

GRAVITY Co., Ltd.
Form 20-F
April 30, 2014

Use these links to rapidly review the document

[TABLE OF CONTENTS](#)

[INDEX TO FINANCIAL STATEMENTS](#)

[Table of Contents](#)

As filed with the Securities and Exchange Commission on April 30, 2014

**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, 2013

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)

**15F, 396 World Cup buk-ro, Mapo-gu,
Seoul 121-795, Korea**

(Address of principal executive offices)

Edgar Filing: GRAVITY Co., Ltd. - Form 20-F

Heung Gon Kim
Chief Financial Officer
15F, 396 World Cup buk-ro, Mapo-gu,
Seoul 121-795, Korea
Telephone: 82-2-2132-7000
Fax: 82-2-2132-7070

(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 depository shares, each representing one-fourth of a share of common stock | The NASDAQ Global Market |

* Not for trading, but only in connection with the listing of American depository 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 issued 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

Table of Contents

TABLE OF CONTENTS

| | | |
|-------------------|---|------------|
| <u>PART I</u> | | <u>6</u> |
| <u>ITEM 1.</u> | <u><i>IDENTITY OF DIRECTORS, SENIOR MANAGEMENT AND ADVISERS</i></u> | <u>6</u> |
| <u>ITEM 2.</u> | <u><i>OFFER STATISTICS AND EXPECTED TIMETABLE</i></u> | <u>6</u> |
| <u>ITEM 3.</u> | <u><i>KEY INFORMATION</i></u> | <u>6</u> |
| <u>ITEM 3.A.</u> | <u>Selected Financial Data</u> | <u>6</u> |
| <u>ITEM 3.B.</u> | <u>Capitalization and Indebtedness</u> | <u>8</u> |
| <u>ITEM 3.C.</u> | <u>Reasons for the Offer and Use of Proceeds</u> | <u>8</u> |
| <u>ITEM 3.D.</u> | <u>Risk Factors</u> | <u>8</u> |
| <u>ITEM 4.</u> | <u><i>INFORMATION ON THE COMPANY</i></u> | <u>27</u> |
| <u>ITEM 4.A.</u> | <u>History and Development of the Company</u> | <u>27</u> |
| <u>ITEM 4.B.</u> | <u>Business Overview</u> | <u>28</u> |
| <u>ITEM 4.C.</u> | <u>Organizational Structure</u> | <u>67</u> |
| <u>ITEM 4.D.</u> | <u>Property, Plants and Equipment</u> | <u>67</u> |
| <u>ITEM 4A.</u> | <u><i>UNRESOLVED STAFF COMMENTS</i></u> | <u>67</u> |
| <u>ITEM 5.</u> | <u><i>OPERATING AND FINANCIAL REVIEW AND PROSPECTS</i></u> | <u>68</u> |
| <u>ITEM 5.A.</u> | <u>Operating Results</u> | <u>68</u> |
| <u>ITEM 5.B.</u> | <u>Liquidity and Capital Resources</u> | <u>83</u> |
| <u>ITEM 5.C.</u> | <u>Research and Development, Patents and Licenses, Etc.</u> | <u>85</u> |
| <u>ITEM 5.D.</u> | <u>Trend Information</u> | <u>85</u> |
| <u>ITEM 5.E.</u> | <u>Off-Balance Sheet Arrangements</u> | <u>86</u> |
| <u>ITEM 5.F.</u> | <u>Tabular Disclosure of Contractual Obligations</u> | <u>86</u> |
| <u>ITEM 5.G.</u> | <u>Safe Harbor</u> | <u>87</u> |
| <u>ITEM 6.</u> | <u><i>DIRECTORS, SENIOR MANAGEMENT AND EMPLOYEES</i></u> | <u>87</u> |
| <u>ITEM 6.A.</u> | <u>Directors and Senior Management</u> | <u>87</u> |
| <u>ITEM 6.B.</u> | <u>Compensation</u> | <u>90</u> |
| <u>ITEM 6.C.</u> | <u>Board Practices</u> | <u>90</u> |
| <u>ITEM 6.D.</u> | <u>Employees</u> | <u>93</u> |
| <u>ITEM 6.E.</u> | <u>Share Ownership</u> | <u>94</u> |
| <u>ITEM 7.</u> | <u><i>MAJOR SHAREHOLDERS AND RELATED PARTY TRANSACTIONS</i></u> | <u>95</u> |
| <u>ITEM 7.A.</u> | <u>Major Shareholders</u> | <u>95</u> |
| <u>ITEM 7.B.</u> | <u>Related Party Transactions</u> | <u>95</u> |
| <u>ITEM 7.C.</u> | <u>Interests of Experts and Counsel</u> | <u>99</u> |
| <u>ITEM 8.</u> | <u><i>FINANCIAL INFORMATION</i></u> | <u>99</u> |
| <u>ITEM 8.A.</u> | <u>Consolidated Statements and Other Financial Information</u> | <u>99</u> |
| <u>ITEM 8.B.</u> | <u>Significant Changes</u> | <u>100</u> |
| <u>ITEM 9.</u> | <u><i>THE OFFER AND LISTING</i></u> | <u>100</u> |
| <u>ITEM 9.A.</u> | <u>Offer and Listing Details</u> | <u>100</u> |
| <u>ITEM 9.B.</u> | <u>Plan of Distribution</u> | <u>101</u> |
| <u>ITEM 9.C.</u> | <u>Markets</u> | <u>101</u> |
| <u>ITEM 9.D.</u> | <u>Selling Shareholders</u> | <u>101</u> |
| <u>ITEM 9.E.</u> | <u>Dilution</u> | <u>101</u> |
| <u>ITEM 9.F.</u> | <u>Expenses of the Issue</u> | <u>101</u> |
| <u>ITEM 10.</u> | <u><i>ADDITIONAL INFORMATION</i></u> | <u>102</u> |
| <u>ITEM 10.A.</u> | <u>Share Capital</u> | <u>102</u> |
| <u>ITEM 10.B.</u> | <u>Memorandum and Articles of Incorporation</u> | <u>102</u> |
| <u>ITEM 10.C.</u> | <u>Material Contracts</u> | <u>107</u> |
| <u>ITEM 10.D.</u> | <u>Exchange Controls</u> | <u>110</u> |
| <u>ITEM 10.E.</u> | <u>Taxation</u> | <u>112</u> |
| <u>ITEM 10.F.</u> | <u>Dividends and Paying Agents</u> | <u>124</u> |
| <u>ITEM 10.G.</u> | <u>Statement by Experts</u> | <u>124</u> |

Table of Contents

| | | |
|-------------------|---|------------|
| <u>ITEM 10.H.</u> | <u>Documents on Display</u> | <u>124</u> |
| <u>ITEM 10.I.</u> | <u>Subsidiary Information</u> | <u>124</u> |
| <u>ITEM 11.</u> | <u>QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK</u> | <u>124</u> |
| <u>ITEM 12.</u> | <u>DESCRIPTION OF SECURITIES OTHER THAN EQUITY SECURITIES</u> | <u>125</u> |
| <u>ITEM 12.A.</u> | <u>Debt Securities</u> | <u>125</u> |
| <u>ITEM 12.B.</u> | <u>Warrants and Rights</u> | <u>125</u> |
| <u>ITEM 12.C.</u> | <u>Other Securities</u> | <u>125</u> |
| <u>ITEM 12.D.</u> | <u>American Depositary Shares</u> | <u>125</u> |
| <u>PART II</u> | | <u>127</u> |
| <u>ITEM 13.</u> | <u>DEFAULTS, DIVIDEND ARREARAGES AND DELINQUENCIES</u> | <u>127</u> |
| <u>ITEM 14.</u> | <u>MATERIAL MODIFICATIONS TO THE RIGHTS OF SECURITY HOLDERS AND USE OF PROCEEDS</u> | <u>127</u> |
| <u>ITEM 15.</u> | <u>CONTROLS AND PROCEDURES</u> | <u>127</u> |
| <u>ITEM 16.</u> | <u>RESERVED</u> | <u>128</u> |
| <u>ITEM 16.A.</u> | <u>AUDIT COMMITTEE FINANCIAL EXPERT</u> | <u>128</u> |
| <u>ITEM 16.B.</u> | <u>CODE OF ETHICS</u> | <u>128</u> |
| <u>ITEM 16.C.</u> | <u>PRINCIPAL ACCOUNTANT FEES AND SERVICES</u> | <u>128</u> |
| <u>ITEM 16.D.</u> | <u>EXEMPTIONS FROM THE LISTING STANDARDS FOR AUDIT COMMITTEES</u> | <u>128</u> |
| <u>ITEM 16.E.</u> | <u>PURCHASES OF EQUITY SECURITIES BY THE ISSUER AND AFFILIATED PURCHASERS</u> | <u>129</u> |
| <u>ITEM 16.F.</u> | <u>CHANGE IN REGISTRANT'S CERTIFYING ACCOUNTANT</u> | <u>129</u> |
| <u>ITEM 16.G.</u> | <u>CORPORATE GOVERNANCE</u> | <u>129</u> |
| <u>ITEM 16.H.</u> | <u>MINE SAFETY DISCLOSURE</u> | <u>129</u> |
| <u>PART III</u> | | <u>129</u> |
| <u>ITEM 17.</u> | <u>FINANCIAL STATEMENTS</u> | <u>129</u> |
| <u>ITEM 18.</u> | <u>FINANCIAL STATEMENTS</u> | <u>129</u> |
| <u>ITEM 19.</u> | <u>EXHIBITS</u> | <u>130</u> |

Table of Contents

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 depository receipts that evidence our ADSs;

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

"China" or the "PRC" are to the People's Republic of China (excluding, for the purposes of this annual report on Form 20-F, Taiwan, Hong Kong and Macau, unless specifically indicated otherwise);

"Chinese Yuan" are to the currency of China;

"EUR" or "Euro" are to the currency of the Eurozone consisting of Austria, Belgium, Cyprus, Estonia, Finland, France, Germany, Greece, Ireland, Italy, Latvia, Luxembourg, Malta, the Netherlands, Portugal, Slovakia, Slovenia and Spain;

"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;

"Hong Kong" are to the Hong Kong Special Administrative Region of the PRC;

"Japanese Yen" or "JPY" are to the currency of Japan;

"Korea" are to the Republic of Korea;

"Macau" are to the Macau Special Administrative Region of the PRC;

"NT dollar" or "NT\$" are to the currency of Taiwan;

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

"Thai Baht" are to the currency of the Kingdom of Thailand;

"US\$," "U.S. dollar," or "Dollar" are to the currency of the United States of America; and

"Won," "Korean Won," or "₩" are to the currency of Korea.

For your convenience, and unless otherwise stated, this annual report contains translations of certain Won amounts into U.S. dollars at the noon buying rate in New York City for cable transfers in Korean Won as certified by the Federal Reserve Bank of New York for customs purposes in effect on December 31, 2013, which was Won 1,055.25 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, 2013 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," "planned," "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.

Table of Contents

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;

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

the effect that any global financial crisis or 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 expectations, 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 or mobile gaming culture; political changes; global economic events including, but not limited to, a significant downturn in the global economic and financial markets and a tightening of the global credit markets; changes in business and economic conditions; fluctuations in foreign exchange rates; fluctuations in the 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. Except as required by law, we undertake no obligation to update or revise any forward-looking statements, whether as a result of new information, future events or otherwise. All subsequent forward-looking statements attributable to us or any person acting on our behalf are expressly qualified in their entirety by the cautionary statements contained or referred to in this section.

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 our audited consolidated financial statements as of December 31, 2012 and 2013 and for the years ended December 31, 2011, 2012 and 2013, and the related notes included elsewhere in this annual report. The selected financial data as of December 31, 2012 and 2013 and for the years ended December 31, 2011, 2012 and 2013 are derived from our audited consolidated financial statements and the related notes thereto 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, | | | | | |
|--|---|---------------|---------------|-----------------|-----------------|---------------------|
| | 2009 | 2010 | 2011 | 2012 | 2013 | 2013 ⁽¹⁾ |
| | (In millions of Won and thousands of US\$, except share and per share data, operating data and percentages) | | | | | |
| Statements of operations | | | | | | |
| Revenues: | | | | | | |
| Online games subscription revenue | ₩ 12,674 | ₩ 9,908 | ₩ 11,556 | ₩ 10,150 | ₩ 8,206 | US\$ 7,776 |
| Online games royalties and license fees | 34,037 | 32,132 | 35,552 | 32,325 | 21,726 | 20,588 |
| Mobile games and applications ⁽²⁾ | 6,496 | 7,224 | 6,609 | 8,262 | 14,504 | 13,745 |
| Character merchandising, animation and other revenue ⁽²⁾ | 4,196 | 3,098 | 3,760 | 7,044 | 3,249 | 3,079 |
| Total revenues | 57,403 | 52,362 | 57,477 | 57,781 | 47,685 | 45,188 |
| Cost of revenues | 21,170 | 20,873 | 24,243 | 34,906 | 35,399 | 33,545 |
| Gross profit | 36,233 | 31,489 | 33,234 | 22,875 | 12,286 | 11,643 |
| Operating expenses: | | | | | | |
| Selling, general and administrative | 21,651 | 20,422 | 22,759 | 20,310 | 17,063 | 16,171 |
| Research and development | 1,799 | 4,652 | 4,136 | 7,018 | 6,131 | 5,810 |
| Impairment loss on intangible assets | 280 | 475 | 3,697 | 14,569 | 5,822 | 5,517 |
| Gain on disposal of equity method investments | | | | (528) | | |
| Gain on loss of control in a subsidiary | | | (548) | | | |
| Settlement cost of litigation | 1,649 | | 29 | | | |
| Operating income (loss) | 10,854 | 5,940 | 3,161 | (18,494) | (16,730) | (15,855) |
| Other income, net | 2,108 | 2,322 | 1,876 | 871 | 2,105 | 1,996 |
| Income (loss) before income tax expenses (benefit) and equity loss on investments | 12,962 | 8,262 | 5,037 | (17,623) | (14,625) | (13,859) |

Edgar Filing: GRAVITY Co., Ltd. - Form 20-F

| | | | | | | |
|---|---------|---------|----------|------------|------------|---------------|
| Income tax expenses (benefit) | 4,544 | 4,207 | (7,962) | 2,584 | 5,108 | 4,840 |
| Income (loss) before equity loss on investments | 8,418 | 4,055 | 12,999 | (20,207) | (19,733) | (18,699) |
| Equity loss on investments, net | (1,424) | (345) | (242) | (333) | (18) | (18) |
| Net income (loss) | 6,994 | 3,710 | 12,757 | (20,540) | (19,751) | (18,717) |
| Net income (loss) attributable to: | | | | | | |
| Non-controlling interest | 77 | (20) | (2,171) | (8,316) | (1,163) | (1,103) |
| Parent company | ₩ 6,917 | ₩ 3,730 | ₩ 14,928 | ₩ (12,224) | ₩ (18,588) | US\$ (17,614) |

Table of Contents

| | As of and for the Years Ended December 31, | | | | | |
|---|---|-----------|-----------|------------|------------|---------------------|
| | 2009 | 2010 | 2011 | 2012 | 2013 | 2013 ⁽¹⁾ |
| | (In millions of Won and thousands of US\$, except share and per share data, operating data and percentages) | | | | | |
| Earnings (loss) per share: | | | | | | |
| Basic and diluted per share | ₩ 995 | ₩ 537 | ₩ 2,148 | ₩ (1,759) | ₩ (2,675) | US\$ (2.53) |
| Basic and diluted per ADS ⁽³⁾ | 249 | 134 | 537 | (440) | (669) | (0.63) |
| Weighted average number of shares outstanding (basic and diluted) | 6,948,900 | 6,948,900 | 6,948,900 | 6,948,900 | 6,948,900 | 6,948,900 |
| Other comprehensive income (loss) | | | | | | |
| Foreign currency translation adjustment | (140) | 290 | (510) | (41) | (1,327) | (1,258) |
| Comprehensive income (loss) | 6,854 | 4,000 | 12,247 | (20,581) | (21,078) | (19,975) |
| Comprehensive income (loss) attributable to: | | | | | | |
| Non-controlling interest | 77 | (20) | (2,171) | (8,316) | (1,163) | (1,103) |
| Parent company | ₩ 6,777 | ₩ 4,020 | ₩ 14,418 | ₩ (12,265) | ₩ (19,915) | US\$ (18,872) |
| Balance sheet data: | | | | | | |
| Cash and cash equivalents | ₩ 51,333 | ₩ 44,122 | ₩ 42,430 | ₩ 36,455 | ₩ 31,222 | US\$ 29,588 |
| Total current assets | 82,899 | 76,343 | 71,833 | 67,929 | 58,651 | 55,582 |
| Property and equipment, net | 2,837 | 2,672 | 2,731 | 3,524 | 2,315 | 2,194 |
| Total assets | 102,438 | 125,490 | 132,878 | 110,555 | 87,765 | 83,170 |
| Total current liabilities | 8,248 | 14,065 | 12,062 | 10,375 | 11,400 | 10,804 |
| Total liabilities | 18,828 | 27,078 | 22,219 | 20,477 | 18,765 | 17,783 |
| Total parent company shareholders' equity | 83,396 | 87,416 | 101,834 | 89,569 | 69,335 | 65,705 |
| Non-controlling interest | 214 | 10,996 | 8,825 | 509 | (335) | (318) |
| Total equity | 83,610 | 98,412 | 110,659 | 90,078 | 69,000 | 65,387 |
| Selected operating data and financial ratios (unaudited): | | | | | | |
| Gross profit margin ⁽⁴⁾ | 63.1% | 60.1% | 57.8% | 39.6% | 25.8% | 25.8% |
| Operating profit margin ⁽⁵⁾ | 18.9% | 11.3% | 5.5% | (32.0)% | (35.1)% | (35.1)% |
| Net profit margin ⁽⁶⁾ | 12.0% | 7.1% | 26.0% | (21.2)% | (39.0)% | (39.0)% |

Notes:

- (1) For convenience only, the Won amounts are expressed in U.S. dollars at the rate of Won 1,055.25 to US\$1.00, the noon buying rate in effect on December 31, 2013 as certified by the Federal Reserve Bank of New York for customs purposes.
- (2) We reclassified certain revenue within Mobile games and applications revenue as Character merchandising, animation and other revenue in 2013 as this better represents the nature of the revenue. The same reclassification has been made to all prior periods to conform to the presentation of 2013. The reclassification has no effect on the Company's previously reported total net revenue and other line items on the consolidated financial statements.
- (3) Each ADS represents one-fourth of a share of common stock.
- (4)

Edgar Filing: GRAVITY Co., Ltd. - Form 20-F

Gross profit margin for each period is calculated by dividing gross profit by total net revenues for each period.

(5) Operating profit margin for each period is calculated by dividing operating income (loss) by total net revenues for each period.

(6) Net profit margin for each period is calculated by dividing net income (loss) attributable to parent company by total net revenues for each period.

Table of Contents**Exchange Rate Information**

The following table sets forth information concerning the noon buying rate as certified by the Federal Reserve Bank of New York for customs purposes for the years 2009 through 2013 and for each month during the previous six months through April 18, 2014 expressed in Won per U.S. dollar.

| Period | At End of Period | Average Rate⁽¹⁾ | High | Low |
|--------------------------------|-------------------------|-----------------------------------|-------------|------------|
| 2009 | 1,163.7 | 1,270.0 | 1,570.1 | 1,149.0 |
| 2010 | 1,130.6 | 1,158.7 | 1,253.2 | 1,104.0 |
| 2011 | 1,158.5 | 1,105.2 | 1,197.5 | 1,049.2 |
| 2012 | 1,063.2 | 1,119.6 | 1,185.0 | 1,063.2 |
| 2013 | 1,055.3 | 1,094.6 | 1,161.3 | 1,050.1 |
| October | 1,060.8 | 1,065.9 | 1,075.5 | 1,057.5 |
| November | 1,057.8 | 1,061.6 | 1,072.7 | 1,054.8 |
| December | 1,055.3 | 1,055.6 | 1,061.4 | 1,050.1 |
| 2014 | | | | |
| January | 1,080.4 | 1,067.1 | 1,083.7 | 1,050.3 |
| February | 1,066.0 | 1,071.3 | 1,084.3 | 1,062.1 |
| March | 1,064.7 | 1,070.5 | 1,079.6 | 1,064.1 |
| April (through April 18, 2014) | 1,037.4 | 1,046.0 | 1,058.3 | 1,035.4 |

Note:

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

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 a significant portion of our revenues.

A significant portion of our revenues has been and is currently derived from a single online game product, Ragnarok Online, which was commercially introduced in August 2002 and is currently commercially offered in 60 countries and markets. We derived Won 21,531 million (US\$20,404 thousand) in revenues from Ragnarok Online in 2013 and Won 32,308 million in revenues from Ragnarok Online in 2012, representing approximately 45.2% and 55.9% of our total revenues in 2013 and 2012, respectively.

Ragnarok Online has been in the market for twelve 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 Ragnarok Online's user base and subscription revenues and royalties. This will likely lead to a decline in our overall revenues, which would materially and adversely affect our business, financial condition and results of operations.

Table of Contents

If we are unable to consistently and timely develop, acquire, license, launch, market or operate commercially successful online and mobile 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 and mobile games in addition to Ragnarok Online in order to retain our existing users and attract new users. In addition to Ragnarok Online, we currently offer five other online games: Ragnarok Online II, Requiem, Dragonica, which is also known as Dragon Saga in the United States, Canada and South America except for Brazil, R.O.S.E. Online and Ragnarok Prequel. We also offer mobile games which are played using mobile phones, including smartphones such as Google Android compatible phones and the Apple iPhone as well as feature phones, and other mobile devices, such as tablet computers. We have entered into a license agreement to publish Weapons of the Gods, a massively multiplayer online role playing game, or MMORPG, in Korea with Shanghai Nineyou Interactive Community and Media Co., Ltd., and its two affiliated Chinese game developers and publishers, Shanghai Nineshine Information Technology Co., Ltd. and HitNorth International Limited.

None of our other online games to date has proven to be as commercially successful as Ragnarok Online, and none of our mobile games to date has been a great commercial success. Since the beginning of 2013, we stopped offering six online games, Ragnarok Online Guild Masters in May 2013, Emil Chronicle Online in July 2013, Finding Neverland Online in July 2013, Maestia in September 2013, Steal Fighter in February 2014 and H.A.V.E. Online in March 2014, as the games did not gain popularity. In particular, the lack of popularity or market acceptance of Ragnarok Online II in major markets could result in financial losses, including termination or amendments of license agreements, which could damage our reputation and have a material adverse effect on our business, prospects, financial condition and results of operations.

A game's commercial success largely depends on appealing to the tastes and preferences of a critical mass of users as well as the willingness of such users to purchase the game and/or in-game items, and to continue as paying subscribers, all of which are difficult to predict prior to a game's development and introduction. Developing games requires substantial development costs, including the costs of employing skilled developers and acquiring or developing game engines which enable the creation of games with the latest technological features. For us to succeed, we must acquire, license or develop promising games at acceptable costs and ensure technical support for the successful operation of such games. The online and mobile gaming industries are highly competitive and we may not be able to acquire, license or develop promising games at acceptable costs. In order to successfully distribute and operate a game, we also need a sizable game management and support staff, continued investment in technology and a substantial marketing budget. We cannot assure you that the games we develop or publish will be attractive to users or otherwise be commercially successful, launched as scheduled or able to successfully compete with games operated by our competitors. If we are not able to consistently develop, acquire, license, launch, market or operate commercially successful games, we may not be able to generate enough revenues to offset our initial development, acquisition, licensing or marketing costs, and our business, financial condition and results of operation may be materially and adversely affected.

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 and certain other countries 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 43.7% of our total revenues in 2013 and 54.3% of our total revenues in 2012. In particular, we are heavily dependent on one licensee for a significant portion of our revenues. In 2013, 38.2% of our total revenues was derived from GungHo Online Entertainment, Inc., or GungHo, our licensee in Japan, which is also our majority shareholder. Deterioration in our relationships with material licensees or material adverse changes in the terms of our licenses with such licensees will likely have a material adverse effect on our business, prospects, financial

Table of Contents

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 and mobile games developed or offered by our competitors, 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, we may not be able to terminate our license agreements or enter into a new license agreement with a different licensee and our revenues and net profit would be adversely impacted. Also, a failure to satisfy our obligation to provide technical and other consulting services to the licensees under the license agreements may negatively affect user satisfaction and loyalty and hinder our licensees' efforts to increase market share, which may lead the licensees to focus their attention on our competitors' games or request modifications to or terminate our licensing agreements and/or not renew expired license agreements.

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 contracts. Failure by our licensees to maintain a stable and efficient billing, recording, distribution and payment collection network in their respective markets may result in inaccurate recording of sales or insufficient collection of payments from such markets and may materially and adversely affect our financial condition and results of operations. Although we have audit rights, pursuant to our license agreements, to ensure that proper payment amounts are being recorded and remitted, such activities can be disruptive and time consuming and as a result we do not exercise such rights on a regular basis. 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.

In addition, disruptions in the political environments in which our licensees operate, including without limitation a deterioration in the relationship between Japan and China and political instability in Thailand, may have a negative impact on the business of our licensees and in turn materially and adversely affect our results of operations and financial condition.

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 result in, among others, a suspension of service of our games in such market which may result in user complaints and a decrease in the use of our game which would likely have a material adverse effect on our business, financial condition and results of operations.

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

Increased competition in the online and mobile game industries in our markets from existing and potential competitors 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 and mobile games and compete across various markets and regions. We expect more companies to enter the

Table of Contents

online and mobile game industries and a wider range of online and mobile games to be introduced in our current and future markets.

Our competitors in the online and mobile game industries vary in size from small companies to very large companies with dominant market shares. 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 do.

As the online and mobile game industries are characterized by rapid technological changes, especially in the technical capabilities of devices for mobile games, and changing interests and preferences of users, continuous investment is required to develop and publish new games. Also, as the online and mobile game industries in many of our markets are 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 and mobile 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 us, 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 offering 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, better 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."

