

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, 2009
- OR
- TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934 For the transition period from _____ to _____
- OR
- SHELL COMPANY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934

Commission file number: 000-50476

주식회사 웹젠

(Exact name of Registrant as specified in its charter)

Webzen Inc.

(Translation of Registrant's name into English)

The Republic of Korea

(Jurisdiction of incorporation or organization)

**14th Floor, Daerung Post Tower 2nd
182-13 Guro-Dong Guro Gu
Seoul, Korea 152-790**

(Address of principal executive offices)

Hwi Joon Shin, Tel: +82 2 3498 1600, Facsimile: +82 2 2057 2568, 14th Floor, Daerung Post Tower 2nd, 182-13
Guro-Dong Guro Gu, Seoul, Korea 152-790

(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 |
|--|---|
| (1) Common shares, par value ₩500 per share ("Common Shares")* | The Nasdaq Global Market |
| (2) American Depositary Shares ("ADSs"), each of which represents three tenths of a common share | The Nasdaq Global Market |

* Not for trading, but only in connection with the registration of American Depositary Shares.

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.

The number of outstanding shares as of December 31, 2009:

| Title of Class | Number of Shares Outstanding |
|----------------|------------------------------|
| Common Shares | 10,499,658 |
| ADSs | 4,524,300 |

Indicate by check mark whether 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 Regulations 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 statement item the registrant has elected to follow.

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

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Unless the context otherwise requires, references in this annual report to:

- “Korea” or the “Republic” are to The Republic of Korea;
- “Government” are to the government of the Republic;
- “China” or the “PRC” are to the People’s Republic of China;
- “Taiwan” are to Taiwan, the Republic of China;
- “U.S.” or the “United States” are to the United States of America;
- “Webzen,” “we,” “us,” “our,” “our company” or “Company” are to Webzen Inc.;
- “Won” or “₩” are to the currency of the Republic;
- “U.S. dollars,” “\$” or “US\$” are to the currency of the United States;
- “Renminbi” or “RMB” are to the currency of China;
- “NT dollars” are to the currency of Taiwan; and
- “Yen” or “¥” are to the currency of Japan.

The consolidated financial statements of Webzen have been prepared in accordance with accounting principles generally accepted in the United States (“U.S. GAAP”). Unless otherwise stated or the context otherwise requires, all amounts in such financial statements are expressed in Won.

For your convenience, this annual report contains translations of certain Won amounts into U.S. dollars at the noon buying rate of the Federal Reserve Bank of New York for Won in effect on December 31, 2009 which was ₩1,163.65 to US\$1.00.

FORWARD-LOOKING STATEMENTS

This annual report contains statements that constitute “forward-looking statements” within the meaning of Section 21(E) of the Securities Exchange Act of 1934. When included in this annual report, the words, “will,” “should,” “expects,” “intends,” “anticipates,” “estimates” and similar expressions, among others, identify forward-looking statements. Such statements, which include, but are not limited to, statements contained in “Item 3. Key Information — 3.D. Risk Factors,” “Item 5. Operating and Financial Review and Prospects” and “Item 11. Quantitative and Qualitative Disclosure about Market Risk,” inherently are subject to a variety of risks and uncertainties that could cause actual results to differ materially from those set forth in such statements. These forward-looking statements are made only as of the date of this annual report. We expressly disclaim any obligation or undertaking to release any update or revision to any forward-looking statement contained herein to reflect any change in our expectations with regard thereto or any change in events, conditions or circumstances on which any statement is based.

[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**3.A. Selected Financial Data**

The following selected consolidated financial information has been derived from our consolidated financial statements as of each of the dates and for each of the periods indicated below. This information should be read in conjunction with and is qualified in its entirety by reference to our consolidated financial statements, including the notes thereto, included in this annual report. Our consolidated financial statements are prepared in accordance with U.S. GAAP.

| | As of and for the years ended December 31, | | | | | |
|---|--|------------|------------|-----------|----------|-------------|
| | 2005 | 2006 | 2007 | 2008 | 2009 | 2009(1) |
| | (in millions of Won and thousands of US\$, except per share data and per ADS data) | | | | | |
| | | | | | | (unaudited) |
| Statement of operations data: | | | | | | |
| Online game subscriptions | ₩ 26,830 | ₩ 21,247 | ₩ 22,884 | ₩ 22,478 | ₩ 19,833 | \$ 17,043 |
| Royalties and license fees | 4,816 | 2,811 | 6,213 | 10,298 | 10,845 | 9,320 |
| Service fees | — | — | — | — | 717 | 616 |
| Total net revenues | 31,646 | 24,058 | 29,097 | 32,776 | 31,395 | 26,979 |
| Cost of revenues | 12,815 | 15,722 | 17,505 | 15,102 | 15,634 | 13,435 |
| Gross profit | 18,831 | 8,336 | 11,592 | 17,674 | 15,761 | 13,544 |
| Selling, general and administrative expenses | 26,763 | 32,699 | 22,848 | 24,590 | 13,761 | 11,825 |
| Research and development expenses | 20,282 | 24,062 | 23,164 | 1,816 | 2,227 | 1,914 |
| Impairment charges | — | — | — | 505 | — | — |
| Operating loss | (28,214) | (48,425) | (34,420) | (9,237) | (227) | (195) |
| Interest income | 4,747 | 3,991 | 3,503 | 3,364 | 2,232 | 1,919 |
| Other income (expense) | (213) | 1,946 | 7,660 | (1,154) | 2,440 | 2,096 |
| Income (loss) before income tax expenses | | | | | | |
| (benefit) and equity in earnings (loss) of related equity investment | (23,680) | (42,488) | (23,257) | (7,027) | 4,445 | 3,820 |
| Income tax expenses (benefit) | (5,507) | 5,102 | 2,579 | 802 | 1,055 | 907 |
| Income (loss) before equity in earnings (loss) of related equity investment | (18,173) | (47,590) | (25,836) | (7,829) | 3,390 | 2,913 |
| Equity in earnings (loss) of related equity investment, net of taxes | (664) | — | — | — | — | — |
| Net income (loss) | (18,837) | (47,590) | (25,836) | (7,829) | 3,390 | 2,913 |
| Net income (loss) attributable to non-controlling interest | (33) | (525) | (242) | (154) | 81 | 69 |
| Net income (loss) attributable to parent company | ₩ (18,804) | ₩ (47,065) | ₩ (25,594) | ₩ (7,675) | ₩ 3,309 | \$ 2,844 |
| Earnings (loss) per share: | | | | | | |
| Net income (loss) attributable to parent company shareholders | | | | | | |
| Basic | ₩ (1,497) | ₩ (3,847) | ₩ (2,078) | ₩ (641) | ₩ 279 | \$ 0.24 |
| Diluted(2) | (1,497) | (3,847) | (2,078) | (641) | 278 | 0.24 |
| Earnings (loss) per ADS(3) | | | | | | |
| Basic | (449) | (1,154) | (623) | (192) | 84 | 0.07 |
| Diluted(2) | (449) | (1,154) | (623) | (192) | 83 | 0.07 |
| Dividends declared per share(4) | ₩ 250 | ₩ — | ₩ — | ₩ — | ₩ — | ₩ — |

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| | As of and for the years ended December 31, | | | | | |
|--|--|------------|------------|------------|------------|-------------|
| | 2005 | 2006 | 2007 | 2008 | 2009 | 2009(1) |
| | (in millions of Won and thousands of US\$, except per share data and per ADS data) | | | | | |
| | | | | | | (unaudited) |
| Weighted average number of shares outstanding: | | | | | | |
| Basic | 12,563,892 | 12,233,204 | 12,319,347 | 11,982,216 | 11,856,948 | 11,856,948 |
| Diluted(2) | 12,563,892 | 12,233,204 | 12,319,347 | 11,982,216 | 11,885,846 | 11,885,846 |
| Balance sheet data: | | | | | | |
| Cash and cash equivalents | ₩ 121,739 | ₩ 78,138 | ₩ 66,857 | ₩ 41,823 | ₩ 64,981 | \$ 55,842 |
| Short-term financial instruments | 2,935 | 5,211 | 8,047 | 11,523 | 1,411 | 1,212 |
| Total assets | 185,685 | 142,385 | 121,414 | 100,117 | 104,367 | 89,689 |
| Total liabilities | 17,406 | 16,691 | 22,475 | 16,929 | 16,768 | 14,410 |
| Total parent company shareholders' equity | 167,412 | 125,396 | 98,869 | 83,188 | 87,575 | 75,259 |
| Non-controlling interest | 867 | 298 | 70 | — | 24 | 20 |
| Total equity | ₩ 168,279 | ₩ 125,694 | ₩ 98,939 | ₩ 83,188 | ₩ 87,599 | \$ 75,279 |

- (1) For convenience, the Won amounts are expressed in U.S. dollars at the rate of ₩1,163.65 to US\$1.00, the noon buying rate in effect on December 31, 2009 as announced by the Federal Reserve Bank of New York. The translation is not a representation that the Won or U.S. dollar amounts referred to herein could have been or could be converted into U.S. dollars or Won, as the case may be, at any particular rate, or at all.
- (2) For further information on historical financial statement effects of stock option issuances, see note 14 to our audited financial statements as of and for the years ended December 31, 2007, 2008 and 2009.
- (3) Based on earnings per share. Each ADS represents three-tenths of a common share.
- (4) The record date for the dividend payment was December 31, 2004.

Exchange Rates

Fluctuations in the exchange rate between Won and U.S. dollars will affect the U.S. dollar equivalent of the Won price of our common shares on The Korea Exchange, Inc. ("KRX") KOSDAQ Market ("KOSDAQ") and, as a result, will likely affect the market price of our ADSs. These fluctuations will also affect the U.S. dollar conversion by the depository of cash dividends paid in Won and the Won proceeds received by the depository from any sale of our common shares represented by our ADSs.

In certain parts of this annual report, we have translated Won amounts into U.S. dollars for the convenience of investors. Unless otherwise stated, the rate we used for the translation was ₩1,163.65 to US\$1.00, which was the noon buying rate announced by the Federal Reserve Bank of New York on December 31, 2009. The translation is not a representation that the Won or U.S. dollar amounts referred to herein could have been or could be converted into U.S. dollars or Won, as the case may be, at any particular rate, or at all. The table below sets forth, for the periods indicated, information concerning the exchange rate for Won, expressed in Won per one U.S. dollar.

| Year ended December 31, | At the end | Average | High | Low |
|-------------------------|--------------------|----------|---------|---------|
| | of period | rate (1) | | |
| | (Won per US\$1.00) | | | |
| 2005 | 1,010.0 | 1,023.2 | 1,059.8 | 997.0 |
| 2006 | 930.0 | 950.1 | 1,002.9 | 913.7 |
| 2007 | 935.8 | 928.0 | 950.2 | 903.2 |
| 2008 | 1,262.0 | 1,105.8 | 1,507.9 | 935.2 |
| 2009 | 1,163.7 | 1,270.0 | 1,570.1 | 1,149.0 |
| December 2010 | 1,163.7 | 1,163.3 | 1,185.4 | 1,149.0 |
| January | 1,158.7 | 1,138.2 | 1,163.1 | 1,120.0 |
| February | 1,159.0 | 1,155.7 | 1,170.0 | 1,144.0 |
| March | 1,131.2 | 1,136.1 | 1,153.0 | 1,128.0 |

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| Year ended December 31, | At the end of period | Average rate (1) | High | Low |
|-------------------------|----------------------------|---------------------|---------|---------|
| | | (Won per US\$1.00) | | |
| April | 1,108.0 | 1,115.5 | 1,126.3 | 1,104.0 |
| May | 1,194.5 | 1,164.8 | 1,253.2 | 1,115.0 |

- (1) Annual average rate refers to the average of the exchange rates on the last date of each month (or a portion thereof) during the period. Monthly average rate refers to the average of daily exchange rates during the period.

