
Japan	₩ 16,913	₩ 18,899	₩ 27,037	50.8%	US\$ 21,172
Korea	10,155	11,119	14,009	26.3	10,970
United States/Canada	2,868	2,614	3,620	6.8	2,835
Taiwan/Hong Kong	4,092	2,369	2,301	4.3	1,802
Russia and CIS countries	6.0	489	1,078	2.0	844
Others	6,929	4,739	5,125	9.8	4,014
Total	₩ 40,963	₩ 40,229	₩ 53,170	100.0%	US\$ 41,637

*Note:*

- (1) For convenience only, the Won amounts are expressed in U.S. dollars at the rate of Won 1,277.0 to US\$1.00, the noon buying rate as quoted by the Federal Reserve Bank of New York in effect on April 30, 2009.

***Korea***

In Korea, we commercially launched and began to charge subscribers for Ragnarok Online in August 2002, R.O.S.E. Online in January 2005, Love Forty and TV Boyz in June 2006, Time N Tales in July 2006, Emil Chronicle Online in August 2007, Pucca Racing in September 2007 and Requiem in October 2007. Our game subscribers in Korea consist of individual PC account subscribers and Internet café subscribers. Individual PC account subscribers are individuals who log on to our game servers from places other than Internet cafés, such as from home or work, whereas Internet café subscribers are commercial businesses operating Internet café outlets equipped with multiple PCs that provide broadband Internet access to their customers who typically prefer to play the most up-to-date versions of online games. Most Internet cafés charge their customers PC usage and Internet access fees that generally range from Won 700 to Won 1,200 per hour and subscribe to various online games. Over 6,400 and 6,000 Internet cafés offered our games in Korea according to our internal data as of December 31, 2008 and 2007, respectively. In order to offer our games, an Internet café typically purchases minimum game hours from us. The subscription collected from Internet cafés accounted for 14.6% and 13.8% of our subscription revenues in Korea in 2008 and 2007, respectively.

***Overseas markets***

Ragnarok Online is commercially offered in the following 37 overseas countries and markets: Japan, China, Taiwan, Hong Kong, United States, Canada, Australia, New Zealand, Singapore, Malaysia, Thailand, the Philippines, Indonesia, Germany, Austria, Switzerland, Italy, Turkey, Brazil, France, Belgium, Vietnam, Armenia, Azerbaijan, Belorussia, Estonia, Georgia, Kazakhstan, Kyrgyzstan, Latvia, Lithuania, Moldova, Russia, Tajikistan, Turkmenistan, Ukraine and Uzbekistan. Ragnarok Online is distributed through local game operators and distributors, except for the countries in which our subsidiaries directly publish Ragnarok Online, such as Gravity Interactive in the United States, Canada, Australia, and New Zealand; Gravity CIS in Russia and CIS countries; and Gravity EU in France and

Belgium. In June 2008, we made an amendment to our license and distribution agreement with Gravity EU to include the United Kingdom, Finland, Sweden, Norway, Ireland, Scotland, Denmark and Spain as service territory and currently plan to conduct closed beta testing of Ragnarok Online in these countries.

In January 2009, we also entered into license and distribution agreement for Ragnarok Online in the following 20 countries: United Arab Emirates, Saudi Arabia, Jordan, Kuwait, Syria, Bahrain, Qatar, Palestine, Oman, Lebanon, Libya, Sudan, Mauritania, Iraq, Yemen, Iran, Egypt, Algeria, Morocco and Tunisia with Tahadi Games Ltd. We are currently in the process of conducting open beta testing of the game in some of these countries.

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The following table lists the overseas countries in which Ragnarok Online is commercially offered through our licensees, the names of the licensees, the dates of the license agreements, and the commercial launch date and expiry date of the license agreements.