Our investments in joint ventures or partnerships, or acquisitions of other companies, related to development or service of online and mobile 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 games. 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 December 2005, we entered into a limited liability partnership agreement to invest an aggregate amount of JPY1,000 million in Online Game Revolution Fund No. 1, a limited liability partnership which purpose was to invest in online games. In 2005, 2006, 2008 and 2009, we made contributions of JPY100 million, JPY150 million, JPY642 million and JPY18 million, respectively, to the partnership. We accounted for our partnership interest under equity method of accounting and recorded our partnership interest as an equity loss equal to Won 1,026 million, Won 5,119 million, Won 1,424 million, Won 358 million, Won 38 million, Won 51 million and Won 18 million in 2007, 2008, 2009, 2010, 2011, 2012 and 2013, respectively. On December 31, 2010, the term of the partnership expired and the liquidation of the partnership was completed in June 2013.

In June 2010, we acquired from Terabit Telecom Ltd., a Russia-based online game company, a 25% equity interest in Ingamba LLC, or Ingamba, a joint venture company established in April 2010 for online game service in Russia. We recorded Won 13 million as equity income of Ingamba in 2010 but Won 134 million and Won 25 million as equity loss of Ingamba in 2011 and 2012, respectively. In May 2012, we sold our 25% equity interest in Ingamba to Stylonos Technologies Ltd., the joint venture partner which owned the remaining 75% equity interest in Ingamba after its purchase thereof from Terabit Telecom Ltd. in December 2010. In October 2010, we acquired an aggregate of 50.83% of the total shares of Barunson Interactive Corporation, subsequently named Gravity Games Corporation, or Gravity Games, an online game developer in Korea, and increased our ownership in Gravity Games to 85.5% in August 2013. For

Table of Contents

details of impairment loss from Gravity Games, see ITEM 3.D. "RISK FACTORS RISKS RELATING TO OUR BUSINESS We could suffer losses due to asset impairment charges." Gravity EU SASU, our former wholly-owned subsidiary in France, was converted into a joint venture company in which we have a 25% equity interest, Gravity EU SAS, with Media-Participations Paris SA as the joint venture partner, in July 2011. We recorded Won 70 million and Won 257 million as equity loss of Gravity EU SAS in 2011 and 2012, respectively.

If our partners or the joint ventures and partnerships in which we and our partners have invested or companies acquired by us are unable to manage their investments, develop promising online and/or mobile games or market or operate commercially successful online and/or mobile games, such joint ventures and partnerships or companies will be unable to attain their investment, development or other business objectives, which may materially and adversely affect the value of our investments and commitments and which may have a material adverse effect on our business, 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 and mobile 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 and mobile game developers. We compete to attract and retain key personnel with other companies in the online and mobile game industries 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.

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 and mobile 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 use 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;

Table of Contents

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 such 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 fix any damage to our system. In addition, we cannot ensure that any measures we take against 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, real-time monitoring against possible intrusion and saving all logs, preventing any unauthorized access to servers, and using firewalls, server virtualization technology, which allows one physical server to be divided into multiple virtual servers, each of which functions individually as a complete and independent server, and encryption technology, we cannot ensure that the measures we have implemented will be effective against all hacking efforts.

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 Web sites against the threat of such computer viruses and to address and resolve any problems resulting from such viruses. 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 business, financial condition and results of operations.

Electronic embezzlement could negatively impact the popularity of our online and mobile games and adversely affect our reputation and results of operations.

Despite security measures, some of our employees or licensees' employees with high-level security access to our network, or other employees or persons 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 and mobile games and publicly or privately sell the game money for their financial benefit. Although we have internal security procedures in place designed to prevent electronic embezzlement and have not had any incident of electronic embezzlement since early 2006, 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 designed 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 and mobile games could negatively impact the popularity of our online and mobile games and adversely affect our reputation and results of operations.

We have experienced numerous incidents where users were able to modify the published rules of our online and mobile games. Although these users did not gain unauthorized access to our systems, they were

Table of Contents

able to modify the rules of our online and mobile games during game play in a manner that allowed them to cheat and disadvantage 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 accumulate in-game points quickly, causing many other players to stop using the game and shortening the game's life cycle. For mobile games, some users bought game money or in-game items through cloned mobile phones and sold such illegally obtained property to other users, which resulted in a shortfall between total sales and our actual revenues. Such unauthorized manipulation of our games may negatively impact users' perception of our games and damage our reputation as well as our results of operations. Although we have taken a number of measures to deter our users from cheating when playing our games, including spot checks and monitoring of game play by game masters and system operators to check for suspicious activity, and encrypting packets, we cannot assure you that we or our licensees will be successful in timely taking the corrective measures necessary to prevent users from modifying the terms of our games.

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

Our intellectual property rights such as copyrights, service marks, trademarks and trade secrets are critical to our business. Unauthorized use of the intellectual property rights 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 unlawfully released on a consistent basis in most of the countries and markets in which Ragnarok Online has been 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. For example, in Japan, we submitted a preliminary written accusation to the Tokyo Metropolitan Police Department in October 2009 and filed criminal charges against an illegal server operator of Ragnarok Online in April 2011 in cooperation with GungHo, our licensee in Japan, and the matter is currently under investigation by the Tokyo Metropolitan Police Department. In December 2007 and June 2008, Gravity Interactive, Inc., our wholly owned subsidiary in the United States which manages Ragnarok Online game operations in the United States, petitioned the Federal Bureau of Investigation for remission or mitigation of forfeiture of the property of two illegal server operators of Ragnarok Online, which property was deemed proceeds of copyright infringement violations by the illegal server operators, and US\$154,674.73 was returned to Gravity Interactive, Inc. in April 2011. We may incur considerable costs in the future in order to remedy software piracy of our server software and to enforce our rights against the operators of unauthorized server networks.

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, Thailand 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.

Table of Contents

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 and mobile 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. For example, in November 2010, Gravity Interactive, Inc., which manages Dragonica game operations under the name Dragon Saga in the United States, Canada and certain other countries, THQ*ICE LLC, the former game distributor of Dragonica in the United States and Canada, and THQ Inc., the former joint venture partner of THQ*ICE LLC, were accused of trademark infringement. The owner of the registered trademark of Dragonica in the United States filed a lawsuit with the United States District Court for the Southern District of Florida seeking damages sustained by the plaintiff and any profits and gains derived by the defendants through the alleged trademark infringement. The lawsuit was settled in March 2012. If we are found to have violated the intellectual property rights of others, we may be enjoined from using such intellectual property rights, be required to pay penalties and fines and pay for the unauthorized use of such intellectual property and 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 and mobile 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 our business operations 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, console games, animation and character merchandising; and

pursuing joint ventures with game development and service 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 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 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

Table of Contents

insurance, we do not 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 operations. 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 2013 report issued by the Korea Creative Content Agency, an industry, non-profit organization that promotes the export of Korean culture, there has been a significant decrease in the number of Internet cafés in operation in 2011 and 2012, and the number of Internet cafés, and as a result the total number of personal computers, or PCs, at Internet cafés, is expected to gradually decrease in the long term as small-scale Internet cafés lacking price competitiveness close down operations. The number of Internet cafés is expected to continue to decrease as a result of the rapid increase in the use of smartphones and other mobile devices with which people access the Internet in a more convenient manner as well as certain legal developments which may have a negative impact on Internet café operations, such as the Juvenile Protection Act, which prohibits minors under the age of 16 from playing online games late at night by an amendment that went into effect in November 2011, and the National Health Promotion Act, which designated all Internet cafés as non-smoking areas by an amendment that took effect in June 2013. 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 at Internet cafés.

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.

We expect that as we introduce new games, a certain number of our existing users may migrate from our existing games to the new games, which may lead to a decrease in the player base of our existing games and in turn make those existing games less playable to other game players, resulting in decreased revenues from our existing games. Players of our existing games may also spend less money to purchase in-game items in our new games than they would have spent if they had continued playing our existing games. In addition, our game players may migrate from our existing games with a higher profit margin to new games with a lower profit margin. If any of the forgoing occurs, our revenue growth and profitability are likely to be materially and adversely affected.

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

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. In April 2013, a new strain of influenza virus subtype H7N9 was found in several provinces in China which according to news reports caused a number of deaths, and was a second spike of newly reported cases of H7N9 in China beginning in October 2013. While there has been no evidence to date of widespread human-to-human transmission in the case of the H7N9 virus, an outbreak of widespread public health problems such as swine flu, avian influenza, or severe acute respiratory syndrome, or SARS, in China or in other countries may prevent our customers from accessing Internet cafés and may adversely affect our prospects, business and operating results.

Table of Contents

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.

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.

Section 3(b)(1) of the Investment Company Act of 1940, or the '40 Act, provides that a company is not an investment company and, therefore, not required to register under the '40 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 (a "Non-Investment Business"). There are several bases on which a company can rely in determining that it is a Non-Investment Business.

Under one set of criteria, the factors to be considered in determining that a company is a Non-Investment Business are: (i) the history of the company; (ii) the manner in which the company represents itself to the investing public; (iii) the activities of its officers and directors; (iv) the nature of its current assets; and (v) the sources of its current income. Based on those factors, we believe that we are engaged primarily and directly in the business of providing online game services, and consequently, that we are a Non-Investment Business, and not an investment company as that term is defined under the '40 Act.

However, the determination as to whether a company satisfies the foregoing criteria is fact sensitive and subjective. Accordingly, it is possible that our determination could be challenged by the U.S. Securities and Exchange Commission (the "SEC"), particularly if at any time we own "investment securities" (as defined in the '40 Act) having a value in excess of 40% of our total assets (exclusive of cash items and U.S. government securities). We do not currently own investment securities in excess of this threshold. Nonetheless, if this were to become the case, we could be required to take actions to reduce our ownership of investment securities to comply with this standard, such as shifting a portion of our short-term investment portfolio into low-yielding bank deposits. If necessary, such actions would likely reduce the amount of interest or other income that we could otherwise generate from our investments. In addition, we might 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 business strategy.

Alternatively, we could consider other actions, including applying to the SEC for an exemptive order pursuant to Section 3(b)(2) of the '40 Act, declaring that we are a company that is primarily engaged in a business or businesses other than that of investing, reinvesting, owning, holding, or trading in securities, without regard to the composition of our assets at any particular time. However, there can be no assurance that we would receive an exemptive order and the process to obtain such an exemptive order could be long and expensive.

The '40 Act contains numerous, complex requirements with respect to the organization and operations of investment companies, including restrictions on their capital structure, operations, and transactions with affiliates, as well as restrictions on the composition of the board of directors and other matters which would be incompatible with our business. Also, if we were to be deemed an investment company in the future, we would effectively be precluded from making public offerings of securities 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

Table of Contents

a party that violate the '40 Act or the rules thereunder might be rendered unenforceable or subject to rescission.

Our status as a passive foreign investment company ("PFIC") in 2013 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 a PFIC for U.S. federal income tax purposes since our initial public offering. In particular, due to the deterioration of the trading price of our ADSs, we believe that we were a PFIC in 2008 through 2013, and there is a significant risk that we will continue to be a PFIC in 2014. If we are a PFIC 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 PFIC in any taxable year. See ITEM 10.E. "TAXATION MATERIAL U.S. FEDERAL INCOME TAX CONSIDERATIONS PFICs."

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 and our ability to prevent or detect fraud may be reduced and investor confidence and the market price of our ADSs may be adversely affected.

We are subject to Section 404 of the Sarbanes-Oxley Act of 2002, 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.

Although we have determined that we do not have a material weakness in our internal controls over financial reporting for the year ended December 31, 2013, we may in the future determine that we have a material weakness in our internal controls over financial reporting. If we fail to maintain 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. Any of these possible outcomes could result in an adverse reaction in the financial marketplace due to loss of investor confidence in the reliability of our consolidated financial statements and could result in investigations or sanctions by the SEC, NASDAQ, or other regulatory authorities or in stockholder litigation. Any of these factors could ultimately harm our business and could adversely impact the market price of our ADSs. See ITEM 15. "CONTROLS AND PROCEDURES."

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

The online and mobile game industries are subject to rapid technological developments and changes in market environment, which could render our online and mobile games under development and commercialized games obsolete or unattractive to users. Any resulting failure to recover capitalized development or licensing costs and the recognition of impairment loss for such costs may materially and adversely affect our financial condition and results of operations. For example, we recognized an impairment loss on intangible assets for capitalized research and development costs of Won 227 million for Finding Neverland Online in 2012. In 2013, we recognized impairment losses on intangible assets for capitalized research and development costs of Won 382 million for Requiem Returns W, Won 381 million for Ragnarok Odyssey Ace for the PlayStation Vita platform, Won 344 million for Steal Fighter, Won 244 million for Game Station, which is a mobile game service platform, Won 237 million for Maestia and Won 154 million for Ragnarok Online Guild Masters.

We could suffer losses due to asset impairment charges.

We held a total of Won nil in acquired intangible assets and Won 1,210 million in goodwill at December 31, 2013. See Note 9 to our consolidated financial statements included in this annual report. We

Table of Contents

test goodwill and indefinite-lived intangible assets at least annually for impairment, and more frequently if an event occurs or circumstances change that would more likely than not reduce the fair value of these assets below their carrying amount. Such an event would include unfavorable variances from established business plans, significant changes in forecasted results or volatility inherent to external markets and industries, which are periodically reviewed by our management. If such an adverse event occurs and has the effect of changing one of the critical assumptions or estimates related to the fair value of our intangible assets or goodwill, an impairment charge could result. For example, during 2012, we decided to discontinue the development of East Road due to the low likelihood that the game would be commercially successful and we recognized an impairment loss of Won 8,503 million on intangible assets of East Road in 2012 since its carrying amount before such recognition of the impairment loss exceeded its fair value. We also recognized an impairment loss of Won 64 million on intangible assets of Jeweled Planet in 2012 since its carrying amount before recognition of impairment losses exceeded its fair value. We recorded impairment losses on goodwill of Won 3,614 million and Won 2,653 million in Gravity Games in 2012 and 2013, respectively, primarily due to the overall decline in the fair value of Gravity Games, and recognized impairment losses of Won 2,161 million and Won 1,424 million on intangible assets of Dragonica in 2012 and 2013, respectively, since the carrying amount of the game before recognition of impairment losses exceeded its fair value. There can be no assurance that future reviews of our goodwill and other intangible assets will not result in impairment charges. Although it does not affect cash flow, an impairment charge does have the effect of decreasing our earnings, assets and shareholders' equity.

The value of our deferred tax assets could become impaired, which could materially and adversely affect our results of operations.

As of December 31, 2013, we had approximately Won 8,606 million in net deferred tax assets. See Note 14 to our consolidated financial statements included in this annual report. These deferred tax assets include net operating loss carryovers that can be used to offset taxable income in future periods and reduce income taxes payable in those future periods. Each year, we determine the probability of the realization of deferred tax assets, using significant judgments and estimates with respect to, among other things, historical operating results and expectations of future earnings. If we determine in the future that there is not sufficient positive evidence to support the valuation of these assets, due to the risk factors described herein or other factors, we may be required to further adjust the valuation allowance to reduce our deferred tax assets. Such a reduction could result in material non-cash expenses in the period in which the valuation allowance is adjusted and could have a material adverse effect on our results of operations.

RISKS RELATING TO OUR COMPANY STRUCTURE

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 over decisions related to the status of our ADSs being eligible for quotation and trading on the NASDAQ Global Market. In addition, as GungHo is also an online and mobile game developer, there may be conflicts of interest. For instance, GungHo may lead our management with strategies and efforts which benefit itself, its affiliates and their respective 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 Executive Directors, Mr. Hyun Chul Park, Mr. Yoshinori Kitamura, Mr. Kazuki Morishita and Mr. Kazuya Sakai currently serve as General Manager, Director and Executive General Manager, President and Chief Executive Officer, and Chief Financial Officer, Director and Investor Relations Officer, respectively, of GungHo, and there may be conflicts of interest in the decisions made by our Board of Directors and senior

Table of Contents

management. See ITEM 7.B. "RELATED PARTY TRANSACTIONS Relationship with GungHo Online Entertainment, Inc."

We are a "controlled company" within the meaning of the NASDAQ Stock Market Rules and may rely on exemptions from certain corporate governance requirements.

As GungHo controls 59.3% of our outstanding voting power as of the date hereof, we are a "controlled company" within the meaning of the NASDAQ Stock Market Rules and may rely on exemptions from certain corporate governance requirements. As a "controlled company," we are not required to have a majority of our board of directors be independent, nor are we required to have a compensation committee or independent director oversight of director nominations function which meet the requirements set forth in the NASDAQ Stock Market Rules. We are relying on these exemptions as a controlled company. Accordingly, our shareholders do not have the same protections afforded to shareholders of companies that are subject to all of the corporate governance requirements of the NASDAQ Stock Market Rules. For our corporate governance policies, see ITEM 6.C. "BOARD PRACTICES CORPORATE GOVERNANCE PRACTICES."

RISKS RELATING TO OUR REGULATORY ENVIRONMENT

Our online and mobile operations and businesses are subject to laws, rules and regulations in the countries in which our games are distributed, such as Korea, the United States and Japan, the changes to which are difficult to predict, and uncertainties in interpretation and enforcement of the laws, rules and regulations in such countries 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 and mobile game industries. However, in many of our principal markets, such as Korea, the United States and Japan, legislators and regulators have implemented or indicated their intention to implement laws, rules 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, rules and regulations on our business and results of operations is difficult to predict as many such laws, rules and regulations are constantly changing. However, as we might unintentionally violate such laws, rules and regulations or such laws, rules or regulations may be modified and new laws, rules and regulations may be enacted in the future, any such developments, or developments stemming from enactment or modification of other laws, rules or regulations, 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, financial condition and results of operations.

Korea

Article 9(4) of the National Health Promotion Act was amended on June 7, 2011, which included changes such as the expansion of the scope of public facilities which are required to be designated as entirely non-smoking areas while, at the same time, permitting the establishment of separate smoking sections in order to protect smokers' rights. Such public facilities include (i) business places offering games to adolescents, (ii) business places offering ordinary games, (iii) business places offering Internet computer games and (iv) business places offering combined distributed games as defined under the Act on Promotion of the Game Industry, and the amendment became effective on June 8, 2013 with respect to such business places. The amendment may cause significant changes in the operation of Internet cafés, which currently operate both smoking and non-smoking sections. The number of Internet cafés in Korea is already gradually decreasing, and the enactment of the proposed amendment may further reduce the number of Internet cafés operated by small business owners and have a material adverse effect on our

Table of Contents

business, financial condition and results of operations. 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 users." See also ITEM 4.B. "BUSINESS OVERVIEW LAWS AND REGULATIONS Korea" for detailed discussion regarding Korean laws that affect our operations.

Under the Act on Promotion of the Game Industry, (i) "business places offering adolescent games" refers to business places which install and provide to the public games which are rated and classified as appropriate for use by all ages, (ii) "business places offering ordinary games" refers to business places which install and provide to the public, in addition to games which are rated and classified as appropriate for use by all ages, games which are rated and classified as prohibited to be used by minors, (iii) "business places offering Internet computer game facilities" refers to business places which have the necessary equipment such as computers to enable the public to play games or access other information materials on the Internet and (iv) "business places offering combined distributed games" refers to business places which provide games or Internet game facilities under the Act on Promotion of the Game Industry as well as other businesses in the same location.

United States and Japan

See ITEM 4.B. "BUSINESS OVERVIEW LAWS AND REGULATIONS" for a detailed discussion regarding U.S. and Japanese laws that may materially impact our operations.

Our online and mobile 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 example, 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. 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.

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 foreign 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 without limitation Taiwan, China and Thailand, 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

Table of Contents

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 results of operations, 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 tax 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 taxes 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.

Recently, there have been series of amendments to tax treaties that Korea has entered into with various countries. The reduced tax rate applicable to license fees and royalties has reduced (i) from 10% to 5% under the amended tax treaty between Korea and Switzerland as to those payable from January 1, 2013, and (ii) from 10% to 5% in general (15% to 10% in case of consideration paid for provision of commercial or technological know-how) under the amended tax treaty between Korea and Luxembourg as to those payable from September 4, 2013. Further, the tax treaty between Korea and Peru went into effect as of March 3, 2014, and the license fees and royalties payable after January 1, 2015 will be taxed at the reduced rate of 15% (10% in case of consideration paid for technical supports). Around January 2014, Korea and India agreed on and initialed a proposed amendment of the tax treaty under which the reduced tax rate applicable to license fees and royalties shall be reduced from 15% to 10%. Around September 2013, Korea and Hong Kong agreed on and initialed a new tax treaty which includes a provision promulgating that the license fees and royalties shall be subject to tax at the reduced rate of 10%. These series of promulgations are all intended to eventually further limit the source country's taxation right with respect to the license fees and royalties. Any adverse changes in tax treaties between Korea and the countries from which we receive license fees and royalties, such as in 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 Korea, Japan, the United States and Canada, Taiwan and Hong Kong/Macau, and China, representing 32.5%, 30.2%, 16.2%, 6.5% and 5.7%, respectively, of our total revenues in 2013. 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 and markets. Adverse economic developments in such markets may have an adverse effect on the number of our users and our revenues and have a material adverse effect on our results of operations.

Deterioration in global economic conditions since the global financial crisis which began in 2007 and the debt crisis in Europe have weakened the economies of the countries in which our games are distributed. There have also persisted increased volatility in credit and financial markets worldwide and greater uncertainty in the global economic condition and prospects. While such global economic developments have not had a material adverse effect on us and various economic indicators show that the global economy may be recovering, a delayed recovery or further negative developments in global economic conditions could materially and adversely affect our business, financial condition and results of operations.

Table of Contents

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 overseas subsidiaries or licensees are denominated in local currencies, which include, among others, the U.S. dollar, the Japanese Yen, the Euro, the NT dollar, the Thai Baht and the Chinese Yuan. In 2013, approximately 67.5% of our revenues were denominated in foreign currencies, primarily in the U.S. dollar and the Japanese Yen. As the revenues denominated in local currencies, other than U.S. dollar, Japanese Yen and Euro, are converted into U.S. dollars 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. 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, 2013, 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 throughout Korea's modern history. The level of tension between the two Koreas has fluctuated and may increase abruptly as a result of current and future events. In recent years, there have been heightened security concerns stemming from North Korea's nuclear weapons and long-range missile programs and increased uncertainty regarding North Korea's actions, particularly in light of the recent leadership change and execution of a high-ranking government official, and possible responses from the international community. There can be no assurance that the level of tension on the Korean peninsula will not escalate in the future. Any further increase in tension, which may occur, for example, if North Korea experiences a leadership or economic crisis, or military hostilities occur, 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.

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, of the total issued and outstanding shares, a shareholder must own at least (i) one percent to bring a shareholders' derivative lawsuit (or to demand that a director cease certain activity or conduct if there are concerns that a director may cause irrevocable damage to the company by acting in violation of applicable laws and regulations or the articles of incorporation), (ii) three percent to demand convocation of an extraordinary meeting of shareholders, demand removal of directors or inspect the books and related documents of a company, or to propose the agenda for a general meeting of shareholders, (iii) ten percent to apply to the court for dissolution if there is gross improper management

Table of Contents

or a deadlock in corporate affairs likely to result in a significant and irreparable harm to the company or to apply to the court for a reorganization in the case of an insolvency, and (iv) twenty percent to block a small-scale share exchange or a small merger 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 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 pursuant to the deposit agreement that governs the rights and obligations of the holders of ADSs. 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 (e.g., 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

Table of Contents

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 shares are issued, except under certain circumstances as provided in our articles of incorporation. See ITEM 10.B. "MEMORANDUM AND 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 joint venture arrangements; or

by a public offering or underwritten by underwriters for the purpose of listing such shares 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 the deposit agreement among us, the depositary and you, as an ADS holder. Upon receipt of the necessary voting materials, you may instruct the

depository to vote the number of shares your ADSs represent. The depository will notify you of shareholders' meetings and arrange to deliver our voting

Table of Contents

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 voting 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 all or a part of the business of any other company having a material effect on our business, or our merger or consolidation with another company, except a small-scale merger (as prescribed under Korean law) that leaves us as the surviving company, dissenting shareholders have the right to require us to purchase their shares 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 ADRs 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 in 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.

Table of Contents

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 all of our directors and officers reside outside 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 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. If GungHo 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, formerly the NASDAQ National Market, under the symbol "GRVY." We list below some of the developments relating to our organizational structure.

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, which was 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 of 2005, we acquired an aggregate of 88.15% equity interest in TriggerSoft Corporation, or TriggerSoft, which developed R.O.S.E. Online. TriggerSoft went into liquidation proceedings in Korea in May 2007 and the liquidation was completed in October 2007.

In November and December of 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, a wholly-owned subsidiary based in France, which was converted into a joint venture company in which we have a 25% equity interest, Gravity EU SAS, with Media-Participations Paris SA as the joint venture partner, in July 2011.

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 October 2007, we founded Gravity RUS Co., Ltd., or Gravity RUS, a Russia-based

Table of Contents

subsidiary, and acquired 99.99% of its voting shares. We transferred 100% of the voting shares of Gravity CIS to Gravity RUS in December 2007 to make Gravity CIS a wholly-owned subsidiary of Gravity RUS. In August 2012, we surrendered our equity interest in Gravity RUS in accordance with Russian law, which resulted in Gravity RUS and Gravity CIS ceasing to be our subsidiaries.

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 formed L5 Games Inc., or L5 Games, a game development studio in the United States which was a wholly-owned subsidiary of Gravity Interactive. L5 Games went into liquidation proceedings in the United States in August 2008 and the liquidation was completed in May 2010.

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 March 31, 2014.

In June 2010, we acquired from Terabit Telecom Ltd., a Russia-based online game company, a 25% equity interest in Ingamba, a joint venture company established in April 2010 for online game service in Russia, and Terabit Telecom sold its 75% of equity interest in Ingamba to Stylonos Technologies Ltd., a Russia-based online game company, in December 2010. In May 2012, we sold our 25% equity interest in Ingamba to Stylonos Technologies Ltd., which resulted in Ingamba ceasing to be our affiliated company.

In October 2010, we acquired an aggregate of 50.83% of the total shares of Barunson Interactive Corporation, or Barunson Interactive, an online game developer in Korea. Barunson Interactive changed its corporate name to Gravity Games on March 28, 2011. In August 2013, we increased our ownership in Gravity Games to 85.5%.