Source: For periods prior to and on December 31, 2008, the noon buying rates of the Federal Reserve Bank of New York; for periods subsequent to December 31, 2008, Federal Reserve Statistical Release, Board of Governors of the Federal Reserve System.

3.B. Capitalization and Indebtedness

Not applicable.

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

Not applicable.

3.D. Risk Factors

Risks Related to the Company

Risks Related to Our Business

The merger with NHN Games Co., Ltd. (“NHN Games”) may expose us to certain risks.

On April 15, 2010, our board of directors approved a transaction with NHN Games, whereby NHN Games will merge with and into us under Korean law, pursuant to which NHN Games will cease to exist and we will be the sole surviving entity (the “Merger”). The board of directors of NHN Games also approved the Merger and both companies entered into a merger agreement. All the assets and liabilities of NHN Games, along with its rights and obligations, will be assumed by us in accordance with applicable laws. At the shareholder meetings of our company and NHN Games, held on June 4, 2010, the shareholders of both companies approved the Merger.

The Merger exposes us to potential difficulties that could prevent us from achieving the strategic objectives for the Merger or harm our ability to achieve anticipated levels of profitability from the Merger. Specifically, these difficulties include:

- diversion of management’s attention from the normal operation of our business;
- potential loss of key employees of NHN Games;
- increases in our expenses and working capital requirements, which reduce our return on invested capital;
- potential increases in debt, which increase our operating costs as a result of higher interest payments;
- exposure to unanticipated contingent liabilities of NHN Games;
- difficulties in integrating NHN Games into our existing operations, technologies and personnel which may prevent us from achieving, or may reduce, the anticipated synergies;
- the inability to generate sufficient revenue to offset the costs and expenses of the Merger;
- the dilution of share ownership; and
- potential loss of, or harm to, relationships with employees, customers and suppliers as a result of challenges from the integration process.

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If we are not able to successfully manage these potential difficulties, the Merger might not result in any anticipated benefits, which could materially and adversely affect our business, financial condition and results of operations.

Our business is intensely “hit” driven. If we fail to deliver “hit” products or if consumers prefer our competitors’ products over our own, our operating results could suffer.

While many new online game products are regularly introduced, only a relatively small number of “hit” titles account for a significant portion of the total net revenue in our industry. We commenced commercial service of Soul of the Ultimate Nation (SUN) in Korea in the fourth quarter of 2006, in Taiwan and China in the second quarter of 2007 and in Japan in the second quarter of 2008. The performance in Korea, however, has not met our initial expectations. We have also conducted multiple tests of Huxley since September 2007, and we expect to commence commercial service of Huxley in the second half of 2010 in Korea and the U.S. In addition to our internal development efforts, we have entered into agreements with NHN Games to broaden our game offerings. We have already started offering Archlord through a portal website jointly operated with NHN Games, and have plans to offer Reign of Revolution (“R2”) in the near future.

We are unable to predict if our new games and services will be successful. In addition, even if any of our games are initially well-received, the introduction of more popular games by our competitors may significantly shorten the life-cycle of our game, which could cause our revenue to fall below our expectations. If our competitors develop more successful products, offer competitive products at lower prices, or if we do not continue to develop consistently high-quality and well-received products, our revenue, margins and profitability will decline.

Additionally, our business is subject to risks that are generally associated with the entertainment industry, many of which are beyond our control. These risks could negatively impact our operating results and include: the popularity, price and timing of our games and the platforms on which they are played; economic conditions that adversely affect discretionary consumer spending; changes in consumer demographics; the availability and popularity of other forms of entertainment; and critical reviews and public tastes and preferences, which may change rapidly and are difficult to predict.

Disruptions in global credit and financial markets and the resulting governmental actions around the world could have a material adverse impact on our business and the ability to meet our funding needs, and could cause the market value of our common shares and ADSs to decline.

Global credit markets have been experiencing difficulties and volatility since the second half of 2008. The market uncertainty that started in the U.S. residential market further expanded to other markets such as those for leveraged finance, collateralized debt obligations and other structured products. These developments have resulted in significant contraction, de-leveraging and reduced liquidity in the global credit markets, as well as bankruptcy or acquisition of, and government assistance to, several major U.S. and European financial institutions. More recently, concerns over volatility in the global financial markets resurfaced when Dubai requested a standstill in connection with debt owed by its state-run companies and growing budget deficits of Greece led the three leading rating agencies to downgrade the country’s debt ratings. In response to such developments, legislators and financial regulators in the United States and other jurisdictions, including Korea, have implemented a number of policy measures designed to add stability to financial markets. However, the overall impact of these legislative and regulatory efforts on the global financial markets is uncertain, and they may not have the intended stabilizing effects. The United States Securities and Exchange Commission (the “SEC”), other regulators, self-regulatory organizations and exchanges are authorized to take extraordinary actions in the event of market emergencies, and may effect changes in law or interpretations of existing laws.

We are exposed to risks related to changes in the global and Korean economic environments, changes in interest rates and instability in the global financial markets. As liquidity and credit concerns and volatility in the global financial markets increased, the value of the Won relative to the Dollar has fluctuated significantly. Furthermore, as a result of adverse global and Korean economic conditions, there has been continuing volatility in securities prices of Korean companies, including ours, which may result in trading and valuation losses on our trading and investment securities portfolio. In addition, limitations on the availability of credit resulting from heightened concerns about the stability of the markets generally and the strength of counterparties specifically have led many lenders and institutional investors to reduce or cease providing funding to borrowers, which may negatively impact

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our liquidity and results of operation. Major market disruptions and the current adverse changes in market conditions and regulatory climate may further impair our ability to meet our desired funding needs. We cannot predict how long the current market conditions will last. These recent and developing economic and governmental factors may have a material adverse effect on our business and the ability to meet our funding needs, as well as negatively affect the market prices of our common shares and ADSs. In addition, if our game players reduce their spending on playing massively-multiplayer role-playing online games, or MMORPGs, due to such uncertain economic conditions, our business may be adversely affected.

We may have conflicts of interest with NHN Games. Because of NHN Games' significant ownership interest in and control over us, we may not be able to resolve such conflicts on terms favorable to us.

Since May 2008, NHN Games purchased common stock of our company (the "Common Shares") from various shareholders including our prior controlling shareholders. As a result, it has gained control of our company and owned 3,469,784 Common Shares or 29.26% of the outstanding Common Shares as of May 06, 2010. In addition, NHN Games entered into an arrangement with Nam-Ju Kim, Ki-Yong Cho, Kil-Saup Song and Chang Keun Kim that they would have a good faith discussion with NHN Games before exercising any voting rights of the Common Shares and that they shall exercise voting rights together in the same direction in accordance with the discussion for matters relating to changing or influencing control of our company. Based on such arrangement, the individuals referred to above each executed and delivered a power of attorney appointing NHN Games as the attorney-in-fact with full power and authority to act with respect to all matters related to Section 147 of the Capital Market and Financial Investment Business Act of Korea, which sets forth the obligation to report beneficial ownership of equity securities of more than 5% of a class of stock listed on Korea Exchange or KOSDAQ. As a result, NHN Games effectively controlled 37.76% of our outstanding Common Shares as of May 06, 2010. Such share holding gives NHN Games the power to significantly affect the actions that require shareholder approval under Korean law and our articles of incorporation, including the election and removal of any member of our board of directors, mergers, consolidations and other business combinations and changes to our articles of incorporation. At the effective date of the Merger, NHN Corporation ("NHN Corp.") and Byoung Gwan Kim, who together owns the majority of the shares of NHN Games, will together own the majority the Common Shares, and thus will have the power to control the actions that require shareholder approval. As a result of such share ownership, its voting power may cause transactions to occur that might not be beneficial to you as a holder of ADSs and may prevent transactions that would be beneficial to you. For example, NHN Games, or after the effective date of the Merger, NHN Corp. and Byoung Gwan Kim, may prevent a transaction involving a change of control of us, including transactions in which you as a holder of our ADSs might otherwise receive a premium for your securities over the then-current market price; approve a merger or consolidation of our company, which you may disapprove; or sell a controlling interest in us to a third party without your approval. Decisions by NHN Games, or after the effective date of the Merger, by NHN Corp. and Byoung Gwan Kim, with respect to us or our business may be resolved in ways that favor them, which may not coincide with the interests of our other shareholders.

If we do not meet our product development schedules, our operating results will be adversely affected.

We have new games and services that we plan to launch from the second half of 2010. Huxley is scheduled for commercial launch in the second half of 2010, and T Project is planned to have an open beta testing in 2011. We have also commenced the development of MU2. Our ability to meet product development schedules is affected by a number of factors, including the creative processes involved, the coordination of development teams required by the increasing complexity of our products and the need to fine-tune our products prior to their release. We have in the past experienced development delays of our products. Failure to meet anticipated production or commercialization schedules may cause a shortfall in our revenue, adversely affect our profitability and cause our operating results to be materially different from expectations. In addition, the perceived or actual delay of our launch schedules has in the past and will likely in the future have a negative affect on the price of our common shares and ADSs.

We currently depend on two games, MU and Soul of the Ultimate Nation (SUN), for substantially all of our revenue.

Substantially all of our revenues and profits are currently derived from two online games, MU and Soul of the Ultimate Nation (SUN). Revenue generated from MU decreased in 2009 and may decrease in the future as the game has reached its declining stage and as users may switch to newly introduced games or other MMORPGs or

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discontinue playing MMORPGs. We commenced commercial service of Soul of the Ultimate Nation (SUN) in Korea in the fourth quarter of 2006, in Taiwan and China in the second quarter of 2007 and in Japan in the second quarter of 2008, but the game is still in its initial stages contributing less to our revenue than MU. We have entered into agreements with NHN Games to broaden our game offerings. We commenced service of Archlord in July 2009 and plan to offer R2 in the near future. If revenue derived from Soul of the Ultimate Nation (SUN) or Archlord does not increase at the pace we expect, or at all, MU revenue continues to decline or commercialization of new games such as Huxley and R2 is delayed for any reason, our future results of operations and the prices of our common shares and ADSs will be negatively affected.

Increased competition in the online game industry may adversely affect our business.