<b>Country</b>	<b>Licensee</b>	<b>Date of License Agreement</b>	<b>Date of Commercial Launch</b>	<b>Date of Expiry</b>
Japan	GungHo Online Entertainment, Inc.	July 2002	December 2002	August 2009(1)
Taiwan/Hong Kong(2)	Soft-World International Corporation	May 2002	October 2002	October 2009(3)
Thailand	AsiaSoft Corporation Public Co., Ltd.(4)	June 2002	March 2003	March 2010(5)
China	Shengqu Information Technology (Shanghai) Co., Ltd.(6)	July 2005	May 2003	August 2010(7)
Singapore/Malaysia(2)	Game Flier (Malaysia) Sdn. Bhd.(8)	May 2003	April 2004	October 2009(9)
Philippines	Level Up! Inc.	March 2003	September 2003	August 2010(10)
Indonesia	PT. Lyto Datarindo Fortuna(11)	April 2004	November 2003	February 2010(12)
Europe((13)	Burda:ic GmbH	November 2003	April 2004	April 2010(14)
Brazil	Level Up! Interactive S.A.	August 2004	February 2005	March 2011(15)
India(16)	Level Up! International Holdings Pte. Ltd.(17)	May 2004	March 2006	June 2009(18)
Vietnam	AsiaSoft Corporation Public Co., Ltd. (4)(19)	July 2008	April 2007	December 2010

*Notes:*

- (1) Renewed in August 2006.
- (2) Governed under a single license agreement covering both markets.
- (3) Renewed in October 2007.
- (4) Formerly known as AsiaSoft International Company Ltd. Changed its name in May 2008.
- (5) Renewed in March 2008.
- (6) Shengqu is a wholly-owned subsidiary of Shanda Interactive Entertainment Ltd., previously with different licensee.
- (7) Renewed in September 2008.
- (8) Game Flier (Malaysia) Sdn. Bhd. is a wholly-owned subsidiary of Soft-World International Corporation.

- (9) Renewed in October 2007.
- (10) Renewed in September 2008.
- (11) Previously with a different licensee.
- (12) Renewed in February 2008.
- (13) Represents massively multiplayer online role playing game operations in Germany, Austria, Switzerland, Italy and Turkey. A single operator services these five countries under one license agreement.

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- (14) Original license agreement was entered into with Burda Holding International GmbH, a 100% subsidiary of Hubert Burda Media, in November 2003, which was transferred to Burda Interactive Communities GmbH, an affiliate of Hubert Burda Media in February 2007, and renewed in April 2007 for additional one year terms under mutual consent of the Company and Burda Interactive Communities GmbH. Burda Interactive Communities changed its name to Burda:ic GmbH in May 2007 and license agreement with Burda:ic GmbH was renewed in April 2008 with the same terms and conditions of the existing license agreement, except adding automatic renewal provision, for a term from April 2008 to April 2009 with one additional renewal term of one year through April 2010. The license agreement was automatically renewed in April 2009.
- (15) Renewed in March 2009.
- (16) We commercially launched Ragnarok Online in India through Level Up! Network India Pvt. Ltd. in March 2006. The licensee in India was changed to Level Up! International Holdings Pte. Ltd. in May 2008 and the game services were suspended in August 2008. We are currently pursuing various other options in India and expect to find an alternative licensee in the near future.
- (17) Previously with a different licensee.
- (18) Renewed in June 2008.
- (19) Previously with a different licensee.

R.O.S.E. Online is currently commercially offered in the United States, Canada and Mexico. Emil Chronicle Online is currently commercially offered in Thailand, Hong Kong and Taiwan. Pucca Racing is commercially offered in Thailand. Requiem is commercially offered in the United States, Canada, Armenia, Azerbaijan, Belorussia, Estonia, Georgia, Kazakhstan, Kyrgyzstan, Latvia, Lithuania, Moldova, Russia, Tajikistan, Turkmenistan, Ukraine and Uzbekistan. See ITEM 4.B. BUSINESS OVERVIEW OUR PRODUCTS.

Our licensees pay us:

an initial license fee for initial set-up costs, technical support and advisory services that we provide until commercial launch; and

ongoing royalty payments based on a percentage of revenues generated from subscription of the game they service in the respective overseas markets.

In addition, if the license agreement is renewed, we typically negotiate a renewal license fee. The license agreements may be terminated in the event of bankruptcy or a material breach by either party, including by us if the licensee fails to pay royalty fees in a timely manner.