Our registered office is located at 15F, 396 World Cup buk-ro, Mapo-gu, Seoul 121-795, Korea. Our telephone number is (822) 2132-7000. Our main Web site is at <http://www.gravity.co.kr>.

ITEM 4.B. BUSINESS OVERVIEW

OVERVIEW

We are a leading developer and publisher of online games in Japan and Thailand based on the number of peak concurrent users as compiled from various statistical data available from public sources in such countries. We are based in Korea, and we currently offer six online games worldwide and have one online game being developed by a third party for which we have entered into a license agreement. Our principal product, Ragnarok Online, is commercially offered in Korea and 59 other countries and markets. Ragnarok Online II is currently commercially offered globally except for Japan, the Philippines, Vietnam, Brazil and China. Requiem is commercially offered globally. R.O.S.E. Online is commercially offered in the United States, Canada, Mexico and 40 other countries. Dragonica is commercially offered in the United States, Canada, South America and 32 other countries and markets. Ragnarok Prequel is commercially offered in China. We also offer a number of mobile games, console games and a game for Internet protocol television, or IPTV, and license the merchandizing rights of character-related products based on our online games. We intend to diversify our game offering by developing online and mobile games in-house as well as publishing additional games developed by third parties.

In Korea, we directly manage all aspects of operations of our online games, such as marketing, operation, billing and customer service. Gravity Interactive, our wholly-owned subsidiary in the United States, is responsible for all aspects of Ragnarok Online game operations in the United States, Canada, Australia, New Zealand, India, Singapore and Malaysia, for all aspects of Ragnarok Online II game operations globally except for Singapore, Malaysia, Indonesia, Thailand, Japan, the Philippines, Vietnam,

Edgar Filing: GRAVITY Co., Ltd. - Form 20-F

Table of Contents

Brazil and China, for all aspects of Requiem game operations globally, for all aspects of R.O.S.E. Online game operations in the United States, Canada, Mexico and 40 European countries, and for all aspects of Dragonica game operations in the United States, Canada and South America except for Brazil under the name Dragon Saga. In the countries where we and Gravity Interactive manage game operations, our online game revenues are recorded as subscription revenues.

Except as managed by us and our affiliates as described above, our overseas licensees are responsible for all aspects of online 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 once the initial term expires. We rely on the initial and renewal 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 or the micro-transaction system in their respective markets.

Except Korea, the United States and Canada, our overseas licensees handle our mobile game operations in close cooperation with us. NeoCyon and Gravity Interactive directly manage all aspects of operations of our mobile games in Korea, and the United States and Canada, respectively. Revenues from our mobile games, regardless of the operator, are recorded as mobile games revenues.

The following table sets forth a summary of our consolidated statements 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 net revenues for the periods indicated.

| | Year Ended December 31, | | | | | | | | | |
|--|--|---------------|---------------|----------|---------------|---------------|---------------------|---------------|--------------------|---------------|
| | 2011 | | 2012 | | 2013 | | 2013 ⁽¹⁾ | | | |
| | (In millions of Won and thousands of US\$, except percentages) | | | | | | | | | |
| Online game revenue⁽²⁾: | | | | | | | | | | |
| Subscription revenue: | | | | | | | | | | |
| Korea ⁽³⁾ | ₩ | 4,740 | 8.2% | ₩ | 5,438 | 9.4% | ₩ | 2,447 | 5.1% US\$ | 2,319 |
| United States/Canada ⁽⁴⁾ | | 5,832 | 10.2 | | 4,712 | 8.2 | | 5,759 | 12.1 | 5,457 |
| Others | | 984 | 1.7 | | | | | | | |
| Subtotal | | 11,556 | 20.1 | | 10,150 | 17.6 | | 8,206 | 17.2 | 7,776 |
| Royalties and license fees: | | | | | | | | | | |
| Japan | | 23,854 | 41.5 | | 23,795 | 41.2 | | 12,103 | 25.4 | 11,469 |
| Taiwan/Hong Kong/Macau ⁽⁵⁾ | | 3,561 | 6.2 | | 2,235 | 3.9 | | 2,002 | 4.2 | 1,897 |
| Others | | 8,137 | 14.2 | | 6,295 | 10.8 | | 7,621 | 16.0 | 7,222 |
| Subtotal | | 35,552 | 61.9 | | 32,325 | 55.9 | | 21,726 | 45.6 | 20,588 |
| Mobile games and applications revenue ⁽⁶⁾ | | 6,609 | 11.5 | | 8,262 | 14.3 | | 14,504 | 30.4 | 13,745 |
| Character merchandising and other revenue ⁽⁶⁾ | | 3,760 | 6.5 | | 7,044 | 12.2 | | 3,249 | 6.8 | 3,079 |
| Total net revenue | ₩ | 57,477 | 100.0% | ₩ | 57,781 | 100.0% | ₩ | 47,685 | 100.0% US\$ | 45,188 |

Notes:

Edgar Filing: GRAVITY Co., Ltd. - Form 20-F

- (1) For convenience only, the Won amounts are expressed in U.S. dollars at the rate of Won 1,055.25 to US\$1.00, the noon buying rate in effect on December 31, 2013 as certified by the Federal Reserve Bank of New York for customs purposes.
- (2) Online game revenues include revenues from Ragnarok Online, R.O.S.E. Online, Requiem, Emil Chronicle Online, Dragonica, Pororo Game, Canaan, H.A.V.E. Online, Eternal Destiny, Ragnarok Online Guild Masters, Kun Woong Online, Finding Neverland Online, Ragnarok Online II, Maestia,

Table of Contents

Steal Fighter, Ragnarok Prequel and our social network games, and from online game channeling service through GnJoy, our online game portal site. H.A.V.E. Online, Eternal Destiny, Ragnarok Online Guild Masters, Kun Woong Online, Finding Neverland Online, Ragnarok Online II, Maestia, Steal Fighter and Ragnarok Prequel were commercially launched in March 2011, August 2011, October 2011, November 2011, January 2012, March 2012, July 2012, February 2013 and October 2013, respectively. Our online game channeling service was launched in August 2011 and ceased in June 2013. We discontinued offering Eternal Destiny, Canaan, Kun Woong Online, Ragnarok Online Guild Masters, Emil Chronicle Online, Finding Neverland Online, Maestia, Steal Fighter and H.A.V.E. Online in November 2011, June 2012, August 2012, May 2013, July 2013, September 2013, February 2014 and March 2014, respectively.

- (3) Requiem game service in Korea was transferred to Gravity Interactive on March 7, 2012. Upon this change, the revenues from Requiem generated in Korea through March 6, 2012 are shown as Online game revenue Subscription revenue Korea and those generated on or after March 7, 2012 are shown as Online game revenue Subscription revenue United States/Canada. Ragnarok Online II game service in Korea was transferred to Gravity Interactive on December 24, 2013 through an amendment to the license agreement with Gravity Interactive dated June 2013 to include Korea as a service country, as the game service in Korea was suspended on December 23, 2013. Upon this change, the revenues from Ragnarok Online II generated in Korea through December 23, 2013 are shown as Online game revenue Subscription revenue Korea and those generated on or after December 24, 2013 are shown as Online game revenue-Subscription revenue-United States/Canada.
- (4) Subscription revenues in the United States and Canada, as shown on this table, also include subscription and other types of game revenues generated in other countries and markets managed by Gravity Interactive. For Ragnarok Online, the countries serviced by Gravity Interactive include the United States, Canada, Australia, New Zealand and India, and further include Singapore and Malaysia since October 24, 2013. Upon this change, the revenues from Ragnarok Online generated in Singapore and Malaysia through October 23, 2013, are shown as Online game revenue Royalties and license fees Others and those generated on or after October 24, 2014 are shown as Online game revenue Subscription revenue United States/Canada. For Ragnarok Online II, the countries serviced by Gravity Interactive include the United States, Canada and 54 other countries and markets. For R.O.S.E. Online, the countries managed by Gravity Interactive include the United States, Canada, Mexico and 40 other countries. For Dragonica, the countries serviced by Gravity Interactive include the United States and Canada, and further include South America except for Brazil since October 28, 2013. For Requiem, the countries serviced by Gravity Interactive include the United States, Canada, the United Kingdom and 38 other European countries, and further include Mexico and 23 other Central and South American countries since June 2011. The license agreement for Requiem with Gravity Interactive was further amended in October 2011 to grant Gravity Interactive the worldwide distribution right of Requiem except for the existing licensed territories in which we have already granted licenses for Requiem game service to other local licensees. Since December 1, 2013, the service territory of Requiem by Gravity Interactive is worldwide as our license agreement with Ingamba to distribute Requiem in Russia and 14 other countries was terminated on November 30, 2013. Gravity Interactive entered into a license agreement with Ingamba on December 1, 2013 to distribute Requiem in Russia and 14 other countries and the revenues from Requiem generated in these countries are shown as Online game revenue Royalties and license fees Others. See also note (3) and (5) to this table for changes to Requiem game service in Korea, Taiwan, Hong Kong and Macau.
- (5) As our license agreement for Requiem in Taiwan, Hong Kong and Macau with Game Flier International Corporation was terminated on August 31, 2012, these markets are included as markets serviced by Gravity Interactive since September 1, 2012. Upon this change, the revenues from Requiem generated in Taiwan, Hong Kong and Macau through August 31, 2012 are shown as Online game revenue Royalties and license fees Taiwan/Hong Kong/Macau and those generated on or

Table of Contents

after September 1, 2012 are shown as Online game revenue Subscription revenue United States/Canada.

- (6) We reclassified certain revenue within Mobile games and applications revenue as Character merchandising and other revenue in 2013 as this better represents the nature of the revenue. The same reclassification has been made to all prior periods to conform to the presentation of 2013. The reclassification has no effect on the Company's previously reported total net revenue and other line items on the consolidated financial statements.

OUR PRODUCTS

We currently categorize our products into three categories: online games; mobile games and applications; and other games, and game-related products and services, including character-based merchandise and animation. Revenues from our principal product, Ragnarok Online, accounted for 45.2% of our total revenues in 2013, compared with 55.9% of our total revenues in 2012.

Online games

Online game is a genre of computer games in which a large number of players interact with one another within a virtual game world.

The following table summarizes the online games that we currently offer.

| Title | Genre | Game Source | Date of Commercial Launch⁽¹⁾ |
|--|-------------------------|--|--|
| Ragnarok Online | Action adventure MMORPG | Developed in-house | August 2002 |
| Ragnarok Online II | Action adventure MMORPG | Developed in-house | March 2012 |
| Requiem | Action adventure MMORPG | Developed in-house | October 2007 |
| Dragonica (Dragon Saga) ⁽²⁾ | Action adventure MMORPG | Originally licensed from third party developer; currently owned by us ⁽³⁾ | February 2009 ⁽⁴⁾ |
| R.O.S.E. Online | Action adventure MMORPG | Originally licensed from third party developer; currently owned by us ⁽⁵⁾ | January 2005 |
| Ragnarok Prequel | Action adventure MMORPG | Developed by third party developer based on our own intellectual property | October 2013 |

Notes:

- (1) The actual date of commercial launch of games in each jurisdiction 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, among others.
- (2) Dragonica is commercially offered in the United States, Canada and South America except for Brazil under the name Dragon Saga.
- (3) We acquired an aggregate of 50.83% equity interest in Gravity Games, formerly known as Barunson Interactive, which developed Dragonica, on October 21, 2010, and subsequently increased our ownership in Gravity Games to 85.5% in August 2013.
- (4) Dragonica was initially launched in China in February 2009 followed by certain other countries and markets under license agreements between Gravity Games and local publishers before our acquisition of Gravity Games.

- (5) 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.

Table of Contents**Ragnarok Online**

Ragnarok Online is commercially offered in Korea and 59 other countries and markets since its commercial launch in August 2002. See ITEM 4.B. "BUSINESS OVERVIEW OUR MARKETS Overseas markets." Ragnarok Online represented 45.2% of our total revenues or Won 21,531 million (US\$20,403 thousand) in 2013, compared with 55.9% of our total revenues or Won 32,308 million in 2012.

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

| Revenue Type | Country | Year Ended December 31, | | | |
|--|-------------------------------------|-------------------------|----------|-------------|---------------------|
| | | 2011 | 2012 | 2013 | 2013 ⁽¹⁾ |
| (In millions of Won and thousands of US\$) | | | | | |
| Online games subscription revenue | Korea | ₩ 4,542 | ₩ 2,648 | ₩ 2,368 | US\$ 2,244 |
| | United States/Canada ⁽²⁾ | 3,479 | 2,969 | 1,925 | 1,824 |
| | Others ⁽³⁾ | 950 | | | |
| | Subtotal | 8,971 | 5,617 | 4,293 | 4,068 |
| Online games royalties and license fees | Japan | 22,320 | 21,514 | 11,480 | 10,879 |
| | Taiwan/Hong Kong/Macau | 2,769 | 1,717 | 1,713 | 1,623 |
| | China ⁽⁴⁾ | 166 | | 1,586 | 1,503 |
| | Thailand | 865 | 867 | 811 | 768 |
| | Brazil | 1,162 | 793 | 633 | 600 |
| | Philippines | 889 | 789 | 375 | 355 |
| | Europe ⁽³⁾ | 201 | 433 | 352 | 334 |
| | Indonesia | 208 | 179 | 195 | 185 |
| | Russia/CIS countries | 89 | 92 | 68 | 64 |
| | Singapore/Malaysia ⁽⁵⁾ | 114 | 100 | 25 | 24 |
| | Middle East/Africa | 209 | 207 | | |
| Subtotal | 28,992 | 26,691 | 17,238 | 16,335 | |
| Total | ₩ 37,963 | ₩ 32,308 | ₩ 21,531 | US\$ 20,403 | |

Notes:

- (1) For convenience only, the Won amounts are expressed in U.S. dollars at the rate of Won 1,055.25 to US\$1.00, the noon buying rate in effect on December 31, 2013 as certified by the Federal Reserve Bank of New York for customs purposes.
- (2) Includes subscription and other types of game revenues generated in Australia, New Zealand and India, and further includes Singapore and Malaysia since October 24, 2013, managed by Gravity Interactive. Such revenues from other countries constitute a minor portion of the revenues recorded as subscription revenues from the United States and Canada.
- (3) Gravity EU SASU, our former wholly-owned subsidiary based in France, was responsible for all aspects of Ragnarok Online game operations in France, Belgium and 26 other European countries through June 30, 2011, when Gravity EU SASU was converted into a joint venture company in which we have a 25% equity interest, Gravity EU SAS. After we entered into a license agreement with

Edgar Filing: GRAVITY Co., Ltd. - Form 20-F

Gravity EU SAS on June 30, 2011 to distribute Ragnarok Online, Ragnarok Online has been serviced in the European countries by Gravity EU SAS. The revenues generated in the European countries through June 30, 2011 are shown as Online games subscription revenue Others and those generated on or after July 1, 2011 are shown as Online games-royalties and license fees Europe.

- (4) Ragnarok Online game service in China by Shengqu Information Technology (Shanghai) Co., Ltd., our former licensee, ceased on December 30, 2011 and we relaunched the game in China with Beijing Kunlun Online Network Tech Co., Ltd., our current licensee, on February 28, 2013.
- (5) Our license agreement with Game Flier (Malaysia) Sdn. Bhd. for Ragnarok Online game service in Singapore and Malaysia expired on October 9, 2013 and we subsequently amended our license agreement for Ragnarok Online games service with Gravity Interactive on October 24, 2013 to include such countries as service countries of Gravity Interactive. Upon these changes, the revenues generated in Singapore and Malaysia through October 9, 2013 are shown as Online games royalties and license fees Singapore/Malaysia and those generated from October 24, 2013 are shown as Online games subscription revenue United States/Canada.

Table of Contents

The table below provides, for the periods indicated, the peak concurrent users and average concurrent users of Ragnarok Online since the first quarter of 2011, in each of our principal markets for Ragnarok Online.

| | | 1Q 11 | 2Q 11 | 3Q 11 | 4Q 11 | 1Q 12 | 2Q 12 | 3Q 12 | 4Q 12 | 1Q 13 | 2Q 13 | 3Q 13 | 4Q 13 | 1Q 14 |
|-------------------|--------------------|--------|--------|--------|--------|--------|--------|--------|--------|--------|--------|--------|--------|--------|
| Japan | PCU ⁽¹⁾ | 43,869 | 44,155 | 47,387 | 48,085 | 38,984 | 44,492 | 40,215 | 34,854 | 32,270 | 26,956 | 24,033 | 21,158 | 19,547 |
| | ACU ⁽²⁾ | 17,995 | 17,907 | 18,147 | 17,176 | 15,079 | 17,673 | 15,148 | 14,366 | 11,696 | 9,939 | 8,698 | 7,042 | 7,296 |
| Korea | PCU | 16,064 | 11,026 | 10,848 | 37,810 | 7,628 | 4,445 | 3,267 | 13,712 | 14,776 | 3,898 | 3,874 | 4,158 | 5,503 |
| | ACU | 6,401 | 3,623 | 3,240 | 3,929 | 3,282 | 1,973 | 1,671 | 1,902 | 2,385 | 2,024 | 2,243 | 2,151 | 2,759 |
| USA/Canada | PCU | 4,692 | 6,635 | 6,811 | 9,201 | 5,180 | 4,948 | 5,895 | 5,384 | 4,618 | 4,530 | 4,291 | 5,882 | 5,895 |
| | ACU | 3,172 | 4,188 | 5,125 | 4,010 | 3,569 | 3,699 | 4,099 | 3,492 | 3,561 | 3,542 | 2,863 | 3,744 | 4,239 |

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.

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 non-financial variables and the data presented has not been audited or reviewed. 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 games 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 MMORPG 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 up to level 175, 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;

Table of Contents

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.

We believe that the PC configurations required to run Ragnarok Online are lower than or similar to many other competing online 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. The recommended minimum PC configuration for Ragnarok Online is Pentium III 1.6 GHz, 256 MB RAM and 32 MB graphics card.

Ragnarok Online II

Ragnarok Online II, an action adventure-based three-dimensional MMORPG, is a sequel to Ragnarok Online with 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 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 commercially launched Ragnarok Online II in Korea in March 2012, Singapore and Malaysia in January 2013, the United States, Canada and 28 European countries in May 2013, Indonesia in August 2013 and Thailand in October 2013. Our license and distribution agreement with Gravity Interactive to distribute Ragnarok Online II in the United States, Canada and 28 European countries was amended in June 2013 to include Australia, New Zealand, India, Russia, Armenia, Azerbaijan, Belarus, Kazakhstan, Kyrgyzstan, Moldova, Tajikistan, Turkmenistan, Ukraine, Uzbekistan, Guyana, Venezuela, Bolivia, Suriname, Argentina, Ecuador, Uruguay, Chile, Colombia, Paraguay, Peru and Korea as service countries, which was further amended in February 2014 to distribute Ragnarok Online II globally except for Singapore, Malaysia, Indonesia, Thailand, Japan, the Philippines, Vietnam, Brazil and China. Ragnarok Online II game service in Korea was transferred to Gravity Interactive on December 24, 2013 as the game service in Korea was suspended on December 23, 2013. As a result, Ragnarok Online II is currently commercially offered globally except for Japan, the Philippines, Vietnam, Brazil and China.

We have license and distribution agreements for Ragnarok Online II with five third-party licensees in seven countries, including Singapore, Malaysia, Indonesia, Thailand, Japan, Vietnam and Brazil. The total value of the license and distribution agreements for Ragnarok Online II with respect to Japan, Vietnam and Brazil in which jurisdictions the game has not been commercially launched, is US\$20,640 thousand as of the date hereof. Our license and distribution agreements for Ragnarok Online II with licensees in China and the Philippines were terminated in November 2013 and April 2014, respectively. We are in the process of finding alternative arrangements to distribute the game in China and the Philippines as of the date hereof. Ragnarok Online II represented 8.8% of our total revenues or Won 4,211 million (US\$3,991 thousand) in 2013 and less than 1% of our total revenues in 2012. 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 and mobile games in addition to Ragnarok Online, our business, financial condition and results of operations may be materially and adversely affected."

Requiem

Unlike Ragnarok Online and Ragnarok Online II, which do not emphasize violent themes, we designed Requiem to showcase user-to-user combat. Requiem provides players with a variety of combat systems, which allow them to accumulate experience and reward points to be used when they buy special items designed for combats.

Table of Contents

Requiem is currently commercially offered globally by Gravity Interactive. Requiem was commercially offered in Russia, Armenia, Azerbaijan, Belarus, Estonia, Georgia, Kazakhstan, Kyrgyzstan, Latvia, Lithuania, Moldova, Tajikistan, Turkmenistan, Ukraine and Uzbekistan by Ingamba under our license agreement with Ingamba until November 2013, when our license agreement with Ingamba was terminated, and these countries are included as countries and markets serviced by Gravity Interactive. Gravity Interactive entered into a license agreement with Ingamba in December 2013 to distribute Requiem in these countries. We also launched a Web-browser based version of Requiem on WarpPortal, Gravity Interactive's game portal site, and Facebook in April 2012 and September 2012, respectively. The amount of revenues from Requiem represented 1.3% of our total revenues or Won 633 million (US\$600 thousand) in 2013 and 2.1% of our total revenues or Won 1,188 million in 2012.

Dragonica (Dragon Saga)

Dragonica is a three-dimensional side-scrolling MMORPG, which is commercially offered in the United States, Canada and South America except for Brazil under the name Dragon Saga. Dragonica was developed by Gravity Games, our 85.5%-owned subsidiary. Dragonica is currently commercially offered in China, Taiwan, Hong Kong, Macau, Austria, Belgium, Bulgaria, Cyprus, Czech Republic, Denmark, Estonia, Finland, France, Germany, Greece, Hungary, Ireland, Italy, Latvia, Lithuania, Luxembourg, Malta, Netherlands, Poland, Romania, Slovakia, Slovenia, Sweden, Switzerland, Norway, the United Kingdom, Vietnam, the United States, Canada and South America. The amount of revenues from Dragonica represented 2.4% of our total revenues or Won 1,154 million (US\$1,094 thousand) in 2013 and 4.2% of our total revenues or Won 2,413 million in 2012.

R.O.S.E. Online

R.O.S.E. Online is a three-dimensional MMORPG, which is commercially offered in the United States, Canada, Mexico, Switzerland, Norway, Denmark, Ireland, Spain, Sweden, the United Kingdom, Iceland, Finland, France, Germany, Greece, Austria, Belgium, Bulgaria, Cyprus, Czech Republic, Hungary, Italy, Luxembourg, Malta, Netherlands, Poland, Portugal, Romania, Slovakia, Slovenia, Albania, Andorra, Bosnia and Herzegovina, Liechtenstein, Moldova, Monaco, Montenegro, San Marino, Serbia, Vatican City State, Croatia, Former Yugoslav Republic of Macedonia and Turkey since its commercial launch in January 2005. The amount of revenues from R.O.S.E. Online in 2013 and 2012 represented less than 1% of our total revenues in 2013 and 2012, respectively.

Ragnarok Prequel

Ragnarok Prequel is a Web browser-based MMORPG, which is played on a Web browser and which does not require any client-side software to be installed. In May 2013, we entered into an agreement with Shanghai The Dream Network Technology Co., Ltd., a Chinese game developer, which was granted the right to develop a Web-browser based game based on Ragnarok Online and distribute the Web-browser based game in China under the agreement. Ragnarok Prequel was commercially launched in China in October 2013. Ragnarok Prequel represented less than 1% of our total revenues in 2013.

Emil Chronicle Online

Emil Chronicle Online, an MMORPG, is the first online game developed by GungHo, 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 commercially launched Emil Chronicle Online in Korea, Thailand, Hong Kong, Taiwan, Indonesia, Singapore/Malaysia and China in August 2007, September 2007, June 2008, August 2008, September 2009, October 2009 and October 2011, respectively, and ceased offering commercial service in Singapore and Malaysia in September 2010, in Korea in November 2010, in Thailand in September 2011, in Indonesia in October 2012, in China in April 2013, and in Hong Kong and Taiwan in July 2013.

Table of Contents

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 in Japan, which was renewed in August 2012 and August 2013. In February 2012, we entered into a license agreement for Emil Chronicle Online with Gravity Interactive to distribute a Web-browser based version of the game worldwide except for Japan through certain designated Web sites, which was renewed in February 2013 and February 2014. The amount of revenues from Emil Chronicle Online in 2013 and 2012 represented less than 1% of our total revenues in 2013 and 2012, respectively.

H.A.V.E. Online (Toy Wars)

H.A.V.E. Online is a casual third person shooter game developed by SK i-media Co., Ltd., currently NQ Games Co., Ltd., an online game developer based in Korea. In April 2010, we entered into a publishing agreement with SK i-media Co., Ltd. to publish H.A.V.E. Online in Korea and Japan, which was amended in March 2014 to exclude Japan from the service territories. We entered into a license and distribution agreement with GungHo in August 2010 to distribute H.A.V.E. Online in Japan, which expired in March 2014. We commercially launched H.A.V.E. Online in Japan under the name Toy Wars in March 2011 and ceased offering commercial service in March 2014. The amount of revenues from H.A.V.E. Online represented 1.0% of our total revenues or Won 489 million (US\$463 thousand) in 2013 and 2.1% of our total revenues or Won 1,209 million in 2012.

Finding Neverland Online

Finding Neverland Online is a three-dimensional casual MMORPG. In February 2011, we entered into a license agreement with X-Legend Entertainment Co., Ltd., a Taiwanese game developer, to publish Finding Neverland Online in Korea, which was terminated in June 2013. We commercially launched Finding Neverland Online in Korea in January 2012 and ceased offering the game in July 2013. The amount of revenues from Finding Neverland Online represented less than 1% of our total revenues in 2013 and 4.1% of our total revenues or Won 2,344 million in 2012.

Maestia

Maestia is a three-dimensional MMORPG. In March 2012, we entered into a license agreement with RoC Works Co., Ltd., a Korean game developer currently called Andromeda Games Ltd., for us to publish Maestia in the United States and Canada. We launched Maestia in the United States and Canada in July 2012 under a license and distribution agreement entered into with Gravity Interactive in June 2012. We terminated the license agreement with Andromeda Games Ltd. and the license and distribution agreement with Gravity Interactive, and ceased offering the game in September 2013. The amount of revenues from Maestia represented less than 1% of our total revenues in each of 2013 and 2012.