Competition in our industry is intense and we expect new competitors to continue to emerge. There are over 100 companies in Korea alone that are dedicated to developing and/or operating online games. Our competitors in the MMORPG industry vary in size from small companies to very large companies with dominant market shares such as Blizzard and NCsoft. Chinese game developers have also developed and successfully launched new games, many of which are tailored to the needs and tastes of Chinese game players. We also compete with online casual game and game portal companies such as NHN, Neowiz, Nexon and CJ Internet. In addition, we may face stronger competition from console game companies, such as Sony, Microsoft and Nintendo, many of which have expanded their game services and offerings to enable console games to be played over the Internet. 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 resources to design and develop new games, undertake extensive marketing campaigns, adopt aggressive pricing policies, pay high compensation to game developers or compensate independent game developers to the same degree as some of our competitors. In markets outside Korea, we may not be able to provide games that are as customized to the tastes and preferences of local customers. We believe the decline in the number of MU subscribers in major overseas market such as China is attributable to the success of new games introduced by our competitors. In addition, increased competition in the online game industry may also reduce the number or growth rate of our subscribers, the average number of hours played by our subscribers, our license fee revenue or our subscription fees. All of these competitive factors may adversely affect our cash flows, operating margins and profitability.

Rapid technological change may limit our ability to recover game development costs and adversely affect our future revenues and profitability.

The online game industry is subject to rapid technological change. We need to anticipate the emergence of new technologies and games, assess their market acceptance, and make substantial game development and related investments. In addition, new technologies in online game programming or new platforms such as the game consoles introduced to the market could render MU, Soul of the Ultimate Nation (SUN) or other online games that we expect to develop in the future less attractive to our subscribers, thereby limiting our ability to recover development costs and potentially adversely affecting our future revenues and profitability.

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 results of operations.

Our games may contain errors or flaws that become apparent only after their release, particularly as we seek to develop and launch new games under tight time constraints. We believe that if our customers have negative experiences with our games, they may be less inclined to commence, continue or resume subscriptions with us or recommend our games to other potential customers. Undetected programming errors and game defects can harm our reputation, cause our customers to terminate subscriptions with us, divert our resources and delay market acceptance of our games, any of which could materially and adversely affect our results of operations and have a negative effect on the price of our common shares and ADSs.

[Table of Contents](#)***Unexpected network interruptions caused by system failures or any leaks of personal information may lead to subscriber and revenue reductions and harm our reputation.***

Any failure to maintain the satisfactory performance, reliability, security and availability of our network infrastructure may cause significant harm to our reputation and our ability to attract and maintain subscribers. Any server interruptions, breakdowns or system failures, including failures attributable to sustained power shutdowns, efforts to gain unauthorized access to our systems, loss or corruption of data or malfunctions of software or hardware, or other events outside our control that could result in a sustained shutdown of all or a material portion of our services could adversely impact our ability to service our subscribers. Our network systems are also vulnerable to damage from fire, flood, power loss, telecommunications failures, hacking and similar events.

In addition, subscriber personal information leaks or any security breach may adversely affect our business. Any failure to maintain reliable network infrastructure or proper security measures can harm our reputation and our business, expose us to litigation risks and have a negative effect on the price of our common shares and ADS.

We may not be able to adequately protect our intellectual property rights, which could decrease our competitiveness.

We regard our proprietary software, domain names, trade names, trademarks and similar intellectual properties as critical to our success. We rely on a combination of copyrights, service marks and patents to protect our intellectual property rights. Policing unauthorized use of proprietary technology is difficult and expensive. Despite our efforts to protect our proprietary rights, unauthorized parties may attempt to copy or otherwise obtain and use our technology. We cannot be certain of our ability to prevent misappropriations of our technology in Korea, China and other countries where intellectual property protection laws may not be as robust as in the United States. From time to time, we may have to resort to litigation to enforce our intellectual property rights, which could result in substantial costs and diversion of our resources.

We believe that we may have been a passive foreign investment company ("PFIC") for 2009, which has certain adverse U.S. federal income tax consequences to holders of common shares and ADSs.

In general, we will be considered a PFIC for U.S. federal income tax purposes for any taxable year in which (i) 75% or more of our gross income consists of passive income or (ii) 50% or more of the average quarterly value of our assets consist of assets that produce, or are held for the production of, passive income. Based on the price of our common shares and ADSs during our 2009 taxable year and the amount of passive assets, including cash and cash equivalents, held by us throughout that year, we believe we may have been a PFIC for our 2009 taxable year. Further, there is a significant risk that we will be a PFIC for our 2010 taxable year and in future taxable years.

If we are a PFIC for any year that you hold common shares or ADSs, certain adverse U.S. federal income tax consequences could apply to you, including recharacterization of gains realized on the disposition of, and certain dividends received on, the common shares or ADSs as ordinary income earned pro rata over your holding period for such common shares or ADSs, taxed at the maximum rates applicable during the years in which such income is treated as earned, and subject to interest charges for a deemed deferral benefit. You should consult your own tax adviser with respect to our potential PFIC status and the consequences to you. See "Item 10. Additional Information – 10.E. Taxation – U.S. Federal Income Tax Considerations – Passive Foreign Investment Company Considerations."

Our online games may be subject to government restrictions or ratings systems, which could delay or prohibit the release of new games or reduce the existing and potential range of our customer base.

Legislation is periodically introduced in Korea by government agencies to establish a system for protecting consumers from excessive usage, the influence of graphic violence and sexually explicit material contained in various types of games. Korean law currently requires online game companies to obtain ratings classifications and implement procedures to restrict the distribution of online games to certain age groups. See "Item 4. Information on

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the Company — 4.B. Business Overview — Laws and Regulations.” Similar mandatory ratings systems and other regulations affecting the content and distribution of our games have also been adopted in China and other markets. In the future we may be required to modify our game content or features or alter our marketing strategies to comply with new government regulations or new 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 range of our customer base. Moreover, uncertainties regarding government restrictions or ratings systems applicable to our business could give rise to market confusion, thereby adversely affecting our business or the prevailing price of our common shares or ADSs.

Foreign operations are subject to different business, political and economic risks.

For the year ended December 31, 2009, 34.5% of our total net revenues came from license and royalty revenues from our operations outside of Korea, including China, Taiwan, Japan, the Philippines, Vietnam and the U.S.. Foreign operations are subject to inherent risks, including disputes with our licensees or joint venture partners, uncertain legal environments, different consumer preferences, unexpected regulatory requirements, tariffs and other barriers, difficulties in training and retraining staff and managing foreign operations, difficulties in obtaining or renewing required licenses and obtaining administrative approvals and difficulties in collecting foreign receivables. We will also be exposed to risks of foreign exchange fluctuations as we record our license and joint venture income in Won in our financial statements.

As the online game industry is at an early stage of development, notwithstanding certain differences among countries, new laws and regulations may be adopted from time to time to require additional licenses and permits and to address new issues that arise. In addition, substantial uncertainties exist regarding the interpretation and implementation of current and any such future laws and regulations applicable to the online game industry. We cannot assure you that we will be able to obtain timely, or at all, required licenses or any other new license required in the future. We cannot assure you that we will not be found in violation of any current laws or regulations should their interpretation change, or that we will not be found in violation of any future laws or regulations.

Risks Related to The Republic of Korea

Increased tension with North Korea could adversely affect us.

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, the sinking of the Korean warship Cheonan and uncertainty regarding North Korea’s actions and possible responses from the international community. In April 2009, after launching a long-range rocket over the Pacific Ocean, which led to protests from the international community, North Korea announced that it would permanently withdraw from the six-party talks that began in 2003 to discuss Pyongyang’s path to denuclearization. On May 25, 2009, North Korea conducted its second nuclear testing and launched several short-range missiles. After North Korea’s second nuclear testing, the Republic joined the Proliferation Security Initiative, a U.S.-led multinational initiative involving the interdiction of third-country ships on the high seas on the basis of carrying nuclear materials, over Pyongyang’s harsh rebuke and threat of war. After the United Nations Security Council passed a resolution on June 12, 2009 to condemn North Korea’s second nuclear test and impose tougher sanctions such as a mandatory ban on arms exports, North Korea announced that it would produce nuclear weapons and take “resolute military actions” against the international community. On March 27, 2010, the Korean warship Cheonan sank, causing casualties of Korean sailors. In May 2010, Korea accused North Korea of causing the sinking, increasing the tension between the two countries.

Recently, there has been increased uncertainty about the future of North Korea’s political leadership. In June 2009, there were reports citing American and South Korean officials that Kim Jong-il, the North Korean ruler who reportedly suffered a stroke in August 2008, designated his third son, in his twenties, to become his successor. The succession plan, however, remains uncertain. In addition, North Korea’s economy faces severe challenges.

There can be no assurance that the level of tension and instability in the Korean peninsula will not escalate in the future, or that the political regime in North Korea may not suddenly collapse. Any further increase in tension or

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uncertainty relating to the military or economic stability in the Korean peninsula, including a breakdown of diplomatic negotiations over the North Korean nuclear program, the occurrence of military hostilities or heightened concerns about the stability of North Korea's political leadership, could have a material adverse effect on the credit rating of Korea, our operations and the price of our common shares and ADSs.

If economic conditions in Korea deteriorate, our current business and future growth could be materially and adversely affected.

We are incorporated in Korea and a significant portion of our operations and assets are based in Korea. As a result, we are subject to political, economic, legal and regulatory risks specific to Korea. Recent difficulties affecting the U.S. and global financial sectors, adverse conditions and volatility in the U.S. and worldwide credit and financial markets, fluctuations in oil and commodity prices and the general weakness of the U.S. and global economy have increased the uncertainty of global economic prospects in general and have adversely affected, and may continue to adversely effect global and Korean economies. Any future deterioration of the Korean and global economy could adversely affect our business, financial condition, results of operations and cash flows.

Developments that could hurt Korea's economy in the future include:

- adverse changes or volatility in foreign currency reserve levels, commodity prices (including oil prices), exchange rates (including fluctuation of the U.S. dollar or Japanese yen exchange rates or revaluation of the Chinese renminbi), interest rates and stock markets;
- substantial decreases in the market prices of Korean real estate;
- increasing delinquencies and credit defaults by consumer and small and medium sized enterprise borrowers;
- declines in consumer confidence and a slowdown in consumer spending;
- adverse developments in the economies of countries that are important export markets for Korea, such as the United States, Japan and China, or in emerging market economies in Asia or elsewhere;
- the continued emergence of the Chinese economy, to the extent its benefits (such as increased exports to China) are outweighed by its costs (such as competition in export markets or for foreign investment and the relocation of the manufacturing base from the Republic to China);
- political, social and labor unrest;
- a decrease in tax revenues and a substantial increase in the Government's expenditures for fiscal stimulus measures, unemployment compensation and other economic and social programs that, together, would lead to an increased government budget deficit;
- financial problems or lack of progress in the restructuring of Korean conglomerates, other large troubled companies, their suppliers or the financial sector;
- loss of investor confidence arising from corporate accounting irregularities and corporate governance issues at certain Korean conglomerates;
- the economic impact of any pending or future free trade agreements, including the Free Trade Agreement recently negotiated with the United States;
- geo-political uncertainty and risk of further attacks by terrorist groups around the world;
- outbreak of the H1N1 flu or the recurrence of severe acute respiratory syndrome, or SARS, or an outbreak of avian flu in Asia and other parts of the world;
- deterioration in economic or diplomatic relations between the Republic and its trading partners or allies, including deterioration resulting from trade disputes or disagreements in foreign policy;

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- political uncertainty or increasing strife among or within political parties in the Republic;
- hostilities involving oil producing countries in the Middle East and any material disruption in the supply of oil or increase in the price of oil resulting from those; and
- an increase in the level of tension or an outbreak of hostilities between North Korea and the Republic or the United States.