**PRICING STRUCTURE AND PAYMENT SYSTEM**

Our overseas licensees generally develop, after consultation with us, a retail pricing structure for the users of the game they service in their respective markets. Pricing structures are determined primarily based on the cost of publishing and operating the game, the playing and payment patterns of the users, the pricing of competing games in a given market and the purchase power parity of consumers in that market. Since the launch of Ragnarok Online in August 2002, we have tracked and accumulated user data generated from our user base, which provide us with an extensive database to analyze user patterns and establish pricing for other markets. The pricing for Ragnarok Online has

remained generally stable in each of our markets since the respective dates of Ragnarok Online's commercial launch in those markets.

In December 2006, we started to apply a micro-transaction system (or sale of virtual in-game items model) as an additional business model, by providing virtual item shops in the games where players can purchase a wide array of items to customize, personalize and enhance their characters and game playing experiences. The micro-transaction model has been introduced in all the countries and markets where Ragnarok Online is serviced except Germany, Austria, Switzerland, Italy and Turkey. We intend to extend our micro-transaction model to other markets. In addition, since January 2007, we have opened free-to-play servers, which only applies the micro-transaction model, in all the countries and markets where Ragnarok Online is serviced except Japan, France, Belgium, Germany, Austria, Switzerland, Italy and Turkey to encourage the players to download and play Ragnarok Online without paying subscription fees or buying playing time and to purchase in-game items pursuant to our

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micro-transaction model. In Russia and Vietnam, we offer our game services with the micro-transaction model only. We also intend to extend free-to-play servers into other markets. The amount of revenue generated from micro-transactions as a percentage of revenue per month from each country varies monthly. For example, the percentage of per month revenue derived from micro-transactions ranged from 24.0% to 42.8% of total monthly royalty revenues for Japan during 2008, 45.2% to 73.4% of total monthly royalty revenues for the United States and Canada during 2008, 57.8% to 75.3% of total monthly royalty revenues for Thailand during 2008, 72.3% to 81.4% of total monthly royalty revenues for Indonesia during 2008, 22.7% to 75.1% of total monthly royalty revenues for Russia during 2008, 17.2% to 68.6% of total monthly royalty revenues for France and Belgium from September 2008 through December 2008 and 42.0% to 74.4% of total monthly revenues for Korea during 2008. As we establish and refine our micro-transaction model internally and with our licensees, we plan to be able to provide reliable micro-transaction data for our other principal markets in the future. The pricing for Ragnarok Online in Korea and our principal overseas markets, Japan, the United States and Canada, Taiwan and Hong Kong, Thailand and China are set forth below:

**Korea**

Individual PC subscribers in Korea can choose from a number of alternative payment options, including charges made through mobile or fixed telephone service provider payment systems, prepaid cards, gift certificates, online credit card payments and bank transfers. We pay a commission in the range of 1.8% to 15% to third parties to process payments. These third parties bear the delinquency risk associated with payments from subscribers.

*Subscription-based fee model*

We determine the pricing plan for Ragnarok Online in Korea. We offer separate pricing plans to Internet cafés and individual PC account subscribers. Our subscribers have an option to pay an hourly fee or a flat monthly fee. The following table sets forth our published pricing plans in Korea for Ragnarok Online access as of December 31, 2008.

		<b>Subscription Fees</b>	
<b>Individual PC users</b>			
Flat-fee rate	1 month	₩	19,800
	2 months		37,600
	3 months		53,500
	6 months		101,000
Hourly-fee rate	5 hours		3,300
	20 hours		8,800
		<b>Number of PCs</b>	<b>Flat Fee per PC</b>
<b>Internet cafés(1)</b>			
Hourly-fee rate	300 hours	₩	69,300
	600 hours		138,600
	1,000 hours		231,000
	2,000 hours		462,000

*Note:*



- (1) Actual monthly and hourly-rate fees may vary depending on discounts we offer based on volume of use by the subscriber.

Approximately 87.5% of our revenues from Ragnarok Online in Korea in 2008 were derived from subscriptions by individual PC users and the remaining 12.5% was derived from Internet cafés.

**Table of Contents***Micro-transaction model*

We have applied a micro-transaction model in Korea since April 2007. Game users buy RO Cash, the currency of the money used in Ragnarok Online which enable them to buy game items. The price range of each of the game items is between Won 200 and 9,800 for paid servers and between Won 250 and 14,700 for free-to-play servers.