Ragnarok Online Guild Masters

Ragnarok Online Guild Masters is a Web browser-based tactical role playing game based on Ragnarok Online. We entered into an agreement with NeoCyon in March 2011 to develop and distribute Ragnarok Online Guild Masters worldwide, which was terminated in June 2013. NeoCyon entered into a consignment agreement with GungHo in April 2011 to develop a Japanese version of the game and a license agreement with GungHo in May 2011 to distribute the game in the Japanese market. We commercially launched Ragnarok Online Guild Masters in Japan and Korea in October 2011 and May 2012, respectively, and we ceased offering the game in Korea in March 2013 and in Japan in May 2013. The amount of revenues from Ragnarok Online Guild Masters represented less than 1% of our total revenues in 2013 and 1.4% of our total revenues or Won 789 million in 2012.

Steal Fighter

Steal Fighter is an action real-time strategy role playing game. We entered into license and distribution agreements with L-Time Games Co., Ltd., the developer of Steal Fighter, to publish the game in Korea in April 2012, and in Taiwan and China, including Hong Kong and Macau, in November 2012, both of which were terminated in January 2014. We entered into a license and distribution agreement with

Table of Contents

Game Flier International Corporation to distribute Steal Fighter in Taiwan in December 2012, which was terminated in November 2013. We commercially launched Steal Fighter in Korea in February 2013 and ceased offering the game in February 2014. The amount of revenues from Steal Fighter represented less than 1% of our total revenues in 2013.

Requiem Returns W

Requiem Returns W is a three-dimensional Web browser-based MMORPG. In August 2012, we entered into an intellectual property license agreement with Weaver Interactive Inc., a Korean game developer, under which we granted Weaver Interactive Inc. the right to develop a Web browser-based game based on Requiem. In October 2012, we entered into a license agreement with Weaver Interactive Inc. that granted us the right to publish and distribute Requiem Returns W worldwide, which was amended to exclude Korea from the service territories in January 2013. Both of our agreements with Weaver Interactive Inc., the intellectual property license agreement and license agreement, were terminated in April 2014.

Mobile games and applications

As compared to online games, mobile games, which are played using mobile phones, including smartphones such as Google Android compatible phones and the Apple iPhone as well as feature phones, and other mobile devices, such as tablet computers, have shorter game playtimes and less complex user-game interactions. 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.

We develop mobile games, most of which are based on our intellectual property, which include Ragnarok Online Uprising: Valkyrie, Ragnarok Online Mobile Story and Ragnarok Violet, and also publish mobile games licensed from third parties.

In contrast to online games, the life cycle of a mobile game is relatively short and generally lasts from 6 to 24 months while reaching its peak popularity within the first 3 months of its introduction, though it varies by genre. As a result, we generate a significant portion of our mobile games revenue from the games that have been released within the recent 12 months.

Edgar Filing: GRAVITY Co., Ltd. - Form 20-F

Table of Contents

The following table sets forth each of the mobile games that we released during 2013.

| Title | Genre | Game Source | Date of Commercial Launch |
|----------------------------|-------------------|-------------------------------------|----------------------------------|
| We Build Story | Social network | Developed in-house | January 2013 |
| What's up? Aliens! | Puzzle | Licensed from third party developer | February 2013 |
| Alpha Zero | Simulation | Licensed from third party developer | February 2013 |
| Dino Island | Adventure | Licensed from third party developer | March 2013 |
| Demon Soul | Role playing | Licensed from third party developer | April 2013 |
| Iruna | MMORPG | Licensed from third party developer | April 2013 |
| Barrage Ballad | Shooting | Licensed from third party developer | July 2013 |
| Kitty Solitaire & Sweeper! | Puzzle | Licensed from third party developer | August 2013 |
| RhythmCoin 2 Revolution! | Simulation | Licensed from third party developer | August 2013 |
| Tower of Ascension | Role playing | Developed in-house | August 2013 |
| Magic Shot! | Arcade | Licensed from third party developer | August 2013 |
| Ragnarok Ash Vacuum | Simulation | Developed in-house | October 2013 |
| Samguk Hero Collection | Trading card | Licensed from third party developer | October 2013 |
| Ayakashi | Role playing card | Licensed from third party developer | October 2013 |
| Kuma Fishing! | Arcade | Licensed from third party developer | October 2013 |
| Foodie Monsters | Arcade | Licensed from third party developer | November 2013 |
| Puzzle Battle! | Puzzle | Licensed from third party developer | November 2013 |
| Train City! | Simulation | Licensed from third party developer | November 2013 |
| Battle Ship | Simulation | Licensed from third party developer | November 2013 |
| Shooting Hero! | Shooting | Licensed from third party developer | December 2013 |
| Bowling Zombies! | Shooting | Licensed from third party developer | December 2013 |
| Catastrophic Zombies! | Shooting | Licensed from third party developer | December 2013 |
| Battle Wars | Simulation | Licensed from third party developer | December 2013 |

For our smartphone games offered where we directly provide mobile games services to users, we share users' payments for micro-transactions with digital storefront owners and mobile telecommunication operators. For our smartphone games in the other markets where the mobile games services offered by our licensees, we receive license fees and royalty revenues from our licensees.

In addition to mobile games offered to users, we also develop mobile applications provided to third-party enterprises. The following are revenues generated from our mobile games and applications business for the periods indicated:

| Country | Year Ended December 31, | | | | 2013⁽¹⁾ |
|----------------------------|---|----------------|-----------------|---------------|---------------------------|
| | 2011 | 2012 | 2013 | | |
| | (In millions of Won and thousands of US\$, except percentages) | | | | |
| Korea | ₩ 1,866 | ₩ 3,984 | ₩ 10,049 | 69.3% | US\$ 9,523 |
| United States | 25 | 307 | 1,917 | 13.2 | 1,817 |
| Japan | 4,710 | 3,962 | 1,202 | 8.3 | 1,139 |
| Taiwan/Hong Kong/Macau | | 9 | 1,104 | 7.6 | 1,046 |
| Others | 8 | | 232 | 1.6 | 220 |
| Total⁽²⁾ | ₩ 6,609 | ₩ 8,262 | ₩ 14,504 | 100.0% | US\$ 13,745 |

Notes:

(1) For convenience only, the Won amounts are expressed in U.S. dollars at the rate of Won 1,055.25 to US\$1.00, the noon buying rate in effect on December 31, 2013 as certified by the Federal Reserve Bank of New York for customs purposes.

(2)

Edgar Filing: GRAVITY Co., Ltd. - Form 20-F

We reclassified certain revenue within Mobile games and applications revenue as Character merchandising and other revenue in 2013 as this better represents the nature of the revenue. The same reclassification has been made to all prior periods to conform to the presentation of 2013. The

Table of Contents

reclassification has no effect on the Company's previously reported total net revenue and other line items on the consolidated financial statements.

Other games and game-related products and services*Other games*

In addition to developing and publishing online games and mobile games, which is our primary business, we also provide games for game consoles and handheld game consoles, such as Nintendo DS, Xbox 360 and PlayStation series. Console games are distributed in the form of a disc or cartridge (game card), or downloaded directly to a console through the Internet.

The following table sets forth the console games we have released.

| Title | Genre | Platform | Release Date |
|--|-----------------------|----------------------|------------------------------|
| Ragnarok DS | Role playing | Nintendo DS | December 2008 ⁽¹⁾ |
| Ragnarok: The Princess of Light and Darkness | Tactical role playing | PlayStation Portable | October 2011 |
| Ragnarok Odyssey | Role playing | PlayStation Vita | February 2012 ⁽²⁾ |
| Double Dragon II | Action | Xbox 360 | April 2013 |
| Ragnarok Odyssey Ace | Role playing | PlayStation Vita | August 2013 ⁽³⁾ |
| Ragnarok Odyssey Ace | Role playing | PlayStation 3 | April 2014 ⁽⁴⁾ |

Notes:

- (1) Ragnarok DS was initially released in Japan in December 2008 followed by Korea in June 2009 and the United States, Canada, Mexico, Brazil, Colombia, Guatemala, Panama and Venezuela in February 2010.
- (2) Ragnarok Odyssey was initially released in Japan in February 2012 followed by Korea, Taiwan, Hong Kong, Singapore, Malaysia, Indonesia and Thailand in August 2012, the United States, Canada, Mexico and Brazil in October 2012 and Europe in February 2013.
- (3) Ragnarok Odyssey Ace for the PlayStation Vita platform was initially released in Japan, Korea, Taiwan, Hong Kong, Singapore, Malaysia, Indonesia and Thailand in August 2013 followed by the United States, Canada, Mexico and Brazil in April 2014.
- (4) Ragnarok Odyssey Ace for the PlayStation 3 platform was released in the United States, Canada, Mexico and Brazil in April 2014.

We are also expanding our business by providing games for IPTV. In September 2008, we entered into a licensing agreement with Iconix Entertainment Co., Ltd., or Iconix Entertainment, to develop and publish Pororo Game, an IPTV game based on Iconix Entertainment's 3D TV animation series "Pororo: The Little Penguin." We commercially launched Pororo Game in September 2009 and renewed our licensing agreement with Iconix Entertainment in September 2011, September 2012 and September 2013.

The amount of revenues from console and IPTV games represented 3.7% of our total revenues or Won 1,744 million (US\$1,653 thousand) in 2013 and 5.3% of our total revenues or Won 3,080 million in 2012.

Game character merchandising

In order to optimize the commercial opportunities presented by our games and their characters, we and our licensees have been marketing dolls, stationery, food and other character-based merchandise, as well as game manuals, monthly magazines and other publications, based on our games. We currently have arrangements with GungHo to license Ragnarok Online's game characters in Japan and with AsiaSoft Corporation

Public Co., Ltd. to license Ragnarok Online II game characters in Thailand.

Table of Contents

The amount of revenues from game character merchandising represented less than 1% of our total revenues in each of 2013 and 2012.

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 a 26 half-hour episode animation series based on the storyline and characters of Ragnarok Online in October 2004. The series was produced by Gravity Entertainment and broadcast on television in nine countries from 2004 through 2007. 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. Our revenues from our animation business represented less than 1% of our total revenues in each of 2013 and 2012.

Other services

NeoCyon provides Web site development and operation services to third parties in addition to its core mobile games business. In addition, we generate revenues from sales of goods related to mobile phones, such as ornamental accessories manufactured or procured by third parties, based on consignment sale agreements with such third parties. The amount of revenues from other services represented 4.3% of our total revenues or Won 2,064 million (US\$1,956 thousand) in 2013, compared with 7.6% of our total revenues or Won 4,375 million in 2012.

OUR MARKETS

Korea, Japan, the United States and Canada, Taiwan and Hong Kong/Macau, and China were our biggest geographic markets in 2013 in terms of revenue. Each of these markets is serviced either by us or a distribution company. We and NeoCyon directly manage online and mobile game operations in Korea, respectively. Gravity Interactive, our wholly-owned subsidiary, manages game operations in the United States and Canada. GungHo Online Entertainment, Inc. is our licensee for Ragnarok Online, Ragnarok Mobile Story and Ragnarok Violet in Japan. Game Flier International Corporation is our licensee for Ragnarok Online and Dragonica in Taiwan, Hong Kong and Macau, and Joymaster Inc. is our licensee for Ragnarok Online Uprising: Valkyrie in Taiwan. Beijing Kunlun Online Network Tech Co., Ltd. is our licensee for Ragnarok Online and Kingworld (Beijing) Technology Co., Ltd. is our licensee for Dragonica in China. Lansha Information Technology (Shanghai) Co., Ltd. is our licensee for Ragnarok Online Uprising: Valkyrie and Meiyu Information & Technology (Shanghai) Co., Ltd. is our licensee for Ragnarok Violet in China.

Table of Contents

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, 2013.

| Countries | Year Ended December 31, | | | | | 2013 ⁽¹⁾ |
|-------------------------------------|--|-----------------|-----------------|---------------|--------------------|---------------------|
| | 2011 | 2012 | 2013 | | | |
| | (In millions of Won and thousands of US\$, except percentages) | | | | | |
| Korea | ₩ 10,458 | ₩ 14,762 | ₩ 15,491 | 32.5% | US\$ 14,680 | |
| Japan | 29,513 | 30,387 | 14,409 | 30.2 | 13,655 | |
| United States/Canada ⁽²⁾ | 5,879 | 5,023 | 7,725 | 16.2 | 7,321 | |
| Taiwan/Hong Kong/Macau | 3,590 | 2,244 | 3,106 | 6.5 | 2,943 | |
| China | 749 | 495 | 2,734 | 5.7 | 2,591 | |
| Others | 7,288 | 4,870 | 4,220 | 8.9 | 3,998 | |
| Total | ₩ 57,477 | ₩ 57,781 | ₩ 47,685 | 100.0% | US\$ 45,188 | |

Notes:

- (1) For convenience only, the Won amounts are expressed in U.S. dollars at the rate of Won 1,055.25 to US\$1.00, the noon buying rate in effect on December 31, 2013 as certified by the Federal Reserve Bank of New York for customs purposes.
- (2) Revenues in the United States and Canada, as shown on this table, also include subscription and other types of game revenues generated in other countries managed by Gravity Interactive. Such revenues from other countries constitute a minor portion of the revenues recorded as subscription revenues from the United States and Canada.

Korea

In Korea, we commercially launched and began to charge users for Ragnarok Online in August 2002, followed by other games. Our online game users in Korea consist of individual PC account users and Internet café subscribers. Individual PC account users 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 online games together with their peers with more powerful PC hardware and faster broadband Internet access than they have at home. Most Internet cafés charge their customers PC usage and Internet access fees of Won 959 on average per hour and subscribe to various online games. Over 9,600 and 9,800 Internet cafés offered our games in Korea according to our internal data as of December 31, 2013 and 2012, respectively. In order to offer our games, an Internet café typically purchases minimum game hours from us. Subscription fees from Internet cafés accounted for 8.2% and 5.2% of our subscription revenues in Korea in 2013 and 2012, respectively.

Overseas markets

Ragnarok Online is commercially offered in the following 59 overseas countries and markets: Japan, Taiwan, Hong Kong, Macau, the United States, Canada, Australia, New Zealand, India, Singapore, Malaysia, Thailand, the Philippines, Indonesia, Brazil, Russia, Armenia, Azerbaijan, Belarus, Estonia, Georgia, Kazakhstan, Kyrgyzstan, Latvia, Lithuania, Moldova, Tajikistan, Turkmenistan, Ukraine, Uzbekistan, France, Belgium, the United Kingdom, Finland, Sweden, Norway, Ireland, Scotland, Denmark, Spain, Austria, Bulgaria, Cyprus, Czech Republic, Germany, Greece, Hungary, Italy, Luxembourg, Malta, Netherlands, Poland, Portugal, Romania, Slovakia, Slovenia, Switzerland, Turkey and China. Ragnarok Online is distributed through local game operators and distributors, except for the United States, Canada, Australia, New Zealand, India, Singapore and Malaysia in which Gravity Interactive directly publishes Ragnarok Online.

Edgar Filing: GRAVITY Co., Ltd. - Form 20-F

Table of Contents

The following table lists the overseas countries and markets 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 dates and expiry dates of the license agreements.

| Country | Licensee | Date of License Agreement | Date of Commercial Launch | Date of Expiry |
|---|---|---------------------------|---------------------------|----------------|
| Japan | GungHo Online Entertainment, Inc. | July 2002 | December 2002 | September 2015 |
| Taiwan/Hong Kong/Macau | Game Flier International Corporation ⁽¹⁾ | May 2002 | October 2002 | October 2015 |
| Thailand | AsiaSoft Corporation Public Co., Ltd. | June 2002 | March 2003 | March 2015 |
| Philippines | Level Up! Inc. | March 2003 | September 2003 | December 2014 |
| Indonesia | PT. Lyto Datarindo Fortuna | April 2004 | November 2003 | February 2015 |
| Brazil | Level Up! Interactive S.A. | August 2004 | February 2005 | March 2016 |
| Russia and CIS countries ⁽²⁾ | Ingamba LLC | June 2010 | March 2007 | June 2015 |
| Europe ⁽³⁾ | Gravity EU SAS ⁽⁴⁾ | June 2011 | April 2004 ⁽⁵⁾ | June 2014 |
| China | Beijing Kunlun Online Network Tech Co., Ltd. | March 2012 | February 2013 | February 2016 |

Notes:

- (1) Game Flier International Corporation is a subsidiary of Soft-World International Corporation.
- (2) Represents game operations in Russia, Armenia, Azerbaijan, Belarus, Estonia, Georgia, Kazakhstan, Kyrgyzstan, Latvia, Lithuania, Moldova, Tajikistan, Turkmenistan, Ukraine and Uzbekistan. A single operator services such 15 countries under one license agreement.
- (3) Represents game operations in France, Belgium, the United Kingdom, Finland, Sweden, Norway, Ireland, Scotland, Denmark, Spain, Austria, Bulgaria, Cyprus, Czech Republic, Germany, Greece, Hungary, Italy, Luxembourg, Malta, Netherlands, Poland, Portugal, Romania, Slovakia, Slovenia, Switzerland and Turkey.
- (4) We own a 25% equity interest in Gravity EU SAS, a joint venture company for game service in Europe.
- (5) Ragnarok Online was initially launched in Germany, Austria, Switzerland, Italy and Turkey with a different licensee in April 2004.

Ragnarok Online II is currently commercially offered globally excluding Japan, the Philippines, Vietnam, Brazil and China. Requiem is currently commercially offered worldwide. Dragonica is currently commercially offered in the United States, Canada, South America and 32 other countries and markets. R.O.S.E. Online is currently commercially offered in the United States, Canada, Mexico and 40 other countries. Ragnarok Prequel is currently commercially offered in China. While most of our mobile games are commercially offered in Korea, we also provide those developed in-house in overseas countries, including the United States, Japan, Taiwan and China, among others. 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

Table of Contents

ongoing royalty payments based on a percentage of revenues generated from subscription fees and/or micro-transactions 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, in our case, 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. In addition, since January 2007, we have opened free-to-play servers, which only apply the micro-transaction model, in all the countries and markets where Ragnarok Online is serviced except China 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 micro-transaction model. We offer Ragnarok Online services only with the micro-transaction model in all the countries and markets where Ragnarok Online is serviced except Japan, Taiwan, Hong Kong, Macau, Thailand, the Philippines and China. The amount of revenue generated from micro-transactions as a percentage of revenue varies by country and market. For example, in 2013, the approximate percentage of revenue derived from micro-transactions accounted for 24.7% of total royalty revenues for Japan, and 97.4% of total royalty revenues for Taiwan, Hong Kong and Macau.

Since September 2007, we have been offering premium services as an additional revenue model, where players are offered certain additional features such as the faster accumulation of experience points or higher rates of item drops for additional fees during a specified period of time, in all the countries and markets where Ragnarok Online is serviced except Japan, Taiwan, Hong Kong, Macau and China. The pricing for Ragnarok Online in Korea and in Japan, the United States and Canada, our principal overseas markets, are set forth below.

Korea

Individual PC account users 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, to buy G Cash which can be used for any games we offer and convert G Cash to RO Points, the currency of the money used in Ragnarok Online which enable them to buy game items or subscribe to Premium Services. Internet café subscribers make payments through credit card or bank transfers. We pay a commission in the range of 1.4% to 15% to third parties to process payments. These third parties bear the delinquency risk associated with payments from users.

Table of Contents***Subscription-based fee model***

The subscription-based fee model is currently applied only to Internet cafés and not individual PC users in Korea. The following table sets forth our published pricing plans for Internet cafés in Korea for Ragnarok Online access as of December 31, 2013.

| Hours⁽¹⁾ | Flat Fee per PC |
|----------------------------|------------------------|
| 300 hours | ₩ 69,300 |
| 600 hours | 138,600 |
| 1,000 hours | 231,000 |
| 2,000 hours | 462,000 |

Note:

- (1) Actual hours may vary depending on additional bonus hours we offer in proportion to hours purchased by the subscriber.

Micro-transaction model

We have applied a micro-transaction model in Korea since April 2007. The price range of each of the game items is between Won 250 and Won 29,800. There are certain game items which users can buy only at Internet cafés.

Premium Service model

Premium Service model was initially applied to free-to-play servers in July 2008 and became available on all the servers in November 2010 when we ceased to apply the subscription-based fee model for individual PC users in Korea. We offer only one rate for the Premium Service model of Ragnarok Online in Korea and charge 5,500 RO Points for 30 days of use. Premium Service users may further choose to use additional services as options, such as faster accumulation of experience points, higher rates of item drops, lower death penalty or a combination of such additional services for additional fees.

Japan

GungHo, our licensee in Japan, determines the pricing plan for Ragnarok Online in Japan. A majority of users in Japan typically pay to gain access to or purchase game items of Ragnarok Online with prepaid cards, such as WebMoney, among others, which can be purchased at convenience stores or retail game outlets, or online. In addition, credit cards are also a popular payment method. Mobile payment, which was introduced in April 2008, is increasingly popular although it cannot be used for the payment of subscription-based fees and can be used only for payment for micro-transactions.

Subscription-based fee model

Our licensee in Japan offers only one rate for Ragnarok Online and charges JPY1,500 per 30 days of unlimited use.

Micro-transaction model

We have applied a micro-transaction model in Japan since December 2006. Game users buy GungHo Shop Points which enable them to buy game items or directly buy game items from the mobile item shop.

Table of Contents

The price range of the game items is between JPY50 and JPY1,500. The following table sets forth our licensee's published basic pricing for GungHo Shop Points in Japan as of December 31, 2013.

| Points | Retail Price⁽¹⁾ | |
|----------------|-----------------------------------|--------|
| 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 convenience only, on December 31, 2013, the noon buying rate of Japanese Yen to U.S. dollars as certified by the Federal Reserve Bank of New York for customs purposes was JPY105.25 to US\$1.00.

The United States and Canada

Gravity Interactive, our wholly-owned subsidiary in the United States, determines the pricing plan for Ragnarok Online in the United States and Canada. Users pay through credit cards, wire and/or bank transfers, or mobile payment or online payment systems such as PayPal. Gravity Interactive ceased to apply the subscription-based fee model in April 2011.

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 in the price range between US\$0.05 and US\$20. 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, 2013.

| Points | Retail Price | |
|---------------|---------------------|--------|
| 1,100 points | US\$ | 10.00 |
| 1,650 points | | 15.00 |
| 2,875 points | | 25.00 |
| 4,600 points | | 40.00 |
| 6,000 points | | 50.00 |
| 9,000 points | | 75.00 |
| 12,000 points | | 100.00 |

VIP Service fee model

Although Ragnarok Online is offered based on the micro-transaction model in the United States and Canada, the VIP Service fee model, a premium service model, was introduced in April 2011 to provide users with enhanced game play as an option. The following table sets forth Gravity Interactive's published basic pricing for VIP Service for Ragnarok Online in the United States and Canada as of December 31, 2013.

| Days and Points | Retail Price | |
|---|---------------------|-------|
| 30 days | US\$ | 7.00 |
| 30 days and 1,500 points ⁽¹⁾ | | 15.00 |
| 90 days | | 19.00 |
| 180 days | | 33.50 |

Note:

- (1) Once a user purchases this package, the user cannot purchase it again before the period of the purchased package ends.

Table of Contents

GAME DEVELOPMENT AND PUBLISHING

We expect the online and mobile game industries to be characterized by increasing demand for sophisticated or original games with the most up-to-date technologies and/or innovative game designs. In response, we intend to expand our game offerings by continuing to develop in-house additional high quality games with the latest technologies and/or innovative game designs and by publishing such new games developed by us or licensed or acquired from renowned third party developers.

To prepare for the commercial launch of a new online game, unlike most mobile games, we conduct closed beta testing for the game to fix technical problems, which is followed by a period of open beta testing in which we allow registered users to play the game free of charge. During these testing periods, users provide us with feedback and our technical team seeks to address any technical problems and programming flaws that may compromise a stable and consistent game playing environment. We conduct several rounds of closed beta testing, which usually takes a few weeks for each round but may take significantly more time if material problems are detected. Open beta testing of online games usually takes one to three months before commercial launch. We generally commence our other marketing activities for online games during the open beta testing stage. For overseas markets, we also localize the language and content of our games to tailor the game to local cultural preferences.

In-house game development

Our game development department is divided into two categories of development teams: one is dedicated to online games and the other is dedicated to mobile games. As of December 31, 2013, we employed a total of 162 game developers. We developed Ragnarok Online, Ragnarok Online II, Requiem, Pucca Racing and some social network games and mobile games, such as Ragnarok Online Uprising: Valkyrie and Tower of Ascension, in-house. In order to remain competitive, we are focusing our in-house game development efforts on enhancing the game experience and on developing new games incorporating the latest technologies (including software improving the communication and interaction between players).

Publishing

We also seek opportunities to publish games developed by third parties if we determine such games have potential to become a commercial success. Our publishing and licensing processes include the following:

Preliminary screening. Our preliminary screening process for a game usually includes preliminary review and testing of the game and discussions with the game developer on technological and operational aspects;

In-depth examination, analysis and commercial negotiation. Once a game passes preliminary screening, we thoroughly review and test the game, conduct a cost analysis, develop operational and financial projections and formulate a preliminary game operating plan. We then begin commercial negotiations with the developer;

Game rating and regulatory registration and approval. Once a license agreement to publish and distribute a game is signed, we submit an application to the Game Rating and Administration Committee to obtain a game rating, except for mobile games, which are not required to be rated by the Game Rating and Administration Committee and may be rated by us as distributor. This process generally takes approximately 15 days. We also typically register our intellectual property rights in Korea under our license agreements, such as copyright and trademark, with the relevant Korean government agency. Our overseas subsidiaries or licensees follow similar procedures in their respective markets where the games we license are commercially offered; and

Testing and marketing. Once the required registration and approvals are obtained, we conduct closed beta testing and open beta testing of the new game and assist the licensor with the development of the game, in the case of online games.