Risks Related to Our ADSs

We recently announced our intention to delist our ADSs from NASDAQ Global Market reducing the liquidity of the ADSs.

On June 18, 2010, we announced our intention to delist our ADSs from NASDAQ Global Market and to deregister and terminate our reporting obligations with the SEC. We have provided a written notice to NASDAQ of the intent to delist and will arrange in due course, after consultation with NASDAQ, the date on which our ADSs will no longer be traded on NASDAQ Global Market. We plan to maintain an American Depositary Receipt program on a Level I basis, which will allow investors to hold their securities in the form of ADSs. As a result, our ADSs will only be traded over-the-counter and will not be traded on any national securities exchange or inter-dealer quotation system in the U.S. Common Shares will continue to be traded on KOSDAQ Market.

KOSDAQ volatility may adversely affect the price of our common shares and the ADSs.

Certain shares listed on the KOSDAQ have recently experienced significant price and volume fluctuations, sometimes without regard to the underlying fundamentals of such shares. Historically, the KOSDAQ itself has had substantially less trading volume than the KRX Stock Market. As a result, our common shares may be less liquid and the prevailing price of the common shares may be more volatile in the future than other shares listed on the KOSDAQ or shares listed on the KRX Stock Market. The volatility and limited liquidity of our common shares on the KOSDAQ may adversely affect the market price of the ADSs.

We currently follow home country practice in lieu of complying with certain requirements of the Nasdaq Stock Market. This may afford less protection to holders of our ordinary shares and ADSs.

Rule 5605 of the Nasdaq Listing Rules, requires listed companies to have, among others, a board of directors comprised of a majority of independent directors, the holding of regularly scheduled meetings at which only independent directors are present, a compensation committee, if any, comprised solely of independent directors, and a nominations committee, if any, comprised solely of independent directors. As a foreign private issuer, however, we are permitted to, and we do, follow home country practice in lieu of the above requirements. See “Item 6.C. Directors, Senior Management and Employees—Board Practices” and “Item 16G. Corporate Governance” for more information on the significant differences between our corporate governance practices and those followed by U.S. companies under the Nasdaq Listing Rules. As a result, we have fewer board members exercising independent judgment and the level of board oversight on the management of our company may therefore decrease. The board members who are not independent may also cause a merger, consolidation, change of control or other transactions or actions without the consent of the independent directors, which may lead to a conflict with the interest of holders of our ordinary shares and ADSs. Holders of our ordinary shares and ADSs may therefore be afforded less protection.

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.

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. 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.

Your ability to deposit common shares into the depositary facility may be limited.

Neither common shares acquired in the open market nor common shares withdrawn from the ADS depositary facility may be deposited or redeposited, as the case may be, under the deposit agreement governing the ADSs without our consent. It is our policy to consent to any deposit unless such deposit is prohibited by Korean law, violates our Articles of Incorporation or the total number of our common shares on deposit with the depositary does not exceed 3,900,000. No assurance can be given that deposits or redeposits of our common shares will always be

permitted. If an investor's ability to deposit common shares is limited, the prevailing market price of our ADSs may differ from the prevailing market price of the equivalent number of our common shares traded on the KOSDAQ.

You may not be able to exercise preemptive rights.

The Korean Commercial Code and our Articles of Incorporation require us, with certain exceptions, to offer shareholders the right to subscribe for new common shares in proportion to their existing ownership percentages

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whenever new common shares are issued. Under the deposit agreement governing the ADSs, if we offer rights to subscribe for additional common shares, the depository under the deposit agreement, after consultation with us, may make such rights available to you or dispose of such rights on your behalf and make the net proceeds available to you or, if the depository is unable to take such actions, it may allow the rights to lapse with no consideration to be received by you. The depository is required to make available any rights to subscribe for any securities only when a registration statement under the United States Securities Act of 1933, as amended (“Securities Act”), is in effect with respect to the securities or if the offering of the securities is exempt from the registration requirements under the Securities Act. We are under no obligation to file a registration statement under the Securities Act to enable you to exercise preemptive rights for our common shares underlying the ADSs, and we cannot assure you that any registration statement will be filed or that an exemption from the registration requirement under the Securities Act will be available. Accordingly, you may not be entitled to exercise preemptive rights and may thereby suffer dilution of your interests in us.

You will not have the same voting rights as a holder of common shares.

You may exercise voting rights with respect to the common shares underlying your ADRs. You may instruct the depository as to how to exercise the voting rights for the common shares which underlie your ADSs if the depository asks you to provide it with voting instructions. After receiving voting materials from us, the depository will notify the ADR holders of any shareholder meeting or solicitation of consents or proxies. This notice will describe how you may instruct the depository to exercise the voting rights for the common shares that underlie your ADSs, subject to Korean law and the provisions of our Articles of Incorporation. For instructions to be valid, the depository must receive them on or before the date specified. The depository will endeavor, insofar as practicable and subject to Korean law and the provisions of our Articles of Incorporation, to vote or to have its agents vote the common shares or other deposited securities represented by your ADSs as you instruct. The depository will not itself exercise any voting discretion. ADSs for which no voting instructions have been received will not be voted. You may only exercise the voting rights in blocks of 10 ADSs. Neither the depository nor its agents are responsible for any failure to carry out any voting instructions (if acting in good faith), for the manner in which any vote is cast or for the effect of any vote. There is no guarantee that you will receive voting materials in time to instruct the depository to vote and it is possible that you, or persons who hold their ADSs through brokers, dealers or other third parties, will not have the opportunity to exercise a right to vote.

You may not be able to exercise dissent and appraisal rights.

In some limited circumstances, including the transfer of the whole or any significant part of our business, our acquisition of a part of the business of any other company having a material effect on our business, and our merger or consolidation with another company, dissenting shareholders have the right to require us to purchase their shares under Korean law. See “Item 10. Additional Information — 10.B. Articles of Incorporation — Rights of Dissenting Shareholders.” 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 and become a direct shareholder prior to the record date for the shareholders’ meeting at which the relevant transaction is to be approved.

You may be subject to Korean withholding taxes.

Under Korean tax law, if you are a U.S. investor, you may be subject to Korean withholding taxes on capital gains and dividends on the ADSs unless an exemption or a reduction under the income tax treaty between the United States and Korea is available. Under the United States-Korea 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, with certain limited exceptions. See “Item 10. Additional Information — 10.E. Taxation — Korean Taxation” for a more detailed discussion of the effects of Korean tax laws on the holders of ADSs, including the possible imposition of a Korean securities transaction tax.

You may have difficulty enforcing any judgment obtained outside Korea against us or our Directors and officers.

We are organized under the laws of Korea, and all of our Directors and officers reside in Korea. All or a significant portion of our assets and the assets of such persons are located outside of the United States. As a result, it

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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. We have, however, appointed an agent in New York to receive service of process in any proceedings in the State of New York relating to our common shares or ADSs. Notwithstanding the foregoing, it may be difficult to enforce in Korea civil liabilities predicated on the federal securities laws of the United States or the securities laws of any state of the United States.

Item 4. Information on the Company

4.A. History and Development of the Company

We were incorporated as a company with limited liability under Korean law on April 28, 2000. Our legal and commercial name is “주식회사 웹젠” (pronounced “Chushikhoesa Webzen”) in Korean, and “Webzen Inc.” in English. Our registered office is located at 14th Floor, Daerung Post Tower 2nd, 182-13 Guro-Dong, Guro-Gu, Seoul, Korea 152-790. Our telephone number is (822) 3498-1600. We maintain a website at <http://www.webzen.com>. The information on our website is not incorporated by reference into this annual report. Our agent for U.S. federal securities law purposes is National Registered Agents, Inc., located at 875 Avenue of the Americas, Suite 501, New York, New York, 10001.

Our largest shareholder is NHN Games, a private company established in Korea in 2004 by NHN Corp. NHN Corp. is the largest diversified internet service provider in Korea, which is listed on KOSPI Market of Korea Exchange. NHN Corp. established NHN Games to strengthen its online game development capabilities. NHN Games is a leading developer and service provider of massively-multiplayer online games and is engaged in the business of developing and distributing online games, licensing software and other related services. NHN Games has developed and provides online games such as Continent of the Ninth (“C9”), Archlord and R2.

Archlord is a fantasy MMORPG, in which players, among other things, aim to become the archlord with unlimited powers and special skills. Archlord has a unique item customizing system that gives players the power to directly change and upgrade their items as part of their skill set. The game was first released in 2005 in Korea and in 2006 in the U.S. and Europe. In 2007, Archlord was offered on a free-to-play basis. We currently offer Archlord both in Korea and globally. R2, a fantasy MMORPG, was first released in 2006. R2 allows player versus player conflict, where one player can actually be killed by another player. C9, a fantasy multiplayer online role-playing game (“MORPG”) was first released in August 2009 and partial commercial service began in September of the same year. In December 2009, C9 won the Grand Prize in 2009 Korean Game Awards. We plan to offer R2 in the second half of 2010 through our game portal. Battle Territory or Battery, is a modern military massively multiplayer online first person shooter game emphasizing military themes, that delivers realistic fight scenes in a military combat environment. We entered into a publishing agreement with NHN Games to publish Battery.

We are a leading developer and distributor of online games in Korea. Some of the important events in the development of our business since the beginning of 2008 are set forth below:

- GameOn Co. Ltd. (“GameOn”) launched open beta testing and commercial service of Soul of the Ultimate Nation (SUN) in Japan in March and April 2008, respectively.

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- In May 2008, Webzen Taiwan Inc. (“Webzen Taiwan”) launched open beta testing and commercial service of Mini Fighter in Taiwan.
- In May 2008, we entered into a three-year license agreement with NHN USA Inc. (“NHN USA”) for the distribution of Huxley in North America and Europe.
- In June 2008, we initiated open beta testing in Korea for Huxley.
- In September 2008, NHN Games became our largest shareholder.
- In October 2008, we appointed new chief executive officer, Mr. Chang Keun Kim.
- In November 2008, we won the second prize by the Chairman of Korea Communications Commission in Korea Internet Award, sponsored by Korea Communications Commission.
- In December 2008, Huxley won the Game Graphics Prize and Game Sound Prize in 2008 Korean Game Awards.
- In March 2009, we entered into a channeling agreement with NHN Corp. to distribute Soul of the Ultimate Nation (SUN) in Korea through NHN Corp.’s online game portal, www.hangame.com.
- In April 2009, we entered into a service agreement with NHN Games to have it develop and maintain our game Parfait Station.
- In April 2009, we entered into a lease agreement with nPluto Co., Ltd., an online game developer, to lease our internet data centers and servers for nPluto’s future games.
- In May 2009, we entered into a three-year exclusive license with NHN USA Inc. to distribute Soul of the Ultimate Nation (SUN) in the United States, Canada, Mexico and the United Kingdom through www.ijji.com.
- In May 2009, we amended the online publishing agreement entered into with Red 5 Studios, Inc. (“Red 5 Studios”).
- In June 2009, we launched the global service of MU online on webzen.com and started development of MU2
- In June 2009, we entered into an outsourcing agreement with NHN Games where we are to provide services relating to strategy, marketing, promotion and businesses abroad.
- In July 2009, we sold off our office space on the 3rd floor of Daelim Acrotel Building C, 467-6, Dogok-dong, Kangnam-gu, Seoul, Korea.
- In August 2009, we entered into a joint venture agreement with NHN Games where we will provide MU and SUN online and NHN Games will provide Archlord and R2 through a jointly operated global game portal called webzen.com.
- In October 2009, we launched the global service of Archlord and SUN: World Edition on webzen.com.
- In November 2009, we began offering MU Blue.
- In December 2009, we filed a suit against The9 Limited (“The9”) for the return of trademark “MU.”
- In December 2009, we moved our corporate headquarters from Daelim Acrotel Building C, 467-6 Dogok-dong Kangnam-Ku, Seoul, South Korea to 14th Floor, Daerung Post Tower 2nd, 182-13, Guro Dong, Guro-Gu, Seoul, South Korea.