The pricing for Ragnarok Online in our principal overseas markets, Japan, the United States and Canada , Taiwan and Hong Kong, Thailand and China is as follows:

*Japan*

Users in Japan typically pay for access to Ragnarok Online with credit cards or cyber money, which is increasingly becoming a popular payment method in Japan.

*Subscription-based fee model*

Our licensee in Japan, GungHo offers only one rate for Ragnarok Online and charges Japanese Yen 1,500 per 30 days of unlimited use.

*Micro-transaction model*

We have applied a micro-transaction model in Japan since December 2006. Game users buy points which enable them to buy game items. The range of the game items is between JPY 50 and 1,500(1).

<b>Points</b>	<b>Retail Price(1)</b>
10,000 points	JPY 1,000
21,000 points	2,000
32,500 points	3,000
55,000 points	5,000
112,000 points	10,000

*Note:*

- (1) For your reference only, as of April 30, 2009, the noon buying rate of Japanese Yens to U.S. dollars quoted by the Federal Reserve Bank of New York was JPY 98.76 to US\$1.00.

**The United States and Canada**

Gravity Interactive, our wholly-owned subsidiary in the United States, permits users to access Ragnarok Online using credit cards, money orders, wire and/or bank transfers and Gravity Game Card, a prepaid card.

*Subscription-based fee model*

The following table sets forth Gravity Interactive's published basic pricing for Ragnarok Online access in the United States and Canada as of December 31, 2008:

<b>Hours or Month</b>	<b>Retail Price</b>		
	<b>Money Order</b>	<b>Wire/Bank Transfer</b>	<b>Credit Card/Debit Card</b>
30 hours	US\$ 9.99	US\$ 8.99	US\$ 7.99
1 month	13.99	12.99	12.00
3 months	35.98	33.99	32.00
6 months	63.48	59.99	57.00

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The following table sets forth Gravity Interactive's published basic pricing for the Gravity Game Card.

<b>Subscription Plan</b>	<b>Price</b>	
14 Day Plan	US\$	5 Gravity Game Card
45 Day Plan	US\$	15 Gravity Game Card
90 Day Plan	US\$	30 Gravity Game Card

***Micro-transaction model***

We have applied a micro-transaction model in the United States and Canada since June 2007. Game users buy points which enable them to buy game items through credit cards and wire and/or bank transfers. The range of the game items is between US\$0.25 and 22 for paid servers and between US\$0.3 and 27.5 for free-to-play servers. The following table sets forth our licensee's published basic pricing for points of Ragnarok Online in the United States and Canada as of December 31, 2008.

<b>Points</b>	<b>Retail Price</b>	
500 points	US\$	4.99
1,050 points		9.99
1,650 points		14.99
2,300 points		19.99
5,200 points		39.99
10,400 points		74.99

In addition, the following table sets forth Gravity Interactive's published basic pricing for the Gravity Game Card to be used only for buying points for users of a micro-transaction model.

<b>Points</b>	<b>Price</b>	
525 points	US\$	5 Gravity Game Card
1,650 points	US\$	15 Gravity Game Card
3,900 points	US\$	30 Gravity Game Card

**Taiwan and Hong Kong**

In Taiwan and Hong Kong, most users purchase prepaid debit point cards to access Ragnarok Online. The prepaid cards can be purchased online, by mobile phones or at convenience stores, Internet cafés and at other locations.

Taiwan has websites dedicated to selling prepaid cards for various uses, including online game payments, which is also used by users in Hong Kong to change their prepaid cards and to buy points.

***Subscription-based fee model***

Our licensee in Taiwan and Hong Kong, Soft-World International Corporation, generally does not offer a separate subscription plan for Internet café outlets. Our licensee in Taiwan and Hong Kong currently offers approximately 200 different rates for Ragnarok Online.