Table of Contents

Our game business team takes the lead in conducting preliminary screenings to select games for potential distribution and the commercial negotiations process. The games initially screened by our game business team are additionally evaluated or tested by other teams, such as the marketing team and quality management team, for a second opinion. Once a license agreement is finalized, we generally create a specific team for the selected game within the marketing department to work with and guide the licensor through the beta testing and/or marketing process for a successful launch of the game.

MARKETING

We employ a variety of traditional and online marketing programs and promotional activities, including in-game events, in-game marketing and offline events. Due to the close-knit nature of the game community, we believe that word-of-mouth is an important medium for the promotion of our games.

In Korea, three independent promotional agents currently promote our online games to Internet cafés pursuant to agency agreements. Under these agreements, each promotional agent is granted non-exclusive promotion rights within a specified geographical area. The agent is generally paid a monthly base commission between 10% and 30% of revenues received from Internet cafés in the allocated area. The commission percentage varies according to the amount of revenues.

We conduct a variety of marketing programs and online and offline events to target potential subscribers accessing the Internet from home. Our main marketing efforts include advertising on Web site portals and in online game magazines, conducting online promotional events, participating in trade shows and entering into promotional alliances with Internet service providers. We spent Won 2,852 million (US\$2,703 thousand) on advertising and promotions in 2013, compared with Won 4,585 million in 2012.

We frequently organize in-game events, such as "fortress raids" for our users, which we believe encourages the development of virtual communities among our users and increases user interest in our games. We also host from time to time in-game tournaments in which users can compete against each other either as a team or individually. In addition, we use in-game events to introduce users to new features of our games. We organized 42 in-game events for Ragnarok Online users in 2013, compared with 28 such in-game events in 2012. In November 2013, we hosted in Japan with GungHo, our licensee in Japan, the Ragnarok World Championship, an offline competition event with approximately 56 active participants, comprised of representatives from 6 teams representing each country and approximately 8 representatives of our five licensees. The event was visited by approximately 2,500 visitors and broadcast live on the Web, which recorded 150,000 views worldwide.

In most of our overseas markets, marketing activities are principally conducted by our licensees and typically consist of advertising on Web site game portals and online game magazines and through television commercials, as well as hosting online and offline promotional events. The licensees are responsible for the costs associated with such advertising and promotional activities. For example, GungHo hosted the GungHo Festival in April 2013, which included the Ragnarok Online Japan Championship, game conference and costume-play stage and other programs for users, and the event was attended by approximately 4,400 visitors. In November 2013, GungHo hosted the Ragnarok Online Eleventh Anniversary Festa which included the Ragnarok World Championship and was attended by approximately 2,500 visitors and broadcast live on the Web and watched by approximately 210,000 viewers. GungHo also sells a DVD and a memorial package of Ragnarok Online software to commemorate the Ragnarok Online Japan Championship every year. Level Up! Inc., our licensee in the Philippines, hosted a tenth anniversary event in September 2013 to celebrate the service of Ragnarok Online in the Philippines starting in 2003, which included the Ragnarok Online Philippines Championship, and such event was attended by approximately 2,500 visitors. Level Up! Inc. also hosted marketing events for all the games published by them, namely Level Up! Live, an annual event which gathered 10,000 in 2013, Level Up! Guild Congress and Level Up! saLU-salo in July 2013, November 2013 and December 2013, respectively. PT. Lyto Datarindo Fortuna, our licensee in Indonesia, hosted an annual event called the Lyto Festival in October 2013 to celebrate the tenth anniversary of the service of Ragnarok Online in Indonesia and to promote Ragnarok Online II, the commercial service of which started in Indonesia in August 2013. The Lyto

Table of Contents

Festival in 2013, which was attended by approximately 12,000 visitors, included the Ragnarok Online Indonesia Championship and the Ragnarok Online II dungeon competition. AsiaSoft Corporation Public Co., Ltd., our licensee in Thailand, hosted the PlayPark FanFest in October 2013, formerly the AsiaSoft All Star Battle, which has been held annually since 2009. The PlayPark FanFest, attended by approximately 30,000 visitors, included the Ragnarok Online Thailand Championship and other promotional events and visitors were invited to experience Ragnarok Online II, a then newly introduced game in Thailand, at the game's booth.

In addition, from time to time our overseas licensees also market our games through sponsoring promotional events jointly with other local game publishers or participating in expositions or other events for online games in order to reach a broader local audience. For example, Gravity EU SAS, our licensee in France, participated in several conventions for animation, game, manga and costume play, such as Japanior and Paris Manga in France in May 2013 and in October 2013, respectively, and AnimagiC and Connichi in Germany in July 2013 and in September 2013, respectively, where Gravity EU SAS set up booths to present Ragnarok Online and Ragnarok Online II to the public and held various events for visitors. Game Flier International Corporation, our licensee in Taiwan, and Beijing Kunlun Online Network Tech Co., Ltd., our licensee in China, participated in the Taipei Game show in January 2013 and the ChinaJoy Expo in July 2013, respectively.

Our licensees are selected in part on the basis of their marketing capabilities, including the size and scope of their distribution networks. In regions where we have a limited network or presence such as Central Asia, we believe that conducting marketing through our licensees is more effective and cost-efficient than direct marketing by us in light of the established brand recognition and marketing networks of our licensees and their comparative advantage in identifying and taking advantage of the cultural and other local preferences of overseas users. However, in more strategic markets where we anticipate considerable growth such as the United States, we also believe that it is important to enhance our own direct publishing network for online game services.

GAME SUPPORT AND CUSTOMER SERVICE

We are committed to providing superior customer service to our users directly and through our licensees. As of December 31, 2013, 6 employees were game masters, or persons who are in charge of testing, updating and providing server maintenance for online games, as well as dealing with customer complaints, 26 employees were members of our domestic customer service team and 44 employees were members of our overseas customer support team.

In Korea, we provide customer service for our online games through bulletin boards of the Web sites of our online games, call centers, email and facsimile and at our walk-in customer service center. Our bulletin boards of the Web sites of our online games allow our customers to post questions to, and receive responses from, other users and our support staff. In our overseas markets, our licensees administer customer service through varying combinations of bulletin boards of the Web sites of our online games, call centers, email and facsimile, with assistance from time to time from our overseas customer support staff.

In addition to providing customer service to our users, our customer service staff also collect user comments with respect to our games and generate daily and weekly reports for our management and operations that summarize important issues raised by users as well as how such issues have been addressed.

NETWORK AND TECHNOLOGY INFRASTRUCTURE

We have designed and assembled our game server network and information management system in Korea to allow centralized game management on a global basis. Our system network is designed to speedily accommodate a growing user base and demand for faster game performance. Our game server architecture runs multiple servers on a parallel basis to readily accommodate increased user traffic through deployment of connection to servers, which permits us to route users in the same country to servers with less user traffic. Each of these servers is linked to our information systems network to ensure rapid implementation of game upgrades and to facilitate game monitoring and supervision.

Table of Contents

We maintain our server hardware in a single climate-controlled facility at KT Mokdong Internet Computing Center at 233-5 Mokdongdong-ro, Yangcheon-gu, Seoul, Korea and our other system hardware in our offices in Seoul. As of December 31, 2013, our server network for our game operations in Korea consisted of a total of 486 servers, including 198 physical servers and 288 servers run on 83 physical servers through the server virtualization technology we have adopted since July 2011, which allows one physical server to be divided into multiple virtual servers, each of which functions individually as a complete and independent server.

In overseas markets, our overseas subsidiaries or licensees own or lease the servers necessary to establish the server network for online games and we assist them with the initial assembly and installation of operating game servers and optimization of their systems network for game operations in their respective markets. While the overseas system architectures are modeled on our system architecture in Korea, they are also tailored to meet the specific needs of each market. When we install and initialize a game in an overseas market, we generally dispatch network engineers and database technicians from Korea to assist with the assembly and operation of the system network and game servers. Following installation, we typically send two to five of our technicians and customer support staff to that market, for a few weeks in some cases and much longer periods in other cases, to assist with on-site game operation and technical support. Our overseas subsidiaries and licensees are responsible for providing database and other game information backup.

Our game management software can program the game content to include localized features such as virtual map zones specific to each market. These features can be updated at the host country level in order to encourage development of a communal spirit among the users from the same country.

COMPETITION

We compete primarily with other online and mobile game developers and distributors in each of our markets. In addition, we compete against providers of games on various platforms, such as console games, handheld games and arcade games. We compete primarily on the basis of the quality of the game experience offered by us to our users, which depends on a number of factors, including our ability to do the following:

hire and retain creative personnel to develop games that appeal to our users;

offer online and mobile game service that is stable and is not prone to server shutdowns, connection problems or other technical difficulties;

provide timely and responsive customer service; and

establish payment systems that are secure and efficient.

Competition in the online game industry

Currently, the leading providers of online games, based on the number of peak concurrent users, are Riot Games, Inc., Activision Blizzard, Inc., Nexon Co., Ltd. and NCsoft Corp. according to data available from various public sources. League of Legends of Riot Games, Inc., Dungeon Fighter Online of Nexon Co., Ltd., and World of Warcraft of Activision Blizzard, Inc., are some of the most popular online games. NCsoft Corp.'s Lineage, Guild Wars and Aion have gained popularity, and each has maintained a large number of players and a loyal user base.

As many of our competitors have significantly greater financial, marketing and game development resources than we have, we face intense competition in the online game industry. We expect competition will continue to be strong as the number of online game developers increases in the future and the online game industry begins to consolidate into a small number of leading companies due to the high cost of game development, marketing and distribution networks, which is likely to drive unsuccessful online game providers to go out of business or be acquired by other successful game providers.

Table of Contents

Competition in the mobile game industry

Compared with the online or console game genres, the mobile game market has a relatively low barrier to entry because development of a mobile game requires relatively less time and personnel due to the limitations of the devices on which mobile games are played such as screen size and processing power. Moreover, development tools for mobile games are easier to obtain and use, and open marketplaces, such as the Google Play Store and Apple's App Store, enable developers to easily distribute mobile games to a large global audience. Therefore, we expect the number of mobile game developers to continually increase in the future and competition to become more intense.

We compete with companies that specialize in developing mobile games such as Supercell Oy and King Digital Entertainment PLC. Our current or potential future competitors for mobile games also include package game companies that have successfully expanded their business into mobile game development such as Electronic Arts Inc. In addition, we believe more companies that previously were or currently are dedicated to developing online or console games will allocate more resources toward developing mobile games because the number of mobile game users is rapidly increasing as the penetration of mobile devices, such as smartphones and tablet computers, continues to deepen.

Competition from other game platforms

We also compete against PC and console-based game developers that produce popular package games, such as Activision Blizzard, Inc. and Electronic Arts Inc., and game console manufacturers such as Microsoft Corp., Sony Computer Entertainment Inc. and Nintendo Co., Ltd., all of which also have their own console game development studios. In November 2013, Microsoft Corp. released Xbox One featuring Kinect motion control camera and voice commands and Sony Computer Entertainment Inc. started distributing its PlayStation 4 game consoles featuring a controller with a capacitive touchpad for additional control options. Nintendo Co., Ltd.'s Wii U was released in November 2012 which supports high-definition graphics with a tablet-like controller. In addition, handheld game consoles, such as Nintendo Co., Ltd.'s Nintendo 3DS and Sony Computer Entertainment Inc.'s PlayStation Vita, are also popular among game users. All the current game consoles enable users to play games with other users online by connecting their console to a network over the Internet. Likewise, a number of PC-based game developers have also introduced online features to their PC-packaged games, such as team plays or users-to-users combat.

Competition in the game market is expected to remain intense as established game companies with significant financial resources seek to enter the industry. For a discussion of risks relating to competition, see ITEM 3.D. "RISK FACTORS RISKS RELATING TO OUR BUSINESS We operate in a highly competitive industry and compete against many large companies."

INSURANCE

We maintain medical and accident insurance for our employees to the extent required under Korean law, and we also maintain fire and general commercial insurance with respect to our facilities. We do not have any business liability or disruption insurance coverage for our operations in Korea. We maintain a directors' and officers' liability insurance policy covering certain potential liabilities of our directors and officers. See ITEM 3.D. "RISK FACTORS RISKS RELATING TO OUR BUSINESS We have limited business insurance coverage and any business interruption could have a material adverse effect on our business."

INTELLECTUAL PROPERTY

Our intellectual property is an essential element of our business. We rely on intellectual property such as copyrights, trademarks and trade secrets, as well as non-competition, confidentiality and license agreements with our employees, suppliers, licensees, business partners and others to protect our intellectual property rights. Our employees are generally required to sign agreements acknowledging that all inventions, trade secrets, works of authorship, developments and other processes generated by them on our behalf are our property, and assigning to us any ownership rights that they may claim in those works.

Table of Contents

With respect to copyrights and computer program rights created by our employees within their employment scope and which are made public bearing our name, we are not required to pay any additional compensation to our employees.

In developing Ragnarok Online, we obtained an exclusive license from Mr. Myoung-Jin Lee to use the storyline and characters from his cartoon titled Ragnarok for the production of games, animation and character merchandising. See ITEM 4.B. "BUSINESS OVERVIEW OUR PRODUCTS Online games Ragnarok Online."

We are the registered owner of 13 registered software copyrights to ten games: Ragnarok Online, Ragnarok Online II, R.O.S.E. Online, Requiem, Ragnarok Violet, Ragnarok Angel Poring, Ragnarok Online Uprising: Valkyrie, Arcturus, Pucca Racing and W Baseball, each of which has been registered with the Korea Copyright Commission. We no longer commercially offer Arcturus, a PC-based, stand-alone game, nor Pucca Racing, and have decided to cease commercialization of W Baseball. As of December 31, 2013, we owned over 50 registered domain names, including our official Web site and domain names registered in connection with each of the games we offer. We had 875 registered discrete trademarks at patent and trademark offices in 51 countries as of December 31, 2013. We had three design patents, two analogous design patents, which are variations of two of the design patents, registered with the Korea Intellectual Property Office, registered copyrights covering 11 game characters, five online game business model patents and one patent pending with the Korea Intellectual Property Office, in each case as of December 31, 2013.

SEASONALITY

Usage of our online games has typically increased slightly around the New Year's holiday and other holidays, in particular during winter and summer school holidays.

LAWS AND REGULATIONS

We are subject to many laws and regulations in the different countries in which we operate. See ITEM 3.D. "RISK FACTORS RISKS RELATING TO OUR REGULATORY ENVIRONMENT." A general overview of the material laws and regulations that apply to our business is provided below for the countries from which we derive a significant portion of our revenues.

Korea

The Korean game industry and online and mobile game companies operating in Korea are subject to the following laws and regulations:

The Act on Promotion of the Game Industry

In January 2007, the National Assembly amended the Act on Promotion of the Game Industry, or the Promotion Act, which became effective on April 20, 2007. Under the amended Article 21 of the Promotion Act, online games are classified into four categories: "suitable for users of all ages," "suitable for users 12 years of age or older," "suitable for users 15 years of age or older" and "suitable for users 18 years of age or older." The 15 years of age or older category was added between the 12 years of age and 18 years of age categories to increase ratings flexibility. Ragnarok Online has been classified as "suitable for users 12 years of age or older."

The amendment to the Promotion Act includes for the first time the definition of the term "speculative game." A speculative game refers to a game that permits betting and offers monetary loss or profit that is determined by chance. Elements that may cause a game to be considered a speculative game include the existence of game money used as a means for betting or purchasing game items (items used within the game for progression in the game) that become the subject of exchange with respect to the game money. The Supreme Court decision No. 2007-4702 rendered on October 26, 2007 provided that the determination of whether a business is speculative or not requires a comprehensive consideration of the following factors: the purpose of use, the method and appearance of use, whether money or gifts

Table of Contents

exchangeable with money are distributed as a result of using the business, the degree and scale thereof, and whether gifts are actually exchanged into cash. Although the new rules and Supreme Court decision are intended to provide more clarity for the determination of whether a game is deemed speculative or not, because our games involve transactions with game items, we may have to expend much effort to ensure that we are in compliance with the new rules.

A game provider has to report any modification in the content of a game to the Game Rating and Administration Committee, which may require the game to be reclassified depending on the scope of the modification. If the Game Rating and Administration Committee determines that the game is speculative, it can refuse to classify such game, in which case the game will be prohibited. According to Article 1(2) of the Enforcement Decree of the Promotion Act newly established on May 16, 2007, any games in which money or items of value are collected from a multiple number of persons and profits or losses are allocated based on winnings or losses determined by chance fall under speculative games. According to Article 16(2) of the Enforcement Decree of the Promotion Act newly established at the same time, so long as certain guidelines are followed, a provision of a gift equivalent to a customer price of Won 5,000 or less, with respect to games that are classified as "suitable for users of all ages," is not deemed to be an act that encourages gambling.

Under the Promotion Act, as partially amended on December 21, 2007, the Minister of Culture, Sports and Tourism may order information and communication service providers to refuse, stop, or restrict the offering of games if such games are unrated, contents are different from those submitted for rating, were denied rating as speculative games, or were manufactured or distributed by a person not registered for operation of manufacturing or distributing games for profit-making. The Game Rating and Administration Committee undertakes examination of the information and communications service providers and provides recommendation of correction to the providers as necessary. The information and communications service providers are required to implement the corrective measures recommended within 7 days and report the results thereof to the chairman of the Game Rating and Administration Committee or the Minister of Culture, Sports and Tourism.

The Game Rating and Administration Committee published the Yearbook for Classification of Game Ratings' in September 2008, June 2009, July 2011 and June 2012 in order to provide information on industry trends. The Yearbooks include data on ratings and classifications of various games released in Korea and the results of the examination of the information and communications service providers during the years 2007, 2008, 2010 and 2011. The Game Rating and Administration Committee published the Yearbook to improve fairness and transparency in inspecting games and to provide industry participants with guidelines on ratings inspection as well as basic information on the development of the game industry.

Prior to a partial amendment on January 1, 2010, the Promotion Act provided that governmental support for the Game Rating and Administration Committee would be provided until December 31, 2009 and the task of rating games would thereafter be privatized. However, based on the determination of the government that the required social conditions for such privatization are not yet established, the Promotion Act, as partially amended on January 1, 2010, promoted the sustained rating of games and operation of supplementary administrative tasks by extending the date for the provision of governmental support until December 31, 2011.

On April 12, 2010, for the purpose of preventing gaming addiction among adults and teenagers and to promote a constructive gaming culture, the Ministry of Culture, Sports and Tourism introduced the "Measures for the Prevention and Alleviation of Excessive Gaming," which includes the following: (i) expanded applicability of the exhaustion system (a program in which the rate at which items are acquired in a game decreases as a person plays the game longer, where this system is closely related to the game scenario); (ii) selective shutdown system for games played by teenagers (a system in which a teenager's access to games can be selectively managed between midnight and 8:00 a.m. with the consent of a parent); (iii) establishment of a fund for the prevention of excessive gaming; and (iv) regulation of Web sites that deal in cash transaction of in-game items.

Table of Contents

Recently in the global online and mobile game industries, there has been growth in the open markets in which small content developers and individual content producers directly supply their programs to consumers. However, under the then-current law, games could be distributed only after being rated by the Game Rating and Administration Committee, and this impeded the development of the open market in Korea. In addition, some games, especially those that permit betting, caused social problems as speculative operating methods illegal automatic playing programs which allow players to cheat and acquire game money or game items were being developed. However, the then-existing laws did not provide sufficient grounds to regulate such situations.

In response, on April 5, 2011, the Act on Promotion of the Game Industry was amended. The amendment provides that all games that cannot receive prior rating by the Game Rating and Administration Committee due to special circumstances in their production and distribution channels should be subject to the distributors' own rating. The Act also provides grounds for sanctioning speculative operating methods and the undermining of fair gaming through illegal programs, among others. The amendment went into effect on July 6, 2011. In addition, consistent with a recent decision by the Constitutional Court on dual punishment, the amendment also includes a revised provision which stipulates that if an employer fulfills her duty of care as a manager and supervisor of her employees, she can be exempt from punishment.

The main content of the Act on Promotion of the Game Industry as amended on April 5, 2011 and the amendment to the Enforcement Decree of the same Act are as follows:

(1) Games which are inappropriate for prior rating by the Game Rating and Administration Committee due to special circumstances in their production and distribution channels, excepting games unsuitable for minors, may be rated by distributors or others involved in the distribution channel at their discretion according to the standards predetermined upon consultation with the Game Rating and Administration Committee. According to Article 11-4 of the Amendment to the Enforcement Decree of the Act on Promotion of the Game Industry, games should fulfill all the following requirements in order to be considered being "inappropriate for prior rating by the Game Rating and Administration Committee": (i) they must be provided through basic communications services by persons who are authorized to engage in the basic communications business under the Telecommunications Business Act; (ii) they must be provided through electronic commerce intermediaries such as online open markets; and (iii) they must be provided using wireless telecommunications terminals which use mobile telecommunications terminals or the same kind of operating programs as those run on mobile telecommunications terminals;

(2) Game-related companies are prohibited from encouraging speculation by using operating methods, devices or machines closely related to the realization of game contents, and any person violating this provision is subject to corrective recommendation or corrective order imposed by the Minister of Culture, Sports, and Tourism;

(3) The act of distributing or manufacturing for distribution computer programs, devices or machines not provided or approved by game-related enterprises for the purpose of interrupting the normal operation of games is prohibited, and any person violating the foregoing is subject to imprisonment for no more than one year or penalty not exceeding Won 10 million; and

(4) In order to realize the principle of responsibility in the dual punishment provision, if an employer fulfills her duty of care as a manager and supervisor with respect to her employees, the employer may be exempt from punishment (proviso in Article 47 of the Promotion Act).

The Promotion Act was further amended on July 21, 2011 and went into effect on January 22, 2012. The amendment was intended to create sound gaming culture by clearly defining the responsibilities of the game industry and the government and to encourage public awareness of prevention of excessive gaming.

Table of Contents

The key content of the amendment are as follows:

(1) A game-related enterprise is required to obtain parental consent when a minor joins a game site as a member and to take measures to prevent excessive use of games by imposing a time limit on minors' game usage time. The Minister of Culture, Sports and Tourism may request game-related enterprises to submit or report data relating to such preventive measures and, after an examination thereof, order the relevant game-related enterprises to correct the preventive measures if they are deemed to be insufficient; and

(2) The government shall provide support for educating the public on the appropriate use of games and the Minister of Culture, Sports and Tourism may request the Minister of Education to cooperate with such efforts by providing education on the appropriate use of games in the curriculum of elementary and middle schools.

The Enforcement Decree of the Act on Promotion of the Game Industry was also amended on January 20, 2012 and became effective on January 22, 2012. The amendment aims to provide measures to implement the Promotion Act, including determining the scope of games subject to the measures to prevent excessive use of games and the methods and procedures of such measures and development of methods and procedures to evaluate the appropriateness of the scope of games subject to the nighttime service limitation.

The key content of the amendment are as follows:

(1) The scope of amendment excludes games which are not likely to cause over-immersion and addiction to games, including those made and distributed for the purpose of use and display at game tournaments or fairs and games which are provided by small and medium sized companies (in order to protect small and medium sized companies in the online game industry);

(2) The amendment provides for methods and procedures to prevent excessive use of games such as requiring game-related enterprises to provide the representation of its legal representative that when a minor joins as a member, the enterprise has obtained the necessary parental consents and that it has posted warnings to prevent game users from excessively using games and has display the elapsed time for users; and

(3) The amendment is expected to make the evaluation of the appropriateness of the scope of games subject to the nighttime service limitation with respect to minors under the age of 16 be performed transparently and reasonably by preparing methods and procedures for such evaluation.

The Promotion Act was partially amended as of May 22, 2013 and the amendment went into effect on November 23, 2013. The Game Rating Board had been long criticized for its unfair administration despite its mission to ensure the fairness as a public agency in charge of ex-ante ratings classifications and ex-post management of the rating classifications of games. In response to such criticism, in order to ensure and reinforce the fairness in the administration of works, the Game Rating Board was abolished and the Game Rating and Administration Committee was newly established to take charge of ratings classifications and ex-post management of games suitable for users 18 years of age or older (Article 16). Other key amendments are as follows:

(1) The Game Rating and Administration Committee is incorporated as a corporate entity (newly added Article 16-2);

(2) For the audit and supervision of fair administration of works by the Game Rating and Administration Committee, it is required to have a standing auditor (previously the Game Rating Board only had a non-standing auditor) (Article 17(2));

(3) The scope of rating classification works which may be entrusted to a private agency is expanded from online games into arcade games but the games suitable for users 18 years of age or older are excluded therefrom (Article 24-2);

Table of Contents

(4) A legal ground is provided for possible delegation of the authority of the Minister of Culture, Sports and Tourism with respect to the ex-post management to the Game Rating and Administration Committee (Article 42(2)); and

(5) The time period of the government's financial support to the Game Rating Board was due to expire on December 31, 2012. However, the foregoing time period is deleted to ensure the stable financial support for the operation of the Game Rating and Administration Committee.

The Telecommunications Business Act

Under the Telecommunications Business Act, a person who intends to run a value-added telecommunications business must report to the Korea Communications Commission, or the KCC, which has the authority to accept and monitor such reports. We are classified as a value-added telecommunications service provider such that we are required to prepare and submit statistical reports regarding, among others, the current status of facilities, subscription records and current status of users to the KCC upon its request. The KCC is responsible for compiling information and formulating telecommunications policies under this Telecommunications Business Act. In addition, we are required to report any transfer, takeover, suspension or closing of our business activities to the KCC, which may cancel our registration or order us to suspend our business for a period of up to one year if we fail to comply with its rules and regulations.

According to Article 21 of the Telecommunications Business Act, however, any person who intends to operate a value-added telecommunications business using small-scale telecommunications facilities is exempted from the obligation to report to the KCC. Before this Article was amended on May 11, 2007, small scale value-added telecommunications business operators had difficulty entering the market because only key telecommunications business operators, such as telephone and Internet service providers, could be exempted from such obligations. The amendment has relieved burdens associated with entering the value-added telecommunications business industry and facilitate its growth, which has intensified competition among online game service business operators.