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- In December 2009, Webzen Taiwan, our subsidiary, entered into an internet game distribution and service agreement with NHN Games Corp. to provide R2 in Taiwan.
- In February 2010, we entered into a publishing agreement with NHN Games to service Battle Territory, a first-person shooter game developed by NHN Games.
- In April 2010, we announced the decision to merge with NHN Games.
- In April 2010, we entered into a channeling agreement with NHN Corp. to distribute Huxley: Dystopia.
- In May 2010, we started offering Huxley: Dystopia on a trial basis.
- In May 2010, we renewed GameNow.net Ltd. (“GameNow”)’s exclusive license to publish and operate SUN in China.

Since 2008, NHN Games purchased Common Shares from various shareholders including our controlling shareholders. As a result, it has gained control of our company and owned 3,469,784 Common Shares or 29.26% of the outstanding common shares as of May 06, 2010.

On June 18, 2009, NHN Games purchased 155,491 Common Shares from Nam-Ju Kim through a block trade after the close of the KOSDAQ market. The total amount paid by NHN Games for the 155,491 shares was ₩2,721,092,500, or ₩17,500 per share.

On June 18, 2009, NHN Games purchased 114,714 Common Shares from Ki-Yong Cho through a block trade after the close of the KOSDAQ market. The total amount paid by NHN Games for the 114,714 shares was ₩2,007,495,000, or ₩17,500 per share.

On June 18, 2009, NHN Games purchased 119,014 Common Shares from Kil-Saup Song through a block trade after the close of the KOSDAQ market. The total amount paid by NHN Games for the 119,014 shares was ₩2,082,745,000, or ₩17,500 per share.

On September 9, 2008, Nam-Ju Kim, Ki-Yong Cho, Kil-Saup Song, Hyung-Cheol Kim and Chang Keun Kim each executed and delivered a power of attorney appointing NHN Games as the attorney-in-fact with full power and authority to act with respect to all matters related to Section 147 of the Capital Market and Financial Investment Business Act of Korea, which sets forth the obligation to report beneficial ownership of equity securities of more than 5% of a class of stock listed on Korea Exchange or KOSDAQ. When NHN Games purchased the Common Stock from Nam-Ju Kim, Ki-Yong Cho, Kil-Saup Song and Hyung-Cheol Kim as set forth above, it had an arrangement (the “Arrangement”) with the individuals referred above that they would have a good faith discussion with NHN Games before exercising any voting rights of the Common Shares and that they shall exercise voting rights together in the same direction in accordance with the discussion for matters relating to changing or influencing control of our company, including:

- elections and dismissals of directors;
- amendments to the article of incorporation regarding our organization including any change to the board of directors;
- changes to our capital;
- approvals of dividend plans;
- mergers and spin-offs;
- general share exchanges or stock transfers;
- transfers or acquisitions of significant business operations;
- disposals of significant assets; and dissolution of our company.

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On August 24, 2009, Hyung-Choel Kim resigned from his post as the CFO and Director of the Company and withdrew from the Arrangement.

NHN Games controls the Board and thereby oversees our business, operations and future plans.

On April 15, 2010, our board of directors approved the Merger. The board of directors of NHN Games also approved the Merger and both companies entered into a merger agreement. After the board approvals and the execution of the merger agreement, we filed a merger report on Data Analysis, Retrieval and Transfer System (“DART”) of the Financial Supervisory Service of Korea (“FSS”) and made it public.

In connection with the Merger, shareholders of NHN Games will be issued Common Shares in exchange for the shares of NHN Games held by them, pursuant to an exchange ratio determined by a formula prescribed under Korean securities law. Article 176-5 of the Enforcement Decree of the Financial Investment Services and Capital Markets Act of Korea (the “Enforcement Decree”) provides that, in cases of a merger between a “stock-listed corporation” and a “stock-unlisted corporation” (i.e., a private company), (i) the stock exchange ratio shall be determined based upon the market price of the stock-listed corporation (as long as market price exceeds the net asset value per share) and the weighted average of “asset value,” “earnings value” and “relative value” of the stock-unlisted corporation, provided that when relative value is unavailable, it may be replaced with the weighted average of the asset value and earnings value (the methods of calculating asset value, earnings value and relative value are to be prescribed by the Financial Services Commission (“FSC”)) and (ii) if the surviving entity after the merger is a stock-listed corporation, the appropriateness of the merger value shall be appraised by an outside appraisal organization such as an accounting firm, credit rating agency or other organizations designated in the rules. FSC has published interpretive guidelines setting forth that (i) asset value shall be calculated by subtracting loans and receivables the payments of which are doubtful from net tangible assets and then dividing by issued and outstanding shares, (ii) earnings value shall be calculated by dividing estimated net profit per share (using the weighted average of the projections of net income for the current year and the immediately subsequent year after subtracting the expected dividends) by the benchmark ROE (150% of the average interest rate of 1-year term savings of four Korean commercial banks designated by FSC) and (iii) relative value is calculated by averaging the market price of two or more companies that are conducting similar businesses, listed on an exchange and meet other requirements and then discounting the price at a reasonable rate, which shall not be lower than 30%. In the Merger, NHN Games used the weighted average of the asset value and earnings value in assessing its stock value for the calculation of the stock exchange ratio. Based on this formula (using April 14, 2010 as the base date for the calculation), the stock exchange ratio was 1.57262712 Common Shares per one NHN Games’ common share. Deloitte Anjin LLC (“Deloitte”), a member firm of Deloitte Touche Tohmatsu, a Swiss Verein, verified the appropriateness of the merger value and stock exchange ratio pursuant to Article 176-5 of the Enforcement Decree. At the shareholder meetings of our company and NHN Games, held on June 4, 2010, the shareholders of both companies approved the Merger. Shareholders of both companies opposing the Merger had appraisal rights under the Korean Commercial Code. We expect the Merger to conclude by July 12, 2010.

Our key strategic objective is to maintain our position as a leading developer of online games in Korea and to emerge as a leading developer and publisher of online games in other markets. We are currently developing several games to diversify our game portfolio and to target various segments in the market. By developing different game genres within the massively-multiplayer online game space, such as first-person shooting games, we will seek to diversify and increase our subscriber base. In addition to our internally developed games, we are also publishing third-party games. We believe that our proven operational experience, established distribution platform and existing subscriber base make us an attractive partner for other online game companies interested in licensing their games to us for distribution in our markets. In line with this objective, we regularly review proposed online games, acquisitions, and investments to supplement and broaden our own game development activities.

On June 18, 2010, we announced our intention to delist our ADSs from the NASDAQ Global Market and to deregister and terminate our reporting obligations with the SEC. Our Board of Directors approved the decision at its meeting held on the same day. We have provided written notice to NASDAQ of the intent to delist and will

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arrange in due course, after consultation with NASDAQ, the date on which our ADSs will no longer be traded on NASDAQ Global Market. We filed a Form 25 with the SEC on June 28, 2010.

The main purpose of delisting is to reduce complexity in financial reporting and related administrative costs as well as to forgo the cost and potential delays of re-submitting a continuing listing application to NASDAQ, the need to re-submit having risen due to the Merger. We plan to maintain an American Depositary Receipt program on a Level I basis, which will allow investors to hold their securities in the form of ADSs. Common Shares will continue to be traded on KOSDAQ Market.

4.B. Business Overview

We are a leading developer and distributor of online games. Our game Soul of the Ultimate Nation (SUN) is a three-dimensional MMORPG provided in Korea, Taiwan, China and Japan and the U.S. MU is a MMORPG initially launched in 2001 and currently is provided in Korea, China, Japan, Taiwan, the Philippines and Vietnam. We are also planning to release new online games beginning in the second half of 2010.

We commercially launched Soul of the Ultimate Nation (SUN) in Korea in November 2006, in Taiwan in April 2007, in China in May 2007 and in Japan in April 2008.

We began offering MU Blue in November 2009.

We have several new games and services that we plan to launch. Huxley is scheduled for commercial launch in the second half of 2010, and T-Project is planned to have an open beta testing in 2011. We have also commenced development of MU2.

In addition to the games developed in-house, we have agreements in place to offer NHN Games' products through our channel. We began offering Archlord to users in Korea in July 2009 and in the U.S. in October 2009. We plan to offer R2 in the second half of 2010. We entered into a publishing agreement with NHN Games to publish Battery.

Current Products

Soul of the Ultimate Nation (SUN) is a MMORPG in which the players experience an epic medieval tale in a world of emperors, armies, magicians and monsters set to an original soundtrack by Howard Shore, an Academy Award winner and composer of the theatrical score for the "Lord of the Rings" films. Soul of the Ultimate Nation (SUN) features a state-of-the-art game graphics environment, taking advantage of normal map rendering and various graphical effects, offering players rich and realistic graphics. Our programmers have developed game engines that enable fluid movement and console-level control of the game characters. Soul of the Ultimate Nation (SUN) can be accessed from any location with a high-bandwidth Internet connection. Registered subscribers may enter our network with a password and a user ID, after downloading our game client software. Players choose a character from five distinct character classes with different fighting skills and magical powers and control the development of that character by allocating points and carrying out tasks to meet the prerequisites for learning certain skills. Players can individually play the game, but they can also form a group using various communication methods to wage a large-scale battle, known as siege warfare.

We commenced the commercial service of Soul of the Ultimate Nation (SUN) in Korea in November 2006, in Taiwan in April 2007, in China in May 2007 and in Japan in April 2008.

In the markets in which we currently provide commercial service of Soul of Ultimate Nation (SUN), we provide the basic service of the game for free. End-users pay us when they buy at our in-game item shops various items for their characters, such as armor, weapons and potions, and the right to change the world or stage in which the end-user plays. This new revenue generating business model is referred to in the online game industry as "microtransaction."

MU is an MMORPG which was initially launched in 2001. MU players select a specific character with which they develop experience and enhanced game capabilities that can be carried over into sequential gaming sessions. Players are able to communicate with each other during the game through instant messaging and may coordinate

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their activities with other players to form groups, thereby coordinating their game skills to achieve collective objectives.

Our MU users pay hourly charges based upon the hour they use our service or, alternatively, pay a flat fee – usually a fixed amount per month – for a longer period of time. In 2007, we introduced microtransaction sales for MU service in Japan, Taiwan and China, and the end-users in those markets pay us when they buy at our in-game item shops various items for their characters, such as armor, weapons and potions and the right to change the world or stage in which the end-user plays. We successfully introduced the same concept to Korea by offering MU Blue in November 2009. Players using MU Blue play on a separate server from players using MU Red, the subscription service. Unlike MU Red, players using MU Blue do not pay hourly or monthly fees.