The following table sets forth our licensee's published basic pricing for Ragnarok Online access in Taiwan as of December 31, 2008:

<b>Points(1) or Days</b>	<b>Retail Price(2)</b>
150 points	NT \$ 150
350 points	350
400 points	400
450 points	450
500 points	500
1,000 points	1,000
30 days	350

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The following table sets forth our licensee's published basic pricing for Ragnarok Online access in Hong Kong as of December 31, 2008:

<b>Points(1) or Days</b>	<b>Retail Price(3)</b>	
50 points	HK\$	12
150 points		39
350 points		88
400 points		98
450 points		113
1,000 points		250

*Notes:*

- (1) Each time a user logs onto Ragnarok Online, 20 points are deducted. After a user's playtime exceeds 12 hours, additional 20 points are deducted for every 12 hours of use.
- (2) For your reference only, as of April 30, 2009, the noon buying rate of NT dollars to U.S. dollars quoted by the Federal Reserve Bank of New York was NT\$33.06 to US\$1.00.
- (3) For your reference only, as of April 30, 2009, the noon buying rate of Hong Kong dollars (HK\$) to U.S. dollars quoted by the Federal Reserve Bank of New York was HK\$7.75 to US\$1.00.

***Micro-transaction model***

We have applied a micro-transaction model in Taiwan and Hong Kong since December 2006. Game users buy points which enable them to buy game items. The price range of each of the game items is between NT\$1 and 899 for paid servers and between NT\$1 and 999 for free-to-play servers. Users in Hong Kong also buy points based on NT dollars.

**Thailand**

Our licensee in Thailand, Asiasoft International Company Ltd., permits users to access Ragnarok Online through prepaid cards or by mobile and electronic payment. Most of the users use prepaid cards to access Ragnarok Online. Each prepaid card has a specified maximum number of hours or days of use. Users can purchase prepaid cards from automated teller machines, Internet cafés or convenience stores.

***Subscription-based fee model***

The following table sets forth our licensee's published basic pricing for Ragnarok Online access in Thailand as of December 31, 2008:

<b>Hours or Days</b>	<b>Points</b>	<b>Retail Price(1)</b>
5 hours	2,800	THB 28
10 hours	5,500	55
20 hours	8,900	89

40 hours	15,900	159
15 days	18,900	189
20 days	24,500	245
No limit within 30 days	34,900	349
40 days	45,000	450
No limit within 90 days	88,800	888

*Note:*

- (1) For your reference only, as of April 30, 2009, the noon buying rate of the Thai Bahts to U.S. dollars quoted by the Federal Reserve Bank of New York was THB 35.23 to US\$1.00.

**Table of Contents*****Micro-transaction model***

We have applied a micro-transaction model in Thailand since February 2007. Game users buy points which enable them to buy game items. The price range of each of the game items is between THB 0.01 and 600.

**China**

Our licensee in China, Shanda Interactive Entertainment Limited, operates and offers Ragnarok Online through Shengqu Information Technology (Shanghai) Co., Ltd. its wholly-owned subsidiary. In China, Ragnarok Online can be accessed through prepaid cards. The prepaid card system was introduced to take account of the limited availability of online and credit card payment systems in China. A majority of Ragnarok Online players purchase prepaid debit point cards at Internet cafés or retail game outlets or purchase prepaid online credits by directly paying at Internet cafés, which in turn purchase online credits from our China licensee. Game users can choose between buying hours or days to play since each prepaid card contains a network access password to access Ragnarok Online from a PC at home or at an Internet café and to buy points which enable them to buy game items. Our licensee in China currently offers two different cards: (i) the Shanda Point Card, of which points and hours or days can be used for any game that our licensee publishes and (ii) the Ragnarok Point Card, of which points and hours or days are for Ragnarok Online only. Each prepaid card can be recharged through the licensee's website.

The following table sets forth our licensee's published basic pricing for the Shanda Point Card in China as of December 31, 2008:

<b>Points</b>	<b>Hours of Day</b>	<b>Retail Price(1)</b>
150 points	25 hours	CNY 10
450 points	75 hours	30
No limit within 30 days	30 days	45

The following table sets forth our licensee's published basic pricing for the Ragnarok Point Card as of December 31, 2008.

<b>Points</b>	<b>Hours of Day</b>	<b>Retail Price(1)</b>
60 points	10 hours	CNY 5
150 points	25 hours	10
No limit within 7 days	7 days	15
450 points	75 hours	30
No limit within 30 days	30 days	45

In addition, the following table sets forth our licensee's published basic pricing for the Ragnarok Point Card to be used only for buying points for users of a subscription-based fee model as of December 31, 2008.

<b>Points</b>	<b>Retail Price(1)</b>
500 points	CNY 5



1,000 points	10
3,500 points	35
4,500 points	45
10,000 points	100
30,	