The Act on Consumer Protection for Transactions through Electronic Commerce

Under this Act, we are required to take necessary measures to maintain the security of consumer information related to our electronic settlement services. We are also required to notify consumers when electronic payments are made and to indemnify consumers for damages resulting from misappropriation of consumer information by third parties. We believe that we have instituted appropriate safety measures to protect consumers against data misappropriation. To date, we have not experienced material disputes or claims in this area.

This Act was partially amended on March 22, 2010, and the amendment became effective on the same day. The amendment allows a company to avoid liability under the Act if it has exercised proper care in the management or supervision of its employees.

This Act was further amended in part on February 17, 2012, which became effective on August 17, 2012. The key contents of the amendment are as follows:

(1) The amendment allows an offer to be rescinded through an electronic document when such offer was made through an electronic document by a business operator engaged in electronic commercial transactions;

(2) The amendment requires that, in case of electronic payments, the business operators and electronic payment service providers provide notice on price of goods and period of service and provide procedures through which consumers can verify the matters notified in order to confirm the actual intention of consumers;

(3) The amendment expanded the scope of the issuer of means for advance payment, who has the duty to inform the matters related to the credibility of the payment method as well as the duty to subscribe

Table of Contents

to consumer injury compensation insurance, from the issuer of means for payment used in multiple online stores to issuer of means for payment used in one or more online stores;

(4) The amendment requires that the provider of hosting service, which is a service for establishing online stores and maintaining servers so that business operators may engage in electronic commercial transactions, take measures to verify the identity of the business operator;

(5) The amendment requires cooperation in accordance with the request from the Korean Fair Trade Commission, such as providing identity of the business operator, in case a dispute arises between a business operator and a consumer;

(6) The amendment requires that, prior to entering into contracts, the telecommunications sales operator indicate, advertise or inform customers information on goods and the matters related to the condition and procedures of payment of compensation due to delay in payment of refund so that consumers can accurately understand the terms and conditions of the transaction and enter into transaction not by mistake or error;

(7) The amendment provides that the telecommunications sales broker and the client of the telecommunication sales broker be jointly and severally liable for monetary damages incurred to consumers due to the failure to provide information on the client of the telecommunications sales broker or the failure to provide accurate information, unless the telecommunications sales broker has exercised proper care;

(8) The amendment prohibits the telecommunications sales operator from installing computer programs without the consumer's consent or without providing clear and easy explanation or notice to the consumer, but it does not provide for the penalties or sanctions imposed in case of violation; and

(9) The amendment provides basis on which the Korean Fair Trade Commission and the Korean Consumer Agency can jointly form an investigation committee to investigate violations of this Act.

Prior to the amendment, this Act prescribed that only the transactions in which the one-time payment amount is above Won 50,000 were eligible for protective measures for payment security which impose on telecommunication sales operators, in case of advance payment in the telecommunications sales, a duty to provide escrow service for payment or subscribe to consumer injury compensation insurance upon the election by a consumer of either option. However, under the amended Act which deleted Article 24(3)(i) concerning the application of such protective measures for payment security, the consumer rights protection was enhanced because even transactions whose amount is small, Won 50,000 or less, can benefit from protective measures for payment security. Such amendment was made as of May 28, 2013 and went into effect on November 29, 2013.

The Act on Promotion of Information and Communications Network Utilization and Information Protection, or Information Protection Act

Under the Information Protection Act, we are permitted to gather personal information relating to our subscribers within the scope of their consent. We are, however, generally prohibited from using personal information or providing it to third parties beyond the purposes disclosed in our subscriber agreements. Disclosure of personal information without consent from a subscriber is permitted only if it is necessary for the settlement of information and communication service charges or is expressly permitted by this or any other statute.

We are required to indemnify users for damages occurring as a result of our violation of the foregoing restrictions, unless we can prove the absence of willful misconduct or negligence on our part. We believe that we have instituted appropriate measures and are in compliance with all material restrictions regarding internal mishandling of personal information.

Penalty surcharges are imposed on any telecommunications enterprises violating the regulation on the protection of personal information to recover any unfair profits gained by such enterprises, and some

Table of Contents

conducts, such as collection of personal information of users without their consent, are the subject of criminal punishment. Any telecommunications enterprises violating its obligation to protect personal information by collecting, using, disclosing such information without consent, and not complying with protective measures, may be imposed with surcharges not exceeding 1% of the sales relevant to the conduct of violation in consideration of the details, degree, period, the number of times, and the scale of gained profits.

The Information Protection Act was partially amended on March 17, 2010, and the amendment became effective on the same day. The amendment allows a company to avoid liability under the Act if it has exercised proper care in the management or supervision of its employees. The amendment sets forth rules for (i) designating institutions providing identity authentication services and for discontinuing and closing authentication services in order to safely and efficiently authenticate identities, (ii) suspending identity authentication services or canceling designation as an identity authentication institution in the event that an institution obtains designation through false or other deceptive methods, (iii) separating the process of obtaining consent to share personal information and the process of obtaining consent to consignment of transaction from the process of signing-up for membership, and (iv) notification requirements by telecommunications billing service providers, instead of the previous practice of referring to a Presidential Decree.

The Information Protection Act was further partially amended on February 17, 2012, which became effective in part on August 17, 2012 and in part on February 17, 2013. The key contents of the amendment are as follows:

(1) The amendment prohibits a telecommunications service provider from collecting or using the resident registration number of a user unless such telecommunications service provider has been designated as the identity authentication institution or the statute allows the collection or use of a user's resident registration number. A person in violation may be punished by a fine not exceeding Won 30 million;

(2) The amendment requires that, in case personal information of a user has been lost, stolen, or leaked, the telecommunications service provider shall notify the user and report to the KCC of the incident and take measures to minimize the damages;

(3) The amendment requires that the telecommunications service providers meeting the criteria set by the Presidential Decree, which refers to telecommunication service providers that (i) stored or managed personal information of one million or more users per day on average for the last three months of the immediately preceding year or (ii) has the sales revenue of Won 10 billion or more in telecommunications service in the preceding year, or in the preceding fiscal year in case of companies, regularly notify the particulars of the use of users' personal information collected to users;

(4) The amendment provides basis of prior examination system for information protection, under which the KCC can recommend operators of certain telecommunications service or electric communications business the implementation of protective measures in accordance with the standards of prior examination for information protection determined and published by the KCC, and allows the telecommunications service providers to appoint executive officers for information protection at the director level; and

(5) The amendment abolishes the security assessment system and unifies the system to authentication system for information protection management, which is a comprehensive management including managerial, technical, and physical protective measures for securing safety and credibility of information and communication network. The amendment also provides legal basis for authentication system by personal information protection management, which is a comprehensive management including managerial, technical, and physical protective measures for systematic and continuous personal information protection on information and communication network.

Table of Contents

The Personal Information Protection Act

The Personal Information Protection Act was enacted on March 29, 2011 and went into effect on September 30, 2011. The scope of the Personal Information Protection Act covers anyone dealing with personal information in the private and public sectors.

If a person's personal information is collected or used, or provided to a third person, such person's consent should be obtained, and if personal information is no longer necessary upon achievement of the purpose of the collection and use of personal information, such information should be immediately destroyed.

Any transaction requiring identifiers granted by law for identification purposes, such as the resident registration number, is generally prohibited, and exceptions are recognized on a restrictive basis only if consent is obtained or if required by law. In addition, any person dealing with personal information as determined pursuant to the Presidential Decree, for instance, such as signing up for a Web site, should provide methods other than using the resident registration number.

In the event of a personal information leak, the processor of personal information should promptly notify the affected person after discovering such incident. If the volume of the leak of personal information exceeds a certain number, the processor of personal information should report the incident to the authorities and take necessary measures to minimize damages.

In addition, the same legislation grants to each individual the right to request perusal, the right to request correction or deletion, and the right to request suspension of process with respect to one's personal information, and also provides the methods to exercise such rights.

To promote prompt and fair settlement of disputes concerning personal information, the same legislation also provides that a Personal Information Dispute Settlement Board, or PIDSB, should be established and the PIDSB's decision, if accepted by the disputing parties, should have the same legal effect as settlement by trial. In consideration of the fact that most identity theft cases are large in scale and small in the amount of monetary damages, the legislation adopts a collective dispute settlement system. A class action system for personal information has been adopted, but in order to prevent frivolous class action suits, litigants are required to go through the collective dispute settlement system prior to bringing a class action and cases are limited to those seeking suspension or injunctive relief.

Prior to the amendment dated August 6, 2013, the Personal Information Protection Act permitted the process of personally identifiable information (resident registration number, passport number, driver's license number and foreigner registration number) under limited circumstances such as when required by law or when consent is obtained, and mandated the implementation of security measures to prevent possible loss, theft, leak, alteration or compromise of personally identifiable information. However, it was not successful in deterring massive leak and misappropriation of resident registration numbers and large scale companies responsible for such leakage have escaped civil and/or criminal liabilities often times, which propelled the public distrust and raised the concerns about expansion of secondary damage.

Against the backdrop of the foregoing, the Personal Information Protection Act was amended partially as of August 6, 2013 with respect to personally identifiable information, which will go into effect on August 7, 2014. The key amendments are: (i) in principle, no person dealing with personal information is permitted to process resident registration numbers (newly added Article 24-2); (ii) in the event of loss, theft, leak, alteration or compromise of resident registration numbers, an administrative fine not exceeding Won 500 million may be imposed (newly added Article 34-2); and (iii) it is made clear that if there is substantial ground to suspect a violation of applicable laws and regulation with respect to personal information protection, the Minister of Safety and Public Administration may advise a relevant personal information processor to take disciplinary action against liable person(s) which include the representative director and responsible executive officers (Article 65(2)). Such amendments purport to prevent any possible leak of resident registration numbers and induce companies to discharge to the fullest extent their responsibilities for the protection of personal information such as resident registration numbers.

Table of Contents

The Korean Civil Code and the Act on the Establishment and Management of the Korea Communications Commission

Pursuant to the Korean Civil Code, contracts entered into with minors, who were persons under 20 years of age without parental consent under the Korean Civil Code prior to its amendment, may be invalidated. The definition of minors is changed to persons under 19 years of age in the amendment to the Korean Civil Code on March 7, 2011, which became effective on July 1, 2013. Under the Act on the Establishment and Management of the Korea Communications Commission, the KCC was established to oversee services relating to broadcasting and communications and also to deliberate and resolve matters concerning the protection of users' information and communications. As a result, telecommunication service contracts and online game user agreements are required to specifically set forth procedures for rescinding service contracts, which may be entered into by persons under 20 years of age without parental consent.

In November 2003, the KCC issued an order addressed to 15 major online game companies in Korea, including us, to regulate certain business practices relating to the settlement of service charges involving persons under 20 years of age. The KCC raised concerns about the ability of persons under 20 years of age to subscribe to online game services without parental consent by settling charges payable to online game companies through settlement systems operated by fixed-line or broadband service providers. The order required online game companies to implement more specific and effective procedures to ensure, where relevant, that parental consent has been specifically obtained.

Although only a small number of our current subscribers are using the settlement options mentioned in the KCC order, we are enhancing our age verification and parental consent procedures for players using the relevant settlement options. We do not expect compliance with the KCC order to be burdensome.

Copyright Act and Computer Programs Protection Act, or Copyright Act

The Copyright Act, which was amended on April 22, 2009, was established by combining the "Copyright Act" on the protection of general works and the "Computer Programs Protection Act" on the protection of computer program works in order to maintain the consistency of copyright protection policies and seek an efficient administration thereof. In addition, the Korea Copyright Commission was established by combining the existing Copyright Commission and the Korea Software Copyright Committee, thereby improving the protection of copyrights and the efficiency in its operation. The amended Copyright Act also includes essential elements of the Computer Programs Protection Act which was abolished on July 23, 2009 and, in connection with computer program works, restrictions on software copyrights, reverse analysis of computer programs, and the establishment of the exclusive right to issue computer programs as a special case apart from other kinds of works.

Among the amendments to the Copyrights Act on June 30, 2011, the key content regarding the online game development and services are as follows:

(1) The amendment extends the period of copyright protection from 50 years to 70 years after the death of copyright holders in order to implement the agreements in the Korea-EU Free Trade Agreement;

(2) The amendment categorizes online service providers into four types: simple conduit, caching, hosting and information searching. A simple conduit conducts acts of transmitting, designating routes or providing connections for the transmission of copyrighted materials without correcting contents, or acts of storing copyrighted materials automatically, intermediately and temporarily in the process of transmission for a period reasonably necessary for transmission thereof. Caching is an act of automatically, intermediately and temporarily storing copyrighted materials transmitted at the request of service users for the purpose of allowing subsequent users to efficiently access or receive them. Hosting is an act of storing copyrighted materials in the computers of online service providers at the request of copiers or transmitters. Finally, information searching is an act of enabling users to become aware of or connect to the location of copyrighted materials on the information and communications networks through information search tools; and

Table of Contents

(3) The amendment clarifies the requirements for indemnification with respect to each of the foregoing types.

(i) *Simple conduit.* Indemnification is possible in any of the following events: (a) The online service provider has yet to begin transmitting copyrighted materials; (b) the online service provider has yet to choose copyrighted materials or their receivers; (c) the online service provider adopts a policy to terminate the accounts of owners who repeatedly infringe on copyrights or any other rights protected under the Copyright Act and reasonably implements such a policy; or (d) when a right holder uses standard technical measures to identify and protect works, an online service provider accepts and does not intervene such use;

(ii) *Caching.* Indemnification is possible in any of the following events: (a) all of the indemnification requirements with respect to a simple conduit are met; (b) the online service provider does not modify copyrighted materials; (c) if there are any terms and conditions of access to provided copyrighted materials, the online service provider permits only the users who have complied with such terms and conditions to access such copyrighted materials that are temporarily stored works; or (d) the online service provider observes any rules of circulation of the copyrighted materials which are specified by the copiers or senders under the data communications rules for computers or communications that are generally accepted in the relevant industry;

(iii) *Hosting.* Indemnification is possible in any of the following events (a) all of the indemnification requirements with respect to a simple conduit are met; (b) when an online service provider has the authority and power to control infringement, it does not directly obtain any monetary gains from such infringement; (c) when an online service provider becomes aware of actual infringement, or the fact or the circumstances of obvious infringement due to any requests to suspend copy and/or transmission, it immediately stops the relevant copyrighted materials from being copied or transmitted; or (d) the online service provider appoints and publicly announces the party to which a request to suspend copy and/or transmission is to be made; and

(iv) *Information searching.* Indemnification is possible in any of the following events: (a) the online service provider has yet to commence the transmission of copyrighted materials; or the indemnification requirements (b), (c) and (d) of the above subparagraph (iii) are met.

The Copyright Act was further amended on December 2, 2011 and went into effect on March 15, 2012, when the Korea-US Free Trade Agreement took effect, in order to promote the protection of rights of copyright holders and fair use of copyrighted materials by amending the relevant provisions necessary for implementing the Korea-US Free Trade Agreement, such as recognition of temporary storage as copying, introduction of a system of fair use of copyrighted materials, prohibition of acts of infringement on the rights of copyright holders including the distribution of forged labels, and the introduction of statutory damages in accordance with the agreements in the Korea-US Free Trade Agreement and to improve and supplement other issues discovered during the operation of the current system. In connection with the amendment to the Copyright Act, the Enforcement Decree and the Enforcement Rules of the Copyright Act were also amended on December 2, 2011 in accordance with the content of the Act.

The key content of the amendment to the Copyright Act on December 2, 2011 regarding online game development and services are as follows:

(1) In order to protect the rights of copyright holders in a digital environment, the amendment specifies that temporary storage falls under the scope of "copying" but allows temporary storage to be extent it is deemed necessary for smooth and efficient information processing; and

(2) An online service provider will be deemed not liable for copyright infringement: (i) if the online service provider has adopted and reasonably implemented a policy of terminating the account of a person

Table of Contents

who infringed copyrights or (ii) if the online service provider has accepted and not interfered with a right holder's use of standard technical measures for identifying and protecting copyrighted materials.

The Juvenile Protection Act

The Juvenile Protection Act, as amended on February 29, 2008, prescribes the establishment of the Juvenile Protection Commission under the authority of the Minister of the Ministry of Health and Welfare in Korea, formerly known as the Ministry for Health, Welfare and Family Affairs, or the MIHWAF, which has the authority to designate the types of media harmful to juveniles. Under the Juvenile Protection Act, any person who intends to sell, lend or distribute media materials harmful to minors or provides them for viewing or utilization is required to confirm the age of the intended user, and shall not sell, rent or distribute such materials, or provide them for viewing or utilization, to minors. A person in violation may be punished by imprisonment for a maximum of three years or by a fine not exceeding Won 20 million.

On March 4, 2009, the MIHWAF issued a public notice announcing that "Web sites for trading items" are considered "harmful mass media" to minors based on the findings of Juvenile Protection Commission that such Web sites for trading online game items are likely to encourage gambling and speculation and negatively influence juveniles. In the public notice, the MIHWAF prohibited any person under the age of 19 from visiting Web sites for trading online game items, effective from March 19, 2009.

A Web site for trading items is a Web site which offers the services of brokerage or agency for trading of tangible or intangible things gained from online games as prescribed in the Promotion Act. A Web site for trading items needs to specify on its Web site that access is not allowed for minors, and any person visiting such Web site is required to go through the adult certification process. Any Web site operator found to be operating such Web site in breach of the requirements under the public notice is subject to a maximum of 3 years of imprisonment or a maximum fine of Won 20 million. On June 3, 2009, Item Bay Co., Ltd., one of the leading Web sites in Korea for trading online game items, initiated an administrative proceeding against the MIHWAF seeking cancellation of the MIHWAF's public notice. Item Bay Co., Ltd. argued that "game items are purchased by users at their own discretion depending on their necessity, and remote from speculative activity. Therefore, Web sites for trading online game items do not fall under media harmful to minors."

While we offer virtual in-game items for sale to our users on the game Web sites that we operate in Korea, we do not broker the trade of such game items or any other tangible or intangible acquisitions obtained by using online games among our users, and currently do not fall under the category of "Web site for trading items." In Korea, however, minors account for a significant percentage of online game users. As they are now prohibited from trading items on Web sites, including virtual in-game items, such prohibition may materially and adversely affect the online game industry in general, which may well have a material adverse effect on our business, financial condition and results of operation.

The Juvenile Protection Act was partially amended on May 19, 2011 and went into effect on November 20, 2011. Under the amendment, online game providers may not provide online games to minors under the age of 16 late at night (specifically, from midnight until 6:00 a.m.) and any provider violating the provision is subject to imprisonment for no more than 2 years and a penalty not exceeding Won 10 million. As an exception, for internet games using apparatus that would not likely cause serious internet game addiction and are specified under the Presidential Decree, including smartphones, tablet PCs and consoles (except for console games that are not provided for free), the late-night restriction became effective as of May 20, 2013.

However, the amendment provides that the Minister of Gender Equality and Family, or the MOGEF, in consultation with the Minister of Culture, Sports, and Tourism, should revisit the guidelines every two years to evaluate the appropriateness of the scope of games subject to the late-night restriction and to take measures for improvement, and, with respect to minors suffering from online game addiction, the MOGEF may also provide services for prevention, consultation, treatment and rehabilitation.

Table of Contents

In this regard, the MOGEF made an administrative announcement on "the proposed public notice on the scope of games subject to the late-night restriction for internet games." According to the public notice, the applicable games are internet games provided for profit in real time via information and communication networks that fall under the games defined in the Promotion Act. Examples based on (i) the type of apparatus include games played on PCs (including laptops) and (ii) the type of games includes online PC games, internet games and PC package games. In addition, the public notice states that the games to which the above restriction is not applicable are (i) games using apparatus that would not likely cause serious internet addiction, as mentioned above, (ii) games that do not collect or use personal information and are not provided for profit, (iii) test versions of the games that are not classified pursuant to Article 21(1)(iii) of the Promotion Act and (iv) games for game contests, exhibitions, education or public advertisements that are not classified pursuant to Articles 21(1)(i) to 21(1)(ii). The effective date of the public notice is from May 20, 2013 to May 19, 2015. Therefore, the late-night restriction still remains not applicable to internet games using apparatus that would not likely cause serious internet addiction, such as smartphones, tablet PCs and consoles (except for console games that are not provided for free).

The Juvenile Protection Act was further amended on September 15, 2011 and went into effect on September 16, 2012. The key content of the amendment are as follows:

- (1) The amendment expands the category of businesses which minors are prohibited from entering, or are prohibited from hiring minors, to include those business which provide "combined distributed games" and business places which provide Internet game facilities;
- (2) The amendment requires protective measures equivalent to packaging;
- (3) The amendment requires a person who intends to sell, rent, distribute or provide any media harmful to minors to check the ages and IDs of his or her counterparties;
- (4) The amendment prescribes that if a person distributes any media harmful to minors through the information and communications network, the Minister of Gender Equality and Family may publicly post the identity of such person and the content of the violation; and
- (5) The amendment requires parental consent when a minor under age 16 joins an Internet game as a member and requires the information on the minor's use of games to be reported to the guardians.

This Juvenile Protection Act was yet further amended in part on January 17, 2012, which became effective on April 17, 2012. The key contents of the amendment are as follows:

- (1) The amendment specifies the basis of establishing Harmful Media Materials Review Subcommittee to assist the Commission on Youth Protection with the review and determination of media materials harmful to minors; and
- (2) The amendment reduces the review period for reconsideration of media materials harmful to minors from the current 60 days to 30 days considering that the review period for re-classifying movies and games is 15 days.

The subsequent amendment of the Juvenile Protection Act dated March 22, 2013, (i) added a new provision, in response to increasing business operation of various new forms such as business providing facilities for both video products and games, to further expand the category of business which minors are prohibited from entering, or are prohibited from hiring minors, by including the business providing combined media materials, based on the general consensus that such business is harmful to minors (Article 2(5)); and (ii) in order to enhance the protection of juveniles from harmful media products, clarified the scope of persons under a duty to affix a mark indicating harmfulness to juveniles, which previously had been delegated to the promulgation by the Presidential Decree, by specifying them within the Juvenile Protection Act as persons who manufacture, import, duplicate or provide games (Article 13).

Table of Contents

Japan

Japan does not currently have any national government regulations targeted specifically at the online game or mobile game industry. Some regulations that are relevant to or that may affect the online game industry are described below.

Protection of personal information

Businesses in Japan are subject to certain statutory requirements with respect to personal information acquired during the ordinary course of business. Pursuant to these statutory requirements, businesses must set up appropriate procedures to protect personal information from use for any purpose other than the intended purpose.

Regulations on sound upbringing of minors

In Japan, Internet and game software content is generally regulated at the local, rather than the national, level. Many local governments have ordinances regarding the sound upbringing of minors, which empower competent authorities to designate game software as detrimental to the sound upbringing of minors and prohibit the sale or distribution to minors of such designated game software. In addition, the Computer Entertainment Rating Organization, or CERO, a nonprofit organization, offers rating services for home-use games, including online games. Game developers may request a rating for their game software from CERO, which will then review such software and assign one of the following five ratings: "suitable for users of all ages," "suitable for users 12 years old or older," "suitable for users 15 years old or older," "suitable for users 17 years old or older," and "suitable only for users 18 years old or older." Ratings are based on, among other factors, the degree of sex, violence and anti-social expression in the game software content. Once a rating is assigned, the relevant game software must prominently display such rating.

United States

Game Ratings and Attempts to Regulate Access to Children

Most video game software publishers comply with the standardized rating system established by the Entertainment Software Rating Board, or the ESRB, a non-profit, self-regulatory body established in 1994 by the Entertainment Software Association, or the ESA. The ESRB rates video games submitted by video game publishers; the ratings include both a symbol for age appropriateness (e.g., "E" for Everyone or "M" for Mature) and a content descriptor (e.g., "Blood and Gore" or "Intense Violence"). The ESRB specifically excludes any online interactions from the rating, as the ESRB is unable to review content, such as chat, text, audio and video generated by other users in an online environment.

The ESRB has rated our games as follows: Requiem is rated "Mature," Ragnarok Online is rated "Teen," and R.O.S.E. Online and Dragon Saga are rated "Everyone 10+."

By submitting a game to the ESRB and using an ESRB rating, a video game publisher must agree to adhere to advertising and packaging guidelines for the rated game, such as using appropriate advertising content and not targeting any advertisement for a game rated "Teen," "Mature" or "Adults only" to consumers for whom the product is not rated as appropriate. The Advertising Review Board has been granted the oversight and enforcement authority for compliance with the advertising guidelines. The ESRB ratings must be displayed on both the front and back of game packaging in compliance with the ESRB requirements. The ESRB may sanction game producers for failing to label their product properly. Although submitting a game to the ESRB is voluntary, many retailers will not sell games without an ESRB rating.

The United States Federal Trade Commission, or the FTC, has also taken action with respect to improper ratings pursuant to its broad authority to prohibit fraudulent, deceptive, or unfair business practices. For example, in response to allegations that two videogame publishers failed to disclose hidden nudity and sexually-themed content to the ESRB during the ratings process, the FTC issued a consent

Table of Contents

order compelling the videogame publishers not to, expressly or implicitly, misrepresent the ratings or content descriptors of their video games and to maintain a system that ensures that all of the content in their video games is considered and reviewed in preparing submissions to the ESRB. The FTC has posted an online form on its Web site for the public to file complaints regarding video game ratings that do not accurately reflect of the content of the game, and has posted a primer for parents describing the ESRB ratings, parental controls, and other video game resources. The FTC issues periodic marketing reports to Congress and in 2009, the FTC reported that 20% of underage "undercover shoppers" were able to purchase "M" rated video games. An Undercover survey in 2010-11, however, showed a statistically significant improvement with only 13% of underage shoppers being able to purchase "M" rated games. That statistic remained at 13% in the 2012 undercover survey, which noted that it is more difficult for an underage consumer to buy an M-rated video game at retail than to see a violent film in the movie theater.

A number of bills have been introduced in Congress to specifically regulate the sale of video games with violent content to minors, but currently no such federal laws are in force. Several States, as well as several cities, have enacted or are considering laws that would regulate game industry content and marketing, including the rental or sale of games with violent content by or to minors.