In addition to the games that we developed internally, we distribute games developed by NHN Games. We currently offer Archlord both in Korea and globally. Archlord is a fantasy MMORPG, in which players, among other things, aim to become the archlord with unlimited powers and special skills. Archlord has an unique item customizing system that gives players the power to directly change and upgrade their items as part of their skill set. The game was first released in 2005 in Korea and in 2006 in the U.S. and Europe. Like Soul of Ultimate Nation (SUN) and MU, revenue from Archlord is generated from microtransaction sales. We also plan to distribute R2, a fantasy MMORPG, which was first released in 2006. R2 allows player versus player conflict, where player can actually be killed by another player. We plan to offer R2 in the second half of 2010 through our game portal. Battle Territory or Battery, is a modern military massively multiplayer online first person shooter game, emphasizing military theme, delivering realistic fight scenes in a military combat environment. We entered into a publishing agreement with NHN Games to publish Battery.

Products under Development

Huxley is a massively-multiplayer online first person shooting game. Users will be able to play a “Doom”-style first person shooting game with up to 5,000 other players simultaneously and battle against opposing races. Huxley finished its closed beta testings in Korea in September 2007 and December 2007 and its open beta testing in Korea in November 2008. After completing several beta tests in 2009, we began offering Huxley on a trial basis in May 2010. We expect to commence its commercial service in Korea and the U.S. in the second half of 2010.

T-Project is being developed by Red 5 Studios and is planned to have a closed beta testing in 2010 and an open beta testing in 2011. For T-Project, we signed a worldwide publishing rights contract with the developing company. The contract is for five years after the game is commercialized, and we have agreed to pay royalties for the exclusive world-wide distribution rights to this game. On May 28, 2009, an amendment to the original publishing agreement was made to waive our obligation to make any additional payments relating to T-project partly in exchange for Red 5 Studios’ publishing rights in the United States and Europe. Under the amendment, Red 5 Studios will pay us 10% of the revenue from the United States and Europe for five years after commercialization and an additional 5% of such revenue (with quarterly cap of US\$2,083 thousand with respect to the 5% additional revenue) for the first three-year period after commercialization. We will remain the exclusive publisher of the game in all other markets throughout the world, but we are required to pay Red 5 Studios 50% of such revenue from other markets for five years after commercialization.

Parfait Station is a massively-multiplayer online shooting game targeting younger age groups and female players. We finished its closed beta testing and open beta testing in Korea in December 2007 and February 2008, respectively. In order to concentrate our development resources on Soul of the Ultimate Nation (SUN) and Huxley, we had put on hold the development of Parfait Station in 2008. In April 2009, we entered into a service agreement with NHN Games under which NHN Games will be responsible for the development, operation and maintenance of Parfait Station until five years after the commercial launch of the game.

Markets

In 2001 and 2002, substantially all of our revenue was generated from online game subscriptions in Korea. In 2003, approximately 85.5% of our revenue was generated from online game subscriptions in Korea and approximately 14.5% of our revenue was generated from the payment of royalties and license fees by our overseas licensee. In 2004, 2005 and 2006, approximately 84.9%, 84.8% and 88.3% of our revenue was generated from online game subscriptions in Korea, Taiwan and China, and approximately 15.1%, 15.2% and 11.7% of our revenue

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was generated from royalties and license fees paid by our licensees in the overseas markets, respectively. In 2007, approximately 67.5%, 6.6% and 4.5% of our revenue was generated from online game subscriptions and microtransaction sales in Korea, Taiwan and China, respectively, and approximately 11.4%, 6.9%, 1.4%, 1.0% and 0.7% of our revenue were generated from royalties and fees paid by our licensees in China, Japan, the U.S., Vietnam and the Philippines, respectively. In 2008, approximately 52.1%, 10.3% and 6.2% of our revenue was generated from online game subscriptions and microtransaction sales in Korea, Taiwan and China, respectively, and approximately 16.0%, 12.8%, 1.4%, 0.8% and 0.4% of our revenue were generated from royalties and fees paid by our licensees in China, Japan, the U.S., Vietnam and the Philippines, respectively. In 2009, approximately 48.2%, 9.6% and 5.3% of our revenue was generated from online game subscriptions and microtransaction sales in Korea, Taiwan and China, respectively, and approximately 22.3%, 9.8%, 1.3%, 0.8% and 0.3% of our revenue were generated from royalties and fees paid by our licensees in Japan, China, Vietnam, the U.S. and the Philippines, respectively.

Korea. We commenced commercial service of MU in Korea in November 2001. We divide our MU online game subscribers in Korea into individual PC account subscribers and Internet cafe subscribers. Individual PC account subscribers are individuals who log on to our game servers either from home or at work, whereas Internet cafe subscribers are commercial businesses with multiple PCs that provide Internet and online game access to their customers for hourly fees. After the introduction of the game, the number of individual PC account subscribers grew until the first quarter of 2004. Since then, the number of individual PC account subscribers has declined, and we recorded 27,806 individual account subscribers at the end of first quarter of 2010 compared to 28,696 at the end of the first quarter of 2009.

The following table sets forth information on MU users and accounts in Korea since 2008:

| | 2008 | | | | 2009 | | | | 2010 |
|--|--------|--------|--------|--------|--------|--------|--------|--------|--------|
| | 1Q | 2Q | 3Q | 4Q | 1Q | 2Q | 3Q | 4Q | 1Q |
| No. of Internet cafe accounts ⁽¹⁾ | 14,972 | 14,136 | 12,701 | 12,149 | 11,171 | 13,460 | 13,007 | 13,157 | 12,560 |
| No. of paying individual PC account subscribers ^{(2) (3)} | 38,461 | 36,323 | 32,626 | 31,209 | 28,696 | 23,481 | 20,636 | 38,198 | 27,806 |

(1) The number of Internet cafe account refers to the number of accounts held by Internet cafes that actually accessed MU online game during the period indicated.

(2) As of the end of the period.

(3) The spike in subscriber numbers in the fourth quarter of 2009 can be attributed to the launch of MU Blue.

We commenced commercial service of our new game Soul of the Ultimate Nation (SUN) in Korea in November 2006. We divide our Soul of the Ultimate Nation (SUN) online game subscribers into individual PC account subscribers and Internet cafe subscribers, but unlike MU, do not collect hourly or monthly subscription fees from them. Our Soul of the Ultimate Nation (SUN) users pay us when they buy – at our in-game item shops – various items for their characters, such as armor, weapons and potions, and the right to change the world or stage in which the end-user plays. Since March 2009, we started to provide our Soul of the Ultimate Nation (SUN) in Korea through NHN Corp.’s game portal www.hangame.com. While the gamers who subscribed for Soul of the Ultimate Nation (SUN) before March 26, 2009 can use our old Soul of the Ultimate Nation (SUN) portal, all new subscribers since then are to use NHN Corp.’s game portal.

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The following table sets forth information on Soul of the Ultimate Nation (SUN) users and accounts in Korea since the first quarter of 2008:

| | 2008 | | | | 2009 | | | | 2010 |
|---|-------|-------|-------|-------|-------|--------|-------|-------|-------|
| | 1Q | 2Q | 3Q | 4Q | 1Q | 2Q | 3Q | 4Q | 1Q |
| No. of Internet cafe accounts ⁽¹⁾ | 8,944 | 6,844 | 5,768 | 3,974 | 2,547 | 11,129 | 8,728 | 8,670 | 7,130 |
| No. of paying individual PC account subscribers ⁽²⁾⁽³⁾ | 6,180 | 4,674 | 3,939 | 2,714 | 3,261 | 6,345 | 4,944 | 5,724 | 4,765 |

- (1) The number of Internet cafe account refers to the number of accounts held by Internet cafes that actually accessed Soul of the Ultimate Nation (SUN) during the period indicated.
- (2) As of the end of the period.
- (3) The spike in number of internet cafe accounts and subscribers in the second quarter of 2009 can be attributed to the SUN being offered through game portals such as Hangame.

Overseas markets. In China, we license our game to GameNow and conduct our business through 9Webzen, Ltd. (“9Webzen”), a Hong Kong company which we established with GameNow. GameNow, a wholly-owned subsidiary of The9, is an operator of a leading Chinese-language game website called The9.com and holds a 30% interest in 9Webzen. GameNow is a licensee of our game Soul of the Ultimate Nation (SUN) and it offers and distributes the game in China. GameNow, through its website The9.com, launched open beta testing of the Chinese version of Soul of the Ultimate Nation (SUN) in April 2007 and launched commercial service in May 2007. Our Soul of the Ultimate Nation (SUN) users in China pay GameNow when they buy at our in-game item shops various items for their characters, such as armor, weapons and potions, and the right to change the world or stage in which the end-user plays. We renewed GameNow’s exclusive license to publish and operate SUN in China. MU has been distributed in China through 9Webzen since 2002. We have licensed our MU online game to 9Webzen, based on a five-year license agreement we entered into in September 2002. The license agreement was extended on an annual basis after the original five-year term ended in September 2007. MU game users in China purchase online credits or prepaid cards to access the game. The operational results and financial position of 9Webzen have been consolidated with our financial statements since December 14, 2005, when we increased our interest in the company from 49% to 70%.

In Taiwan, Soul of the Ultimate Nation (SUN) was commercialized through our Taiwan subsidiary in April 2007 after a four-month beta testing period. Our Soul of the Ultimate Nation (SUN) users in Taiwan pay us when they buy at our in-game item shops various items for their characters, such as armor, weapons and potions, and the right to change the world or stage in which the end-user plays. We introduced MU in August 2002 through a license agreement with IGC, a content publishing company in Taiwan. In July 2004, our two-year agreement with IGC expired, and we decided to provide our online game services in Taiwan through a wholly-owned subsidiary, which we established in July 2004. We offer R2 through Webzen Taiwan under an agreement with NHN Games Corporation.

In 2007, we introduced microtransaction sales for MU service in Taiwan and China, and the end-users in those markets pay us for various items they buy for their characters at our in-game item shops, in addition to the subscription fee.

In Japan, we entered into a three-year term licensing agreement with GameOn, for Soul of the Ultimate Nation (SUN) in October 2007. Soul of the Ultimate Nation (SUN) went through closed beta testing in

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February 2008 and open beta testing in March 2008 and was commercialized in April 2008. MU has been distributed in Japan by GameOn since February 2003. From GameOn, we received one-time licensing fees when we entered into the license agreements. GameOn receives microtransaction payments from MU and Soul of the Ultimate Nation (SUN) users in Japan, and we receive a certain percentage of the revenue generated in Japan as a royalty fee.

In other overseas markets, we licensed MU to game developers and operators such as New Era Online Co., Ltd. in Thailand (June 2003), Digital Media Exchange, Inc. in the Philippines (May 2004) and FPT Communications in Vietnam (May 2005). In each case, we agreed to receive a certain percentage of the revenue generated in each market as a royalty fee for licensing MU. The terms are usually two years and renewable. From Digital Media Exchange and FPT Communications, we received installation fees for setting up the game servers. In Thailand, the licensing agreement with New Era Online Co., Ltd. ended in June 2006, and we did not renew the contract.

In December 2005, we entered into a three-year licensing agreement with K2 for the licensing of a MU global server. The global server provides MU service in countries where we have no exclusive licensing agreements. We received an initial installation fee for setting up the game servers and have received a certain percentage of the revenue as a royalty fee. In January 2007, we extended the global server licensing agreement for two more years. In April 2009, the extended term of the global server licensing agreement expired, and we began directly operating the MU global server starting from May 2009. In August 2009, we began offering MU globally through webzen.com, a portal website jointly operated with NHN Games, through which SUN is also being offered since October 2009.

The following table presents the royalty revenue generated from MU distributors in overseas market since 2008:

| | 2008 | | | | 2009 | | | | 2010 |
|---------------------------------------|----------------------|-----|-----|-----|------|-----|-----|-----|------|
| | 1Q | 2Q | 3Q | 4Q | 1Q | 2Q | 3Q | 4Q | 1Q |
| | (in millions of Won) | | | | | | | | |
| Revenues from MU⁽¹⁾ | | | | | | | | | |
| Japan | 508 | 461 | 523 | 751 | 750 | 616 | 485 | 475 | 445 |
| Philippines | 43 | 29 | 29 | 31 | 25 | 20 | 17 | 28 | 26 |
| Vietnam | 36 | 43 | 102 | 98 | 221 | 63 | 74 | 63 | 65 |
| U.S. | 104 | 93 | 113 | 133 | 142 | 50 | — | — | — |

(1) Includes royalty revenue for licensing and installation fee.

The following table presents the royalty revenue generated from the Soul of the Ultimate Nation (SUN) distributors in overseas market since 2008:

| | 2008 | | | | 2009 | | | | 2010 |
|---|----------------------|-------|-------|-------|-------|-------|-----|-------|------|
| | 1Q | 2Q | 3Q | 4Q | 1Q | 2Q | 3Q | 4Q | 1Q |
| | (in millions of Won) | | | | | | | | |
| Revenue from Soul of the Ultimate Nation (SUN)⁽¹⁾ | | | | | | | | | |
| China | 1,158 | 1,349 | 1,459 | 1,281 | 1,000 | 584 | 796 | 697 | 631 |
| Japan | — | 483 | 484 | 984 | 1,552 | 1,312 | 717 | 1,090 | 869 |
| U.S. | — | — | — | — | — | — | — | 64 | 62 |

(1) Includes royalty revenue for the licensing and installation fee.

Seasonality

Usage of our online games has typically increased around the New Year and other Korean holidays, in particular during winter and summer school holidays. See “Item 3. Key Information — 3.D. Risk Factors” for a description of other factors that affect the demand for our games.

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Marketing

We have engaged independent promotional agents to promote our online games to Internet cafes in Korea. We grant each promotional agent exclusive rights to promote our online games within a specified area and pay a monthly commission based on the revenue generated from Internet cafes in the allocated area. We also conduct a variety of marketing programs and online events to target potential subscribers accessing the Internet from home. Our main marketing efforts include:

- advertising on website portals and in online game magazines;
- conducting online promotional events;
- forming alliances with Internet service providers.

In 2005 and 2006, we participated in the Electronic Entertainment Expo, or E3, held in Los Angeles. Since 2007, however, we decided not to participate in E3 after reassessing the marketing impact and as part of our cost-cutting measures. In 2009, our marketing activities were primarily conducted in Korea. Our advertising and promotion expenses were ₩2,271 million, ₩3,824 million and ₩735 million (US\$632 thousand) in 2007, 2008 and 2009, respectively.

Our marketing activities in China are managed through The9 Computer Technology Consultation Co., Ltd., and marketing activities in Taiwan are conducted by Webzen Taiwan. Marketing activities in Japan, the Philippines and Vietnam are primarily conducted by our licensees and consist of advertising on website portals and in online game magazines and conducting online promotional events.

Information Technology

In connection with deploying our games in Korea, we have designed and assembled a flexible and reliable game server and information systems network. Our distributors in China, Japan, the Philippines and Vietnam have separate game servers and information system networks modeled on our system architecture in Korea.

In order to provide MU online game service in foreign markets where we do not have a distributor, we established in September 2003 a “global server” network in our office in Korea. Through this server, users in countries in which we did not have a presence could download for free a reduced version of MU. On December 1, 2005, we licensed the operation of this global server to K2. In April 2009, the term of the global server licensing agreement expired. In July 2009, we launched our global game portal webzen.com, which is jointly operated with NHN Games. In August 2009, we began offering MU on webzen.com and plan to offer other games in the second half of 2010.

Competition

We believe that the principal competitive factors in the online game industry are the ability to consistently attract creative game developers and offer new online games, maintain a high-quality network and implement innovative and effective sales and marketing campaigns.

Korea. Our primary subscription-based online game competitors in the Korean market are NCsoft, Neowiz, Nexon, NHN, CJ Internet, Hanbit Soft and Blizzard Entertainment. In 2010, the industry has launched or is expecting the launch of several additional online game titles in the Korean market, such as Bluehole Studio’s Terra. The new releases of high-quality game will increase competition in our industry.

China. Our primary online game competitors in China are Shanda’s *Yong Heng Zhi Ta* (Aion developed by NCsoft), Netease’s *World of WarCraft*, Tencent’s *Dungeon and Fighter* and *Cross Fire*, 9you’s *Audition*, Giant’s *Zheng Tu* and *Giant Online*, and Wanmei’s *Perfect World*.

Japan. Our primary online game competitors in Japan are GungHo’s *Ragnarok*, NCsoft Japan’s *Lineage II*, Square Enix’s *Final Fantasy Online*, YNK Japan’s *ROHAN* and Game On’s *RED STONE*. To date, Japan’s game

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market still has been primarily driven by console games, although online games are gaining popularity among Japanese game users as broadband access becomes more widely available.

North America and Western Europe. Our primary online game competitors in the North America and Western Europe are: Blizzard Entertainment's *World of Warcraft*, Mythic Entertainment's *Warhammer Online*, *Dark Age of Camelot* and *Ultima Online*, Sony Online Entertainment's *PlanetSide*, Turbine's *Lord of the Rings Online* and Eidos' *Age of Conan*. Webzen's massively-multiplayer online first person shooting game title, *Huxley: The Distopia* (published by NHN USA) targets to compete with not only MMORPGs but also first person shooting games such as *Halo 3*.

In all of these markets, we also compete against PC-based game developers producing popular PC-packaged games, including Electronic Arts, Take Two Interactive Software, Activision, THQ and Midway Games, Inc., and against game console manufacturers such as Microsoft (which produces Xbox), Sony (which produces Playstation) and Nintendo (which produces Wii). Microsoft, Sony and Nintendo are providing Internet online game services with their consoles, Xbox 360, Playstation 3 and Nintendo Wii, respectively.

Intellectual Property

We require all key personnel engaged in technological research and development capacities to sign agreements that subordinate our exclusive right to those works and to transfer any ownership claim that they may have in those works to us.

In Korea, we own two patents relating to data transmission over the Internet for online games, obtained program registration for our games and own service marks. In other countries, we registered some of our service marks and plan to apply for the registration of our other intellectual properties. We will take legal action in any jurisdiction where we believe our intellectual property rights have been infringed.

Insurance

We maintain medical and accident insurance for our employees to the extent required under Korean law, and we are insured against fire with respect to our facilities in Korea. In addition, we maintain directors' and officers' liability insurance policies covering potential liabilities of our Directors and officers.

Laws and Regulations

Korea. The Korean game industry is subject to comprehensive regulation by the Ministry of Culture, Sports and Tourism ("MCST"), which is responsible for establishing policies for the industry under the Act on Promotion of Game Industry. As an online game company operating in Korea, we are also subject to:

- regulation by the Ministry of Knowledge Economy ("MKE"), which is responsible for setting industrial, trade, resource and energy policies;
- regulation by the Korea Communications Commission ("KCC"), under the Telecommunication Business Act and the Protection of Communication Secrets Act
- regulation by the KCC and the Ministry of Public Administration and Security under the Act on Promotion of Information and Communications Network Utilization and Information Protection;
- regulation by the Fair Trade Commission under the Act on Consumer Protection for Transactions through Electronic Commerce;
- regulation by the MCST under the Copyright Act, the Computer Program Protection Act and the Online Digital Contents Business Development Act;
- regulation by the Game Rating Board under the Act on Promotion of Game Industry; and
- regulation by the Ministry for Health, Welfare and Family Affairs under the Juvenile Protection Act.

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Ratings regulation. Businesses manufacturing or importing games for the purpose of distributing or providing games in Korea must obtain game ratings in advance from the Game Rating Board. Online games are generally divided into four ratings categories: “suitable for users of all ages,” “suitable for users over 12 years of age,” “suitable for users over 15 years of age” and “suitable for users over 18 years of age.” Soul of the Ultimate Nation (SUN) has been rated “suitable for users over 18 years of age.” Our standard player-versus-player (“PVP”) version of the MU online game, which allows players to kill other players’ characters, has been rated “suitable for users over 18 years of age.” We also offer a non-player-versus-player (“non-PVP”) version of MU, which allows players to kill only non-player characters, which has been rated “suitable for users over 15 years of age” in Korea. Our Huxley online game has recently been rated “suitable for users over 15 years of age.”

Value-added communications business regulation. Under the Telecommunications Business Act we are classified as a value-added service provider and are required to make periodic reports to the MKE and report any transfer, takeover, suspension or closing of our business activities. The MKE 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.

Protection of interests of online game users under 20 years of age. Pursuant to Korea’s civil law, contracts entered into with persons under 20 years of age without parental consent may be invalidated. Under the Telecommunication Framework Act, telecommunication service providers are also required to take certain steps to protect the rights of telecommunication service users. As a result, telecommunication service contracts and online game user agreements are required to set forth specific procedures for rescinding service contracts, which may be entered into by persons under 20 years of age without parental consent. Also, under the Promotion of Information and Communications Network Utilization and Information Protection Act, the operator of a website should monitor and delete any content harmful to minors.

Protection of consumer information for electronic settlement services. Under the Act on Consumer Protection for Transactions on Electronic Commerce, we are required to take 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 the misappropriation of consumer information by third parties.

We believe that we have instituted appropriate safety measures to protect against data misappropriation. To date, we have not experienced material disputes or claims in this area.

Protection of personal information for users of information and communications services. Under the Act on Promotion of Information and Communications Network Utilization and Information Protection, we are permitted to gather personal information relating to our subscribers within the scope of their consents. We are, however, generally prohibited from utilizing 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 if:

- it is necessary for the settlement of service charges;
- the personal information is processed so that the specific individual is unidentified and is provided for compiling statistics, academic research or surveys; or
- it is otherwise permitted by laws and regulations.

We are required to indemnify users for damages occurring as a result of our violation of the foregoing restrictions, unless we can prove an 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.