For example, the State of Maryland has enacted a law that regulates the sale of video games with explicit sexual content to minors. The Maryland law has not been challenged in court, remains in force, and is supported by the ESA. Other States have enacted laws that require the posting of signs providing information about ESRB ratings. To date, laws that regulate the sale of video games based on content, when challenged, have been declared unconstitutional. Most prominently, the United States Supreme Court ruled in 2011 that a California law that imposed fines on retailers that sell certain violent video games to minors violated the First Amendment of the U.S. Constitution. The Court held that video games represent a form of protected expression under the First Amendment, and that California's statute, no matter how well intentioned, lacked adequate justification for the regulation of such speech. Yet, lawmakers may persist in attempting to pass regulation restricting the sale of violent video games to minors, particularly in the wake of several well-publicized incidents of mass violence. A bill proposed by Senator Rockefeller in 2013, the Violent Content Research Act, proposed the National Academy of Sciences study the relationship between real-world violence and virtual-world violence in video games in hopes that conclusive statistical and scientific data could support renewed call for legislation. President Obama also called upon the Center for Disease Control (CDC) and scientific agencies to conduct research on the causes and prevention of gun violence, including investigating the relationship between video games, media images, and violence, though Congress has not yet approved funding for the research.

Irrespective of any laws or industry guidelines, U.S. retailers have become more reluctant to sell "M" rated video games to minors. Consumer advocacy groups have also opposed sales of interactive entertainment software containing graphic violence, profanity or sexually explicit material by engaging in public demonstrations and media campaigns.

Online Collection of Information from Children

The Children's Online Privacy Protection Act of 1998 ("COPPA") governs the online collection of personal information from children under 13. In 2012, the FTC revised its Rule implementing COPPA to, among other things, expand the definition of personal information. COPPA and its implementing regulation prohibit any Web site operator from collecting, maintaining or using personal information (including first and last name, home address, email address, telephone number, Social Security number, image or likeness, mobile device identifier or other persistent identifier which would permit the physical or online contacting of a specific individual) of children under 13 years of age, unless the Web site operator obtains verifiable parental consent.

A Web site that knowingly collects information from children under 13 years old, or that in whole or in part is directed to children under 13 years old, must obtain verifiable parental consent before collecting personal information from any child. In 2012, the FTC clarified that this includes the passive collection of technological information, such as through cookies or mobile device IDs. Effectively, this means that

Table of Contents

websites or online services subject to COPPA must obtain verifiable parental consent before engaging in online advertising in many cases. The Web site operator must also post a clear online privacy policy that provides notice of what information is collected from children, how the information is used, and a list of third parties with whom the operator may share or sell the child's information; parents must be given the choice to determine whether the child's information can be shared with third parties, and must also be provided access to the child's information and the opportunity to delete any such information collected. Moreover, the operator must establish and maintain reasonable procedures to protect the confidentiality, security and integrity of any personal information collected from children under 13 years of age. The COPPA also prohibits conditioning a child's participation in a game on the child disclosing more personal information than is reasonably necessary to participate in such activity.

The COPPA authorizes the FTC and the State Attorneys General to bring actions against Web site operators to enforce the statute.

In 2011, the FTC released the results of a study showing that many mobile application providers do not clearly disclose the ways in which they collect and share children's information. The FTC suggests that the providers of mobile applications in the "kids app ecosystem" do more to disclose key information to parents about the types of information they collect from children, and the ways in which that information is shared with third parties.

Protection of Personal Information

Most States have some form of specific legislation regarding the protection of personal information collected, processed, maintained or used in electronic form, as well as specific notification procedures in the event that such information is accessed by unauthorized individuals. Under these laws, among other things, businesses are required to implement and maintain reasonable security measures designed to protect the computerized personal information of its customers or users from unauthorized access, disclosure or use. These measures may require the encryption of sensitive data, such as credit card numbers, social security numbers, bank security access codes, etc. In the event that a business suffers a security breach, these laws generally require the business to provide notice of such breach to each individual user affected by the breach, and in some circumstances, to the State Attorney General, the FTC, or other state or federal agencies. In addition, if such personal information is accessed by unauthorized individuals as a result of the business' failure to use reasonable measures to protect the information, the business may be liable to those customers for any misuse of such personal information and may be liable for statutory fines or penalties, as well as civil and even potential criminal prosecution by government authorities.

Privacy Policy Requirements

The FTC and many States require an operator of a Web site or online service that collects personal information from users to develop, maintain and post on its Web site a privacy policy that informs its customers and users of the categories of personal information that are collected by the operator, how that personal information is used and shared with third parties and how users may change or update such information and opt out of its collection and use. While most States have generally not imposed statutory fines or penalties on an operator for failing to comply with its privacy policy, an operator may be directly liable to its customer or users if it fails to comply with its posted privacy policy if such noncompliance harms the users. The FTC, however, has initiated numerous investigations and imposed significant civil penalties in several cases involving alleged failures by companies to comply with the representations made in their online privacy policies and/or adequately disclose the companies' actual practices in such policies. In 2011, for instance, Google entered into a settlement agreement with the FTC in which Google agreed to be subject to twenty years of privacy audits and to revise its privacy practices in response to FTC charges that Google used deceptive tactics and violated its own privacy policy when it launched its social network, Google Buzz, in 2010. The Google settlement comes amidst increasing pressure from the FTC on online service providers to conspicuously and accurately disclose their user data collection and disclosure practices. This is especially true in the mobile context, where new technologies have presented novel

Table of Contents

consumer privacy questions. Specifically, the collection and use of mobile geolocation and device identifier data have come under increased FTC scrutiny in the past year. Similarly, the California Attorney General has explicitly stated that mobile device applications must comply with the state privacy disclosure regulations and has initiated enforcement against mobile apps which failed to post a privacy policy.

In February 2013, the FTC released a Staff Report on mobile privacy disclosures which recommends that mobile app developers post a privacy policy accessible through the app or the app store, provide just-in-time disclosures and obtain affirmative express consent when collecting sensitive information such as children's data. The FTC Report also encourages mobile app developers to consider participating in self-regulatory programs, trade associations and industry organizations which may provide guidance on short-form privacy disclosures. The FTC has increased its scrutiny of mobile platforms and mobile apps and brought several consent decrees against app developers in 2011, 2012, and 2013 relating to misleading privacy disclosures, the over-collection of data from a user's mobile device, and the collection of information from children under 13 in violation of COPPA.

In 2013, the California Attorney General issued guidance for mobile app developers which recommends, among other things, that app developers use enhanced measures or special notices, to alert users to unexpected data use cases.

Liability Arising from User Speech and Conduct

Section 230 of the Communications Decency Act of 1996, or the CDA, provides limited protection to interactive computer services, such as an online game service, from liability for publishing information posted or provided by others, such as the users of an online game service. The CDA can, for example, help protect an online game service provider from liability as a publisher that could otherwise arise from a user making defamatory statements on the service about another user. Section 230 has also been used to protect intermediaries against claims of negligent misrepresentation, interference with business expectancy, breach of contract, intentional nuisance, violations of federal civil rights, and emotional distress. The protections of the CDA, however, do not immunize interactive computer services from criminal liability under United States Federal law (e.g., obscenity or child pornography), for infringement of intellectual property law, or any state laws that are not inconsistent with the CDA.

Some commentators consider Section 230 of the CDA controversial and have called for it to be amended by Congress because a number of courts have interpreted it as granting broad tort immunity. One recent case rejected immunity by holding that claims involving a person's personal information is a violation of such persons' publicity rights, which the court held were intellectual property rights outside of the scope of immunity. Another court recently held that an interactive computer service was not immune from federal Fair Housing Act violations because the interactive computer service provided tools such as pull down menus that assisted the users in creating the content that violated the Fair Housing Act. State law proposals have sought to limit the protections offered by the CDA by introducing legislation to carve out protection in cases of violations of state criminal law or child prostitution. Thus far, no such law has been enacted or upheld.

Congress or the courts could continue to narrow the application of Section 230 of the CDA, in which case online game service operators, such as the Company, could face increased potential liability for certain speech or conduct by the users on their online game service.

Table of Contents

ITEM 4.C. ORGANIZATIONAL STRUCTURE

The following is our organizational structure as of March 31, 2014:

Note:

- (1) Gravity Middle East & Africa FZ-LLC went into liquidation proceedings in the United Arab Emirates in September 2008.

ITEM 4.D. PROPERTY, PLANTS AND EQUIPMENT

As of December 31, 2013, our property and equipment mainly consisted of (i) game engines, (ii) network servers, (iii) PCs and (iv) software purchased externally. As of December 31, 2013, the net book value of our property and equipment was Won 2,315 million (US\$2,194 thousand). Because our main business is to develop and distribute online and mobile game services, we do not own any factories.

Korea

Our principal executive and administrative offices are located at 15F, 396 World Cup buk-ro, Mapo-gu, Seoul 121-795, Korea. We currently occupy 105,670 square feet of office space, which we lease from Korea Software Industry Promotion Agency, pursuant to a lease that will expire on December 31, 2014 and which is renewable for one additional year. The annual lease payment amounts to Won 2,054 million (US\$1,946 thousand). The offices of NeoCyon, our 96.11% owned subsidiary, are located at 14F, 396 World Cup buk-ro, Mapo-gu, Seoul 121-795, Korea. NeoCyon currently occupies 9,980 square feet of office space, subleased from us. The annual lease payment amounts to Won 194 million (US\$184 thousand). We believe that the existing facilities of Gravity and NeoCyon are adequate for our current requirements and that additional space can be obtained on commercially reasonable terms to meet our future requirements.

United States

The offices of Gravity Interactive, our wholly-owned subsidiary in the United States, are located at 7001 Village Drive, Suite 150, Buena Park, California 90621. Gravity Interactive currently occupies 5,838 square feet of office space, leased from a third party. The annual lease payment amounts to US\$119 thousand. We believe that the existing facilities of Gravity Interactive are adequate for their current requirements and that additional space can be obtained on commercially reasonable terms to meet their future requirements.

ITEM 4A. UNRESOLVED STAFF COMMENTS

Not applicable.

Table of Contents**ITEM 5. OPERATING AND FINANCIAL REVIEW AND PROSPECTS**

You should read the following discussion together with our consolidated financial statements and the related notes which appear elsewhere in this annual report. The following discussion is based on our consolidated financial statements, which have been prepared in accordance with U.S. GAAP. Our historic performance may not be indicative of our future results of operations and capital requirements and resources.

ITEM 5.A. OPERATING RESULTS**OVERVIEW**

We are a leading developer and distributor of online games in Japan and Thailand based on the number of peak concurrent users. Our headquarters is in Korea, and we are incorporated under the laws of Korea. Our revenues have been and continue to be driven primarily by our first game, Ragnarok Online, which was commercially launched in August 2002. Our future growth and profitability will be determined by our ability to enhance the features on our existing games and introduce new games with characters, features and functions that gain market acceptance and following.

In 2013, our revenues decreased by 17.5% to Won 47,685 million (US\$45,188 thousand) from Won 57,781 million in 2012. In 2012, our revenues increased by 0.5% to Won 57,781 million from Won 57,477 million in 2011. We recorded a net loss attributable to parent company of Won 18,588 million (US\$17,614 thousand) in 2013 as compared to a net loss attributable to parent company of Won 12,224 million in 2012 and a net income attributable to parent company of Won 14,928 million in 2011. Our gross profit margin decreased to 25.8% in 2013 from 39.6% in 2012 and 57.8% in 2011. Our operating margin was negative 35.1% in 2013 due to an operating loss of Won 16,730 million (US\$15,855 thousand) in 2013 as compared to a negative operating margin of 32.0% in 2012 and versus a positive operating margin of 5.5% in 2011. The decrease in revenues in 2013 was primarily due to: (i) decreased royalties and license fees from Ragnarok Online in Japan; (ii) decrease in revenues from Finding Neverland Online in Korea; and (iii) decreased revenues from Ragnarok Odyssey. The decrease in revenues in 2013 was partially offset by increased revenues from mobiles games and applications, revenues from Ragnarok Online II, which was launched in Singapore, Malaysia, the United States, Canada, Indonesia, Thailand and 53 other countries and markets during 2013, and revenues from Ragnarok Online in China where the game was relaunched in February 2013. Our cost of revenues for 2013 increased as compared to 2012 mainly due to increased commissions paid related to services provided to third parties. Our operating expenses for 2013 decreased as compared to 2012 mostly due to decreased impairment losses on intangible assets and goodwill, advertising expenses and R&D expenses. Our revenue trend will continue to be materially affected in the future by the popularity of online and mobile games introduced by our competitors.

Our corporate income tax rate in 2013 was 22%.

Revenues

We derive, and expect to continue to generate, most of our revenues from online game subscription revenue generated in the countries and markets where our games are offered by us, royalties and license fees paid by our licensees in our overseas markets, and mobile games and applications revenue. Our revenues can be classified into the following four categories:

online games subscription revenue;

online games royalties and license fees;

mobile games and applications; and

character merchandising, animation and other revenue.

Table of Contents

Online games subscription revenue

Subscription revenue consists of revenues from (i) micro-transactions, (ii) subscription fees from Internet cafés and (iii) premium services for individual PC users. Micro-transaction fees for consumable in-game items are deferred when such in-game items are purchased by users and recognized as revenue when the purchased in-game items are used in the games while those for permanent in-game items are recognized ratably as revenues over the estimated life cycle of such in-game items. Micro-transaction fees for in-game items with limited time period are deferred and recognized as revenue in proportion to the number of days lapsed. All online game subscription fees and premium service fees are prepaid. Prepaid subscription fees from Internet cafés are deferred and recognized as revenue on a monthly basis based on actual hours used. Prepaid premium service fees from individual PC users are deferred and recognized as revenue on a monthly basis in proportion to the number of days lapsed.

Online games royalties and license fees

We license the right to market and distribute our games in various countries for a license fee and receive monthly royalties based on an agreed percentage of the licensees' revenues from our games. For a table setting forth details of each license agreement of our principal product, Ragnarok Online, see ITEM 4.B. "BUSINESS OVERVIEW OUR MARKETS Overseas markets."

The initial license fees are deferred and recognized ratably as revenue over the license period, which generally does not exceed three years. If license agreements are renewed upon expiration of their terms, we generally receive renewal license fees, which are deferred and recognized ratably over the new license period. The guaranteed minimum royalty payments are deferred and recognized as the relevant royalty is earned.

We also receive royalty revenues from our licensees based on an agreed percentage of each of the licensees' revenues from our games. Royalty revenues are recognized on a monthly basis after the licensee confirms its revenues based on the licensee's sales from our games during the month. Our licensees' sales consist of revenues from subscription fees and micro-transactions, except in Russia and CIS countries, France and 27 other countries in Europe, Indonesia and Brazil where our game services are only offered with the micro-transaction model. We generally are advised by each of our licensees as to the amount of royalties earned by us from such licensee within 15 to 25 days following the end of each month and we generally receive payments of the royalties within 20 to 30 days following the end of each month.

Mobile games and applications revenue

Mobile games and applications revenue consists of (i) revenues from micro-transactions and a proportion of the per-download fees that users pay in cases where we directly provide mobile games services to users, such as in Korea; (ii) license fees and guaranteed minimum royalty payments, and royalty revenues from our licensees to which we license the right to market and distribute our mobile games in overseas countries; (iii) contract prices, which are related to various development services and products provided by us to third parties, such as developing games embedded in mobile phones, mobile applications, and sound for mobile phones and appliances; (iv) revenues from mobile games operation service for third parties; and (v) intellectual property royalty revenues from third parties that develop and provide services for mobile games based on our original intellectual property.

Micro-transaction fees are deferred when in-game items are purchased by users and recognized as revenue when the purchased in-game items are used in the game. Per-download fees are recognized on a monthly basis as they are earned. License fees are deferred and recognized ratably as revenue over the license period and guaranteed minimum royalty payments are deferred and recognized as the relevant royalty is earned. Royalty revenues are based on an agreed percentage of each of the licensees' revenues based on the licensee's sales from our mobile games and recognized on a monthly basis. Revenues of contract prices for certain mobile applications are recognized by measuring progress-to-completion under the percentage-of-completion method. If we do not have a sufficient basis to measure progress towards completion, revenues are recognized when we receive final acceptance from the customer that the services

Table of Contents

have been completed. Other contract prices are recognized when the products or services have been delivered or rendered and the customers can begin use in accordance with the contractual terms. Revenues from mobile games operation service are based on an agreed percentage of each of the licensors' revenues based on the licensor's sales from the mobile games we operate on their behalf and recognized on a monthly basis after the licensor confirms its revenues based on the licensor's sales from the relevant mobile games during the month. Intellectual property royalty revenues are recognized on a monthly basis.

We generally are advised by each of our licensees or licensors as to the amount of royalty revenues, revenues from mobile games operation service and intellectual property royalty revenues earned by us from such licensee or licensor within 15 to 60 days following the end of each month and we generally receive payments of the royalties within 45 to 90 days following the end of each month.

Character merchandising, animation and other revenue

Character merchandising, animation and other revenue consist of revenues from sales of console games, game character merchandising, animation and other services, including sales of goods related to mobile phones and Web site development and operation services for third parties.

Revenues from sales of console games are derived from a specified percentage of the publisher's sales after deductibles, including payments to the platform holder and others, and recognized on a quarterly basis as they are earned by the publisher. Royalty payments from game character merchandising are recognized on a quarterly basis as they are earned by the licensee. Contract prices for our services provided to third parties are recognized when the products or services have been delivered or rendered and the customers can begin their use in accordance with the contractual terms.

The following table sets forth a breakdown of revenues by type of revenue and the percentage of total revenue for the periods indicated:

| Revenue Type | Year Ended December 31, | | | | | | | |
|---|--|---------------|-----------------|---------------|-----------------|---------------|---------------------|--|
| | 2011 | | 2012 | | 2013 | | 2013 ⁽¹⁾ | |
| | (In millions of Won and thousands of US\$, except percentages) | | | | | | | |
| Online games subscription revenue | ₩ 11,556 | 20.1% | ₩ 10,150 | 17.6% | ₩ 8,206 | 17.2% | US\$ 7,776 | |
| Online games royalties and license fees | 35,552 | 61.9 | 32,325 | 55.9 | 21,726 | 45.6 | 20,588 | |
| Mobile games and applications ⁽²⁾ | 6,609 | 11.5 | 8,262 | 14.3 | 14,504 | 30.4 | 13,745 | |
| Character merchandising, animation and other revenue ⁽²⁾ | 3,760 | 6.5 | 7,044 | 12.2 | 3,249 | 6.8 | 3,079 | |
| Total | ₩ 57,477 | 100.0% | ₩ 57,781 | 100.0% | ₩ 47,685 | 100.0% | US\$ 45,188 | |

Notes:

- (1) For convenience only, the Won amounts are expressed in U.S. dollars at the rate of Won 1,055.25 to US\$1.00, the noon buying rate in effect on December 31, 2013 as certified by the Federal Reserve Bank of New York for customs purposes.
- (2) We reclassified certain revenue within Mobile games and applications revenue as Character merchandising, animation and other revenue in 2013 as this better represents the nature of the revenue. The same reclassification has been made to all prior periods to conform to the presentation of 2013. The reclassification has no effect on the Company's previously reported total net revenue and other line items on the consolidated financial statements.

Cost of revenues

Our cost of revenues consists principally of the following:

operational expenses, server depreciation expenses, server maintenance costs and related personnel costs, outsourcing fees related to developing updates to games currently commercially offered and

Table of Contents

amortization of development-related costs as described in ITEM 5.A. "OPERATING RESULTS CRITICAL ACCOUNTING POLICIES Capitalized software development costs";

royalty payments to the third parties that are developers of some of the games we offer as a service distributor based on license agreements; and

royalty payments to Mr. Myoung-Jin Lee for the right to use the storyline and characters from his "Ragnarok" cartoon series used in our games and other products based on Ragnarok. We paid Mr. Lee an initial license fee of Won 40 million and are required to pay royalties based on 1.0% or 1.5% of adjusted revenues (net of value-added taxes and certain other expenses) or 2.5%, 5% or 10% of net income generated from the use of the Ragnarok brand, depending on the type of revenues received from the operation or licensing of Ragnarok Online.

The cost of revenues from the payments to Mr. Myoung-Jin Lee was Won 284 million (US\$269 thousand) for 2013 and Won 388 million for 2012. This agreement expires in January 2033.

Selling, general and administrative expenses

Selling, general and administrative expenses consist of sales commissions paid to independent promotional agents that distribute our online games to our Internet café subscribers in Korea, commissions paid to payment settlement providers, administrative expenses and related personnel expenses of executive and administrative staff, and marketing and promotional expenses and related personnel expenses.

Research and development expenses

Research and development expenses consist primarily of payroll and other overhead expenses which are all expensed as incurred (i) until technological feasibility of an online game is reached or (ii) until commercial operation of a mobile game commences. Once technological feasibility of an online game is reached, these costs are capitalized and, once commercial operation commences, amortized as cost of revenues. See ITEM 5.A. "OPERATING RESULTS CRITICAL ACCOUNTING POLICIES Capitalized software development costs."

Foreign currency effects

In 2013, 67.5% of our revenues were denominated in foreign currencies, primarily in U.S. dollar and Japanese Yen.

In most of the countries in which our games are distributed, the revenues generated by our overseas subsidiaries and licensees are denominated in local currencies, which include Japanese Yen, Euro, NT dollar, Thai Baht and Chinese Yuan. The revenues from those countries, other than the United States, Japan and European countries, are converted into the U.S. dollar for remittance of monthly royalty payments to us. Depreciation of these local currencies against the U.S. dollar will result in reduced monthly royalty payments in U.S. dollar terms, thereby having a negative impact on our net income.

Although we receive our monthly royalty revenues from our overseas licensees in foreign currencies, primarily in Japanese Yen and U.S. dollar, and other local currencies, such as NT dollar and Chinese Yuan in our other principal markets, substantially all of our costs are denominated in Won. We receive monthly royalty payments from our overseas licensees based on an agreed percentage of revenues confirmed and recorded at the end of each month applying the foreign exchange rate applicable on such date. We generally receive these royalty payments 20 to 30 days after the end of each month unless delayed due to extraordinary circumstances. Appreciation or depreciation of the Won against these foreign currencies during this period will result in foreign currency losses or gains and affect our net income.

As of December 31, 2013, 2012 and 2011, we had no foreign currency forward contract outstanding. See ITEM 11. "QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK Foreign currency risk."

Table of Contents

Income tax expenses

See ITEM 3.D. "RISK FACTORS RISKS RELATING TO OUR BUSINESS Adverse changes in the withholding tax rates in the countries from which we receive license fees and royalties could adversely affect our net income." and ITEM 5.A. "OPERATING RESULTS CRITICAL ACCOUNTING POLICIES Income taxes."

CRITICAL ACCOUNTING POLICIES

Our discussion and analysis of our financial condition and results of operations are based upon our financial statements, which have been prepared in accordance with U.S. GAAP. The preparation of these financial statements requires us to make estimates, judgments and assumptions that affect the reported amounts of assets and liabilities, contingent liabilities, and revenue and expenses during the reporting period. We evaluate our estimates on an ongoing basis based on historical experience and other assumptions we believe are reasonable under the circumstances, the results of which form the basis for making judgments about the carrying values of assets and liabilities that are not readily apparent from other sources. The policies discussed below are considered by our management to be critical because they are not only important to the portrayal of our financial condition and results of operations but also because application and interpretation of these policies require both judgment and estimates of matters that are inherently uncertain and unknown. As a result, actual results may differ materially from our estimates.

Revenue recognition

We derive, and expect to continue to generate, most of our revenues from online game subscription revenue generated in the countries where our games are offered by us, royalties and license fees paid by our licensees in overseas markets, and mobile games and applications revenue. Our revenues can be classified into the following four categories: (i) online games subscription revenue; (ii) online games royalties and license fees; (iii) mobile games and applications; and (iv) character merchandising, animation and other revenue. For details, see ITEM 5.A. "OPERATING RESULTS OVERVIEW Revenues."

We recognize revenue in accordance with U.S. GAAP, as set forth in Accounting Standard Codification, or ASC 605, *Revenue Recognition* and other related pronouncements.

Allowances for doubtful accounts

We maintain allowances for doubtful accounts receivable for estimated losses that result from the inability of our customers to make the required payments. We base our allowances on the likelihood of recoverability of accounts receivable based on past experience and current collection trends. We record allowances for doubtful accounts based on historical payment patterns of our customers and increase our allowances as the length of time such receivables become past due increases.

Subsequent to June 2003, pursuant to agreements with various payment processing service providers, the providers are responsible for remitting to us the full subscription revenues generated in Korea after deducting their fixed service fees and charges of approximately 1.4% to 15%. In addition, we do not assume any collection risk since payment processing service providers now bear the risk of loss and delinquency.

Capitalized software development costs

We account for capitalized software development costs in accordance with ASC 985, *Costs of Software to be Sold, Leased, or Marketed*. Software development costs incurred prior to the establishment of technological feasibility are expensed when incurred and treated as research and development expenses. Once the game has reached technological feasibility, all subsequent software development costs for that product are capitalized until it is available for general release to customers. Technological feasibility is evaluated on a product-by-product basis, but generally occurs once the online game has a proven ability to operate on a multiplayer level for a large number of users. After the game is available for general release to customers, the capitalized product development costs are amortized and expensed over the game's

Table of Contents

estimated useful life. We continually evaluate the reasonableness of the economic life of the capitalized software development costs based on the average life cycle of the games whenever each new game is commercially launched or acquired. Further, when the fair value of an intangible asset is measured by income to be derived from such intangible asset, we consider amortizing such intangible asset following a schedule of when the expected benefits will be consumed or otherwise used up. This expense is recorded as a component of cost of revenues.

We evaluate the recoverability of capitalized software development costs on a product-by-product basis. Capitalized costs for those products whose further development or sale is terminated are expensed in the period at which cancellation of the development or sale of such products occurs. In addition, a charge to operating expenses is recorded when management's forecast for a particular game indicates that unamortized capitalized costs exceed the net realizable value of that asset.

Significant management judgment is required to assess the timing of technological feasibility as well as the ongoing recoverability of capitalized costs.

Impairment of goodwill and other intangible assets

Goodwill represents the excess of the purchase price over the fair value of the identifiable net assets acquired in a business combination. As of December 31, 2013, the carrying value of goodwill for each reporting unit, NeoCyon and Gravity Games, are Won 1,210 million (US\$1,147 thousand) and nil, respectively.

Goodwill is accounted for under ASC 350, *Intangibles - Goodwill and Other*, which requires that goodwill and indefinite-lived intangible assets are not amortized, but instead be tested at least annually for impairment, and more frequently if an event occurs or circumstances change which would more likely than not reduce the fair value of these assets below their carrying amount. Such an event would include unfavorable variances from established business plans, significant changes in forecasted results or volatility inherent to external markets and industries, which are periodically reviewed by our management. Specifically, qualitative factors are assessed to determine whether it is more likely than not that the fair value of a reporting unit is less than its carrying amount, including goodwill. In evaluating whether it is more likely than not that the fair value of a reporting unit is less than its carrying amount, the relevant events and circumstances are assessed. If, after assessing the totality of events or circumstances, it is determined that it is not more likely than not that the fair value of a reporting unit is less than its carrying amount, then a two-step process of the goodwill impairment test is not performed.

If it is determined that it is more likely than not that the fair value of a reporting unit is less than its carrying amount, then the first step of the two-step goodwill impairment test is performed. The first step of the goodwill impairment test is used to identify potential impairment by comparing the fair value of a reporting unit with its carrying amount, including goodwill. If the carrying amount of a reporting unit exceeds its fair value, the second step of the goodwill impairment test is performed to measure the amount of impairment loss, if any. The second step of the goodwill impairment test compares the implied fair value of the reporting unit's goodwill with the carrying amount of that goodwill. If the carrying amount of the reporting unit's goodwill exceeds the implied fair value of that goodwill, an impairment loss is recognized immediately in an amount equal to that excess. The goodwill impairment test is carried out at the reporting unit, which is either an operating division or a subdivision, for which stand-alone financial information is available to the management personnel of such division or subdivision for evaluating operating results.

We performed our annual impairment test for goodwill at all of our reporting units using data as of December 31, 2013. In performing the valuations, we used cash flows, which reflected management's forecasts and discount rates which reflect the risks associated with the current market. Prior to performing the two-step impairment test for goodwill, we performed a qualitative assessment for the reporting units NeoCyon and Gravity Games.

In 2013, we performed the annual impairment test for goodwill for NeoCyon and the fair value of the business reporting unit NeoCyon was determined to be greater than its book value. Therefore, we

Table of Contents

concluded not to recognize impairment loss for NeoCyon. In performing the annual impairment test for goodwill for Gravity Games, the fair value of the business reporting unit Gravity Games was determined to be lower than its book value. Therefore, during the fiscal year ended December 31, 2013, we recorded impairment losses of Won 2,653 million (US\$2,514 thousand) in reporting unit of Gravity Games due to the overall decline in the fair value of the reporting unit and uncertainty in the future. The fair value of the reporting unit was estimated principally using the expected present value of the future cash flows.

Product technology, presented as an acquired intangible asset in balance sheets, represents product technology related to Dragonica which was recognized as a result of a business combination with Gravity Games in 2010. As of December 31, 2013, the carrying value of product technology is nil.

Product technology is accounted for under ASC 350, *Intangibles - Goodwill and Other*, which requires that intangible assets subject to amortization shall be reviewed for impairment whenever events or changes in circumstances indicate that the carrying amount of the asset or asset group may not be recoverable in accordance with ASC 360, *Property, Plant and Equipment*. An impairment loss shall be recognized if the carrying amount of an intangible asset is not recoverable and its carrying amount exceeds its fair value. The carrying value is considered unrecoverable if it exceeds the sum of the undiscounted cash flows anticipated from the use and eventual disposition of the asset. Impairment loss is measured as the amount by which the carrying value of an asset exceeds its fair value.

As a significant decrease in revenue of Dragonica was noted in 2013, which was a trigger event for long-lived assets impairment analysis as of December 31, 2013, we performed an impairment test on Dragonica. As the carrying amount of Dragonica exceeded the sum of the estimated undiscounted future cash flows from the use, we recognized an impairment loss of Won 1,424 million (US\$1,349 thousand) for Dragonica.

The assessment of impairments under ASC 350 and ASC 360 requires significant judgment and requires estimates to assess fair values. We believe that the estimates of future cash flows and fair value used in the impairment tests of goodwill and product technology are reasonable. However, in the future, changes in estimates resulting in lower than currently anticipated cash flows and fair value due to unforeseen changes in business assumptions could negatively affect the valuations, which may result in us recognizing impairment charges for goodwill and other intangible assets in the future.

Income taxes

We account for income taxes under the provisions of ASC 740, *Income Taxes*. Under ASC 740, income taxes are accounted for under the asset and liability method.

Management judgment is required in determining our provision for income taxes, deferred tax assets and liabilities, and the extent to which deferred tax assets can be realized. A valuation allowance is provided for deferred tax assets to the extent that it is more likely than not that such deferred tax assets will not be realized. Realization of future tax benefits related to the deferred tax assets is dependent on many factors, including our ability to generate taxable income within the period during which the temporary differences reverse, the outlook for the economic environment in which the business operates and the overall future industry outlook.

We have significant deferred income tax assets, including tax credits, that may be used to offset taxable income in future periods. Our ability to utilize deferred income tax assets is dependent on our ability to generate future taxable income sufficient to utilize these tax credits before their expiration. Changes in estimates of our ability to realize our deferred tax assets are generally recognized in earnings as a component of our income tax (benefit) expense. At each reporting date, we review our deferred tax assets for recoverability considering historical profitability, projected future taxable income, the expected timing of reversals of existing temporary differences and expiration of tax credits. If we are unable to generate sufficient future taxable income, the deferred tax assets are reduced to the extent that it is more likely than not that the related tax expense will be recorded. A decrease in deferred tax assets would result in an increase in our effective tax rate and may materially adversely impact our operating results. Conversely, if

Table of Contents

conditions improve and we determine that deferred tax assets should be increased because of changes in estimates in future taxable income or other conditions that affect our expected recovery of deferred tax assets, this would result in an increase in reported earnings in such period.

Based on the assessments that we have conducted during 2012 and 2013, which took into account our projected future taxable income, we concluded that it was more likely than not that portions of the deferred tax assets of Gravity and all of the deferred tax assets of NeoCyon as of December 31, 2012 and 2013, which mainly consist of tax credits in Korea, would be realized.

Deferred income taxes as of December 31, 2013 were calculated based on the rate of 22% for fiscal year 2013 and thereafter for the amounts expected to be realized during the relevant fiscal year.

Recent accounting pronouncements

In December 2011 and January 2013, the Financial Accounting Standards Board, or FASB issued FASB Accounting Standards Update, or ASU, No. 2011-11, *Disclosures about Offsetting Assets and Liabilities*, and ASU 2013-01, *Clarifying the Scope of Disclosures about Offsetting Assets and Liabilities*, respectively, which create new disclosure requirements about the nature of an entity's rights of offset and related arrangements associated with its financial instruments and derivative instruments. The disclosure requirements are effective for annual reporting periods beginning on or after January 1, 2013, and interim periods therein, with retrospective application required. The new disclosures are designed to make financial statements that are prepared under U.S. GAAP more comparable to those prepared under International Financial Reporting Standards, or IFRS. The adoptions of ASU 2011-11 and 2013-01 did not have a material impact on the Company's consolidated financial statements.

In July 2012, the FASB issued ASU 2012-02, *Testing Indefinite-Lived Intangible Assets for Impairment* as an update to the authoritative guidance related to testing indefinite-lived intangible assets for impairment. This update gives an entity the option to first consider certain qualitative factors to determine whether the existence of events and circumstances indicates that it is more likely than not that the fair value of an indefinite-lived intangible asset is less than its carrying amount as a basis for determining whether it is necessary to perform the quantitative impairment test. This update is effective for the indefinite-lived intangible asset impairment test performed for fiscal years beginning after September 15, 2012 with early adoption permitted. The Company has early adopted this ASU and the adoption had no material impact on the Company's consolidated financial statements.

In February 2013, the FASB issued ASU 2013-02, *Reporting of Amounts Reclassified Out of Accumulated Other Comprehensive Income* to require new disclosures about reclassifications from accumulated other comprehensive income to net income. These disclosures may be presented on the face of the statements or in the notes to the consolidated financial statements. The standards update is effective for fiscal years beginning after December 15, 2012 with early adoption permitted. The Company adopted the provisions of ASU 2013-02 in the year ended December 31, 2013 and has presented its requirements in the consolidated statements of comprehensive income (loss).

In March 2013, the FASB issued ASU 2013-05, *Foreign Currency Matters*, to clarify the accounting for the release of a cumulative translation adjustment into net income when a parent either sells a part or all of its investment in a foreign entity or no longer holds a controlling financial interest in a subsidiary or group of assets that is a nonprofit activity or a business within a foreign entity. The new standard is effective for fiscal years, and interim periods within those fiscal years, beginning on or after December 15, 2013. The Company does not anticipate that this adoption will have a significant impact on its financial position, results of operations, or cash flows.

In July 2013, the FASB issued ASU 2013-11, *Income Taxes*, which requires the presentation of certain unrecognized tax benefits as reductions to deferred tax assets rather than as liabilities in the Consolidated Balance Sheets when a net operating loss carryforward, a similar tax loss, or a tax credit carryforward exists. The new standard requires adoption on a prospective basis in the first quarter of 2015; however, early adoption is permitted. The Company adopted the provisions of ASU 2013-02 in the year ended December 31, 2013, and has presented its requirements in the consolidated statements of comprehensive income (loss).

Table of Contents**RESULTS OF OPERATIONS: 2013 COMPARED TO 2012**

The following table summarizes our results of operations for the periods indicated:

| | Year Ended December 31, | | | |
|---|-------------------------|-------------------|----------------------|---------------|
| | 2012 | 2013 | 2013 ⁽¹⁾ | % Change |
| (In millions of Won and thousands of US\$, except percentages) | | | | |
| Revenues⁽²⁾: | | | | |
| Online games subscription revenue | ₩ 10,150 | ₩ 8,206 | US\$ 7,776 | (19.2)% |
| Online games royalties and license fees | 32,325 | 21,726 | 20,588 | (32.8) |
| Mobile games and applications ⁽³⁾ | 8,262 | 14,504 | 13,745 | 75.6 |
| Character merchandising, animation and other revenue ⁽³⁾ | 7,044 | 3,249 | 3,079 | (53.9) |
| Total net revenue | 57,781 | 47,685 | 45,188 | (17.5) |
| Cost of revenue | 34,906 | 35,399 | 33,545 | 1.4 |
| Gross profit | 22,875 | 12,286 | 11,643 | (46.3) |
| Gross profit margin⁽⁴⁾ | 39.6% | 25.8% | 25.8% | |
| Operating expenses: | | | | |
| Selling, general and administrative expenses | 20,310 | 17,063 | 16,171 | (16.0) |
| Research and development | 7,018 | 6,131 | 5,810 | (12.6) |
| Impairment loss on intangible assets | 14,569 | 5,822 | 5,517 | (60.0) |
| Gain on disposal of equity method investments | (528) | | | N/M |
| Total operating expenses | 41,369 | 29,016 | 27,498 | (29.9) |
| Operating loss | (18,494) | (16,730) | (15,855) | (9.5) |
| Operating profit margin⁽⁵⁾ | (32.0)% | (35.1)% | (35.1)% | |
| Other income (expenses): | | | | |
| Interest income | 1,763 | 1,334 | 1,265 | (24.3) |
| Interest expense | (55) | (41) | (39) | (25.5) |
| Foreign currency loss, net | (902) | (413) | (391) | (54.2) |
| Others, net | 65 | 1,225 | 1,161 | 1,784.6 |
| Total net other income | 871 | 2,105 | 1,996 | 141.7 |
| Loss before income tax expenses and equity loss on investments | (17,623) | (14,625) | (13,859) | (17.0) |
| Income tax expenses | 2,584 | 5,108 | 4,840 | 97.7 |
| Loss before equity loss on investments | (20,207) | (19,733) | (18,699) | (2.3) |
| Equity loss on investments, net⁽⁶⁾ | (333) | (18) | (18) | (94.6) |
| Net loss | (20,540) | (19,751) | (18,717) | (3.8) |
| Net loss attributable to: | | | | |
| Non-controlling interest ⁽⁷⁾ | (8,316) | (1,163) | (1,103) | (86.0) |
| Parent company | ₩ (12,224) | ₩ (18,588) | US\$ (17,614) | 52.1 |

Other comprehensive loss

Edgar Filing: GRAVITY Co., Ltd. - Form 20-F

| | | | | |
|---|------------|------------|---------------|---------|
| Foreign currency translation adjustment | (41) | (1,327) | (1,258) | 3,136.6 |
| Comprehensive loss | (20,581) | (21,078) | (19,975) | 2.4 |
| Comprehensive loss attributable to: | | | | |
| Non-controlling interest ⁽⁷⁾ | (8,316) | (1,163) | (1,103) | (86.0) |
| Parent company | ₩ (12,265) | ₩ (19,915) | US\$ (18,872) | 62.4% |

N/M = not meaningful

Notes:

- (1) For convenience only, the Won amounts are expressed in U.S. dollars at the rate of Won 1,055.25 to US\$1.00, the noon buying rate in effect on December 31, 2013 as certified by the Federal Reserve Bank of New York for customs purposes.
- (2) The accompanying 2013 consolidated statement of operations includes certain out-of-period adjustments primarily related to the understatement of revenues for in-game items of Won 981 million that were not properly deferred in fiscal year 2012. Management believes the impact of these items,

Table of Contents

both individually and in the aggregate, to the year ended December 31, 2013 and to prior years presented are not material.

- (3) We reclassified certain revenue within Mobile games and applications revenue as Character merchandising, animation and other revenue in 2013 as this better represents the nature of the revenue. The same reclassification has been made to all prior periods to conform to the presentation of 2013. The reclassification has no effect on the Company's previously reported total net revenue and other line items on the consolidated financial statements.
- (4) Gross profit margin for each period is calculated by dividing gross profit by total net revenue for each period.
- (5) Operating profit margin for each period is calculated by dividing operating loss by total net revenue for each period.
- (6) Represents the losses from our 25% equity interest in Gravity EU SAS, our 25% equity investment in Ingamba and our 16.39% equity investment in Online Game Revolution Fund No. 1 in 2012. Represents the loss from our 16.39% equity investment in Online Game Revolution Fund No. 1 in 2013. These investments were accounted for using the equity method of accounting.
- (7) Represents the non-controlling interest in NeoCyon, a 96.11%-held subsidiary acquired in December 2005, and Gravity Games, a subsidiary acquired in October 2010, in which our initial ownership was 50.83% and which increased to 85.5% in August 2013.

Revenues

Our total revenues decreased by 17.5% to Won 47,685 million (US\$45,188 thousand) in 2013 from Won 57,781 million in 2012, primarily due to:

a 32.8% decrease in royalties and license fees to Won 21,726 million (US\$20,588 thousand) in 2013 from Won 32,325 million in 2012, which was due mainly to decreased revenues from Ragnarok Online in Japan resulting from increasing competition and as a result of the relative maturity of such game, and the strengthening of the Korean Won by approximately 19.7% against the Japanese Yen from 2012 to 2013, though such decrease was partially offset by revenues from Ragnarok Online in China where the game was relaunched in February 2013 and revenues from Ragnarok Online II in Singapore, Malaysia, Indonesia and Thailand where the game was commercially released during 2013;

a 53.9% decrease in character merchandising, animation and other revenue to Won 3,249 million (US\$3,079 thousand) in 2013 from Won 7,044 million in 2012, which resulted primarily from decrease in revenues from Ragnarok Odyssey and revenues from sales of goods related to mobile phones in 2012, which did not occur in 2013; and

a 19.2% decrease in subscription revenue to Won 8,206 million (US\$7,776 thousand) in 2013 from Won 10,150 million in 2012, resulting primarily from decreased revenues from Finding Neverland Online, which we ceased offering in Korea in July 2013 though such decrease was partially offset by revenues from Ragnarok Online II in the United States, Canada and 53 other countries and markets resulting from the game's commercial launch in such countries and markets commencing in May 2013.

Such decreases were offset by:

a 75.6% increase in mobile games and applications revenue to Won 14,504 million (US\$13,745 thousand) in 2013 from Won 8,262 million in 2012, which was mainly driven by revenues from NeoCyon's mobile games operation service for a third party and revenues from Ragnarok Online Uprising: Valkyrie.

Table of Contents

Cost of revenues

Our cost of revenues increased by 1.4% to Won 35,399 million (US\$33,545 thousand) in 2013 from Won 34,906 million in 2012, primarily due to:

a 42.4% increase in commissions paid to Won 8,298 million (US\$7,864 thousand) in 2013 from Won 5,829 million in 2012 mostly related to our services provided to third parties and for digital storefronts where our mobile games are offered; and

a 5.5% increase in salaries to Won 12,600 million (US\$11,940 thousand) in 2013 from Won 11,939 million in 2012 primarily resulting from increases in salaries resulting from the commercial launch of some of our mobile games and increased number of mobile game developers of NeoCyon.

Such increases in cost of revenues were substantially offset by a 42.1% decrease in outsourcing fees to Won 2,095 million (US\$1,985 thousand) in 2013 from Won 3,620 million in 2012, which is mostly related to the development of Ragnarok Online, Ragnarok Online II and mobile games, and cost of goods sold associated with sales of goods related to mobile phones in 2012, which did not occur in 2013.

Gross profit and gross profit margin

As a result of the foregoing, our gross profit decreased by 46.3% to Won 12,286 million (US\$11,643 thousand) in 2013 from Won 22,875 million in 2012. Our gross profit margin decreased to 25.8% in 2013 from 39.6% in 2012.

Operating expenses

Selling, general and administrative expenses. Our selling, general and administrative expenses decreased by 16.0% to Won 17,063 million (US\$16,171 thousand) in 2013 from Won 20,310 million in 2012, primarily due to:

a 37.8% decrease in advertising expenses to Won 2,852 million (US\$2,703 thousand) in 2013 from Won 4,585 million in 2012 primarily due to marketing expenses for open beta testing and commercial launch of Finding Neverland Online and Ragnarok Online II in 2012, which did not occur in 2013, and for decreased marketing expenses for Ragnarok Online; and

a 7.7% decrease in salaries to Won 6,896 million (US\$6,535 thousand) in 2013 from Won 7,470 million in 2012 mostly attributable to a decrease in salaries for the headquarters mostly as a result of a decrease in the number of employees.

Research and development expenses. Our research and development expenses decreased by 12.6% to Won 6,131 million (US\$5,810 thousand) in 2013 from Won 7,018 million in 2012 mainly due to decreases in development expenses for East Road resulting from the discontinuation of its development in 2013. The decrease was partially offset by development expenses for Ragnarok Odyssey Ace for the PS Vita platform and increased development expenses for mobile games in 2013.

Impairment loss on intangible assets. We had Won 5,822 million (US\$5,517 thousand) in impairment losses on intangible assets in 2013, which mostly consisted of impairment losses for goodwill of Gravity games, intangible assets of Dragonica, and capitalized research and development cost of Requiem Returns W, Ragnarok Odyssey Ace for the PlayStation Vita Platform, Steal Fighter, Game Station, which is a mobile game service platform, Maestia and Ragnarok Online Guild Masters.

Operating loss and operating profit margin

As a result of the cumulative effects of the reasons stated above, we recorded an operating loss of Won 16,730 million (US\$15,855 thousand) in 2013, compared to an operating loss of Won 18,494 million in 2012, and our operating profit margin was negative 35.1% in 2013.

Table of Contents**Net other income**

Our net other income increased 141.7% to Won 2,105 million (US\$1,996 thousand) in 2013 from Won 871 million in 2012 primarily due to other income related to the liquidation of Online Game Revolution Fund No. 1 in 2013, which is mostly attributable to realization of related accumulated other comprehensive income balance.

Income tax expenses

We recorded an income tax expense of Won 5,108 million (US\$4,840 thousand) in 2013, compared to an income tax expense of Won 2,584 million in 2012, mostly due to the partial release of deferred tax assets of Gravity. In 2013, we recognized Won 2,642 million (US\$2,504 thousand) or 13% of the deferred tax assets from tax credit carry forwards, Won 1,488 million (US\$1,410 thousand) of net deferred tax assets from the other temporary differences, and Won 1,980 million (US\$1,876 thousand) of net deferred tax assets from net operating loss carry forwards. In 2012, we recognized Won 7,214 million or 34% of the deferred tax assets from tax credit carry forwards and Won 2,362 million of net deferred tax assets from the other temporary differences.

Equity loss on investments

In 2012, equity loss on investments represents the losses from the equity loss of Gravity EU SAS and Ingamba, and the loss incurred from a 16.39% partnership interest in Online Game Revolution Fund No. 1. The investments in Gravity EU SAS and Ingamba, in each of which our ownership is or was 25%, are accounted for as equity method investments. The Company could not significantly influence the operation and financial policies of Online Game Revolution Fund No. 1 under the partnership agreement; however, we accounted for the investment under the equity method of accounting in accordance with ASC 323, *Investment Equity Method and Joint Ventures*, which requires the use of equity method unless the investors' interest "is so minor that the limited partner may have virtually no influence over partnership operating and financial policies." We recorded Won 257 million, Won 25 million and Won 51 million as equity loss of Gravity EU SAS, Ingamba and the partnership of Online Game Revolution Fund No.1 in 2012, respectively. In May 2012, we sold our 25% equity interest in Ingamba to Stylonos Technologies Ltd., which resulted in Ingamba ceasing to be our affiliated company.

In 2013, equity loss on investments represents the loss incurred from a 16.39% partnership interest in Online Game Revolution Fund No. 1. We recorded Won 18 million (US\$ 18 thousand) as equity loss of the partnership of Online Game Revolution Fund No.1 in 2013. On December 31, 2010, the term of the partnership of Online Game Revolution Fund No. 1 expired and its liquidation was completed in June 2013, which resulted in Online Game Revolution Fund No.1 ceasing to be our equity method investee.

Non-controlling interest

Non-controlling interest represents the net loss from NeoCyon, our 96.11%-held subsidiary and Gravity Games, our 85.5%-held subsidiary, attributable to third-party minority interest holders. We acquired 96.11% of the voting equity of NeoCyon in 2005. We acquired 50.83% of the voting equity of Gravity Games in 2010 and increased our ownership in Gravity Games to 85.5% in August 2013.

Net loss attributable to parent company

As a result of foregoing, we recorded a net loss attributable to parent company of Won 18,588 million (US\$17,614 thousand) in 2013 compared to a net loss attributable to parent company of Won 12,224 million in 2012.

Table of Contents**RESULTS OF OPERATIONS: 2012 COMPARED TO 2011**

The following table summarizes our results of operations for the periods indicated:

| | Year Ended December 31, | | |
|---|-------------------------|------------|----------|
| | 2011 | 2012 | % Change |
| (In millions of Won, except percentages) | | | |
| Revenues: | | | |
| Online games subscription revenue | ₩ 11,556 | ₩ 10,150 | (12.2)% |
| Online games royalties and license fees | 35,552 | 32,325 | (9.1) |
| Mobile games and applications ⁽¹⁾ | 6,609 | 8,262 | 25.0 |
| Character merchandising, animation and other revenue ⁽¹⁾ | 3,760 | 7,044 | 87.3 |
| | | | |
| Total net revenue | 57,477 | 57,781 | 0.5 |
| Cost of revenue | 24,243 | 34,906 | 44.0 |
| | | | |
| Gross profit | 33,234 | 22,875 | (31.2) |
| Gross profit margin ⁽²⁾ | 57.8% | 39.6% | |
| Operating expenses: | | | |
| Selling, general and administrative expenses | 22,759 | 20,310 | (10.8) |
| Research and development | 4,136 | 7,018 | 69.7 |
| Impairment loss on intangible assets | 3,697 | 14,569 | 294.1 |
| Gain on disposal of equity method investments | | (528) | N/M |
| Gain on loss of control in a subsidiary | (548) | | N/M |
| Settlement cost of litigation | 29 | | N/M |
| | | | |
| Total operating expenses | 30,073 | 41,369 | 37.6 |
| Operating income (loss) | 3,161 | (18,494) | N/M |
| Operating profit margin ⁽³⁾ | 5.5% | (32.0)% | |
| Other income (expenses): | | | |
| Interest income | 1,844 | 1,763 | (4.4) |
| Interest expense | (58) | (55) | (5.2) |
| Foreign currency income (loss), net | 180 | (902) | N/M |
| Others, net | (90) | 65 | N/M |
| | | | |
| Total net other income | 1,876 | 871 | (53.6) |
| Income (loss) before income tax expenses (benefit) and equity loss on investments | 5,037 | (17,623) | N/M |
| Income tax expenses (benefit) | (7,962) | 2,584 | N/M |
| | | | |
| Income (loss) before equity loss on investments | 12,999 | (20,207) | N/M |
| Equity loss on investments, net ⁽⁴⁾ | (242) | (333) | 37.6 |
| | | | |
| Net income (loss) | 12,757 | (20,540) | N/M |
| Net income (loss) attributable to: | | | |
| Non-controlling interest ⁽⁵⁾ | (2,171) | (8,316) | 283.0 |
| | | | |
| Parent company | ₩ 14,928 | ₩ (12,224) | N/M |

| | | | |
|--|----------|------------|--------|
| Other comprehensive loss | | | |
| Foreign currency translation adjustment | (510) | (41) | (92.0) |
| Comprehensive income (loss) | 12,247 | (20,581) | N/M |
| Comprehensive income (loss) attributable to: | | | |
| Non-controlling interest ⁽⁵⁾ | (2,171) | (8,316) | 283.0 |
| Parent company | ₩ 14,418 | ₩ (12,265) | N/M% |

N/M = not meaningful

Notes:

- (1) We reclassified certain revenue within Mobile games and applications revenue as Character merchandising, animation and other revenue in 2013 as this better represents the nature of the revenue. The same reclassification has been made to all prior periods to conform to the presentation

Table of Contents

of 2013. The reclassification has no effect on the Company's previously reported total net revenue and other line items on the consolidated financial statements.

(2)

Gross profit margin for each period is calculated by dividing gross profit by total net revenue for each period.