Taxation. Under the Special Tax Treatment Control Law, we may claim a tax credit that can be carried forward for five years. In 2007 and 2008, we realized net losses, which were claimed for carried forward tax credit and in 2009, we posted a net profit. The statutory tax rate applied to us was 27.5% in 2007 and 2008, and 24.2% in 2009. Due to the amendment to the Korea corporate income tax law, the rate of 24.2% will be applied for the fiscal years

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from 2009 through 2011 and 22% for the fiscal year 2012 and thereafter. Our deferred income taxes as of December 31, 2009 were calculated based on the rate of 24.2% for fiscal years 2010 and 2011 and 22% thereafter for the amounts expected to be realized during the relevant fiscal year.

China. The online games industry in China operates under a legal regime that consists of the State Council (especially, the State Council Information Office), which is the highest authority of the executive branch of the PRC central government, and the various ministries and agencies under its leadership. These ministries and agencies include the Ministry of Industry and Information Technology; the Ministry of Culture; the Ministry of Public Security; the State Administration of Industry and Commerce; and the General Administration of Press and Publications. The State Council and these ministries and agencies have issued a series of rules that regulate a number of different substantive areas of our business, including, among others, foreign ownership restrictions, Internet content provider licenses and regulation of Internet content. See “Item 3. Key Information — 3.D. Risk Factors — Risks Related to Our Business — Foreign operations are subject to different business, political and economic risks.”

4.C. Organization

As of December 31, 2009, Webzen Taiwan was our only significant wholly-owned subsidiary. We ceased the operation of Webzen America and Webzen China in 2008. We also own 55.4% of the common shares of Flux, Inc., a privately held wireless game developer, and 70% of 9Webzen, a joint venture with GameNow.

4.D. Property, Plant and Equipment

Because our main business is to provide online game services to our clients, we do not own any factories or facilities that manufacture products. There are no factories currently under construction, and we have no plans to build any factories in the future.

Korea. Our principal executive and administrative offices are located at the 14th Floor, Daerung Post Tower 2nd, 182-13 Guro-Dong, Guro-Gu, Seoul, Korea 152-790. We currently lease 60,449 square feet. The latest of our leases expires in December 2011.

Taiwan. The offices of Webzen Taiwan are located at 7F-3, No.176, Jian 1st Rd., Zhonghe City, Taipei County, Taiwan 23553, Republic of China.

We believe that our existing facilities are adequate for our current requirements and that additional space can be obtained on commercially reasonable terms to meet our future requirements.

Item 4A. Unresolved Staff Comments

There are no unresolved outstanding comments.

Item 5. Operating and Financial Review and Prospects

5.A. Operating Results

The following discussion and analysis provides information that management believes to be relevant to understanding our consolidated financial condition and results of operations. This discussion should be read in conjunction with the consolidated financial statements of Webzen, including the notes thereto included in this Annual Report. See “Item 18. Financial Statements.”

Overview

We are a developer and distributor of online games. Our total net revenues, which include online game subscription, microtransaction sales, royalties and license fees and service fees, were ₩32,776 million and ₩31,395 million (US\$26,979 thousand) in 2008 and 2009, respectively. Substantially all of our revenue come from our two online games, MU and Soul of the Ultimate Nation (SUN). With MU approaching the end of its life cycle in most of its markets and with

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intensifying competition due to the introduction of new games by competitors, we expect a decline in revenues generated from MU going forward.

In our overseas market, where we have licensed MU and/or Soul of the Ultimate Nation (SUN) to licensees, we recorded royalties from Japan, China, Vietnam, the U.S. and the Philippines in the amounts of ₩6,996 million (US\$6,012 thousand), ₩3,077 million (US\$ 2,644 thousand), ₩421 million (US\$362 thousand), ₩256 million (US\$220 thousand) and ₩90 million (US\$77 thousand), respectively, in 2009.

Our cost of revenues increased in 2009 to ₩15,634 million (US\$13,435 thousand) from ₩15,102 million in 2008 mainly due to expansion of service revenue. Our operating expenses, which includes selling, general and administrative expenses, research and development expenses and impairment charges, significantly decreased in 2009 to ₩15,988 million (US\$13,739 thousand) from ₩26,911 million in 2008 as we implemented a series of cost-cutting measures. We posted a net income attributable to parent company of ₩3,309 million (US\$2,844 thousand) in 2009 compared to a net loss attributable to parent company of ₩7,675 million in 2008.

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 accounting principles generally accepted in the United States. The preparation of these financial statements requires management to make estimates, judgements and assumptions that affect the reported amounts of assets and liabilities, contingent assets and 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 fees paid by our MU subscribers, royalties and license fees paid by our licensees and sales of game items to Soul of the Ultimate Nation (SUN) subscribers. We recognize revenue in accordance with accounting principles generally accepted in the United States, as set forth in Accounting Standard Codification (“ASC”) 605, *Revenue Recognition* (formerly referenced as SEC Staff Accounting Bulletin No. 104, *Revenue Recognition*, Statement of Position 97-2, *Software Revenue Recognition*) and other related pronouncements. Our current revenues can be classified into the following categories:

Online subscription fees. Subscription fees are fees we directly collect from client terminal level end-users. Our revenues from our operations in Korea consist mostly of prepaid subscription fees paid by individual PC accounts and Internet cafe subscribers, accounting for ₩13,041 million (US\$11,207 thousand) and ₩2,100 million (US\$1,805 thousand), respectively, in 2009. Online subscription fees earned by our consolidated subsidiaries, which recorded ₩1,669 million (US\$1,434 thousand) from 9Webzen and ₩3,022 million (US\$2,597 thousand) from Webzen Taiwan in 2009, are also included in this item.

Microtransaction sales. Microtransaction sales are fees we collect from in-game item sales for the online game Soul of the Ultimate Nation (SUN), which was commercialized in Korea in the fourth quarter of 2006, in Taiwan and China in the second quarter of 2007 and in Japan in the second quarter of 2008. The microtransaction sales model is also utilized in the MU online game in Japan, China and Taiwan. We recently incorporated the same business model to MU by offering MU Blue. Under this model, players purchase points for in-game premium features. Microtransaction sales are typically paid by credit card or charged to the users’ mobile phone bills. These

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payments are deferred when received and the relevant revenues are recognized over the life of the premium features or as the premium features are consumed. Under our micro-transaction sales model, or item-based revenue model, game players can access our games free of charge or for a low membership fee, but may purchase consumable virtual items, including those with a predetermined expiration time, such as three months, or perpetual items, such as certain costumes that stay binded to a game player for the life of the game. Revenues in relation to consumable virtual items are recognized as they are consumed, as our services in connection with these items have been fully rendered to our game players as of that time. Revenues in relation to perpetual virtual items are recognized over their estimated lives. We will provide continuous online game services in connection with these perpetual virtual items until they are no longer used by our game players. We have considered the average period that game players typically play our games and other game player behavior patterns to arrive at our best estimates for the lives of these perpetual virtual items.

One-time license fee. In certain cases, we receive a one-time license fee from licensees after we enter into a licensing agreement. License fees are deferred and recognized as revenue over the licensing period. When we receive a one-time license fee, we generally provide our licensees with minimal post-contract customer support on our software products, consisting of access to a support hotline and occasional unspecified upgrades or game enhancements, which typically occur within one year of the beginning of the licensing agreements. The estimated costs of providing such support are insignificant and sufficient vendor-specific evidence does not exist to allocate the revenue from software and related integration projects to the separate elements of such projects. As a result, all of our licensing revenue is recognized ratably over the life of the agreement.

Installation fee. In connection with certain overseas licensing agreements, we receive a one-time installation fee in lieu of a licensing fee as we install game servers and information systems networks for our licensees. The system and network we use for our licensees are modeled after our system in Korea. As there are no sufficient vendor-specific information to allocate the revenue between installation service and other services, we recognize installation fees as revenue ratably over the life of the agreements.

Royalty revenues. We receive royalty revenues from our licensees based on agreed percentage of the licensees' revenue. Royalty revenues are recognized on a monthly basis after the licensees confirm their revenues based on the actual number of hours of services sold during the prior month. Royalty revenues generated from our consolidated subsidiaries, such as 9Webzen or Webzen Taiwan, are eliminated during the consolidation process and are not included in this item. Royalty revenues from foreign licensees accounted for 28.9% of our total net revenues in 2009. The following table sets forth our royalty revenues from each of our overseas licensees for the periods indicated.

| | 2008 | | | | 2009 | | | |
|-------------------------|----------------------|-------|-------|-------|-------|-------|-------|-------|
| | 1Q | 2Q | 3Q | 4Q | 1Q | 2Q | 3Q | 4Q |
| | (in millions of Won) | | | | | | | |
| Royalty revenues | | | | | | | | |
| China(1) | 840 | 1,031 | 1,138 | 959 | 685 | 266 | 475 | 376 |
| Japan(2) | 497 | 870 | 911 | 1,640 | 2,209 | 1,833 | 1,107 | 1,470 |
| Philippines | 43 | 29 | 29 | 31 | 25 | 20 | 17 | 28 |
| Vietnam | 13 | 19 | 78 | 74 | 198 | 54 | 74 | 63 |
| U.S. | 64 | 52 | 71 | 92 | 102 | 35 | - | 36 |

- (1) Since we increased our interest in 9Webzen from 49% to 70% and 9Webzen became a consolidated subsidiary in December 14, 2005, revenues for MU in China are no longer recognized as royalty revenues, but are recorded under online subscriptions fees. Royalty revenues from China in this table refer only to royalty fees we receive from GameNow.net Ltd., the operator of Soul of the Ultimate Nation (SUN) in China.
- (2) Running royalty of Japan at 1Q 2009 include incentive in relation to revenue goal achievement.

Service revenues. In connection with certain leasing and business agency agreements, we received ₩717 million (US\$616 thousand) for service rendered in 2009. We had no such revenue in 2008. Under the lease agreement with nPluto Co., Ltd., an online game developer, we agreed to provide our internet data centers and servers for ₩82 million. We also

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received ₩93 million per month from NHN Games under the business agency agreement dated June 8, 2009 in return for providing strategy formulation, marketing, publishing and other general corporate support functions. Service revenues accounted for 2.3% of our total net revenues in 2009. Revenue from services is recognized on a monthly basis when the services have been rendered in accordance with the contract.

Allowances for doubtful accounts

We maintain allowances for doubtful accounts receivable for estimated losses that result from the inability of our customers to make required payments. We base our allowances on the likelihood of recoverability of accounts receivable which is based on past experience and current collection trends. Allowances for accounts receivable generally arise when individual PC account subscribers who elect to make their payments through their fixed-line or mobile phone service provider fail to make such payments. We record allowances for doubtful accounts based on the historical payment patterns of our overall subscribers and increase our allowances as the length of time after which such receivables become past due increases.

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* (formerly referenced as the Financial Accounting Standards Board (“FASB”) Statement of Financial Accounting Standards (“SFAS”) No. 86, *Accounting for the Costs of Computer Software to be Sold, Leased, or Otherwise Marketed*). Software development costs incurred prior to the establishment of technological feasibility are expensed when incurred and treated as research and development expenses. Once a software product, such as an online game, has reached technological feasibility, then all subsequent software development costs for that product are capitalized and the capitalization stops when the game is available for general release to customers. Technological feasibility is evaluated on a product-by-product basis but typically occurs once the online game has a proven ability to operate on a massively-multiplayer level. After an online game is available for general release to customers, the capitalized product development costs are amortized based on the expected life of the game. This amortized 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 that are cancelled are expensed in the period of cancellation. In addition, a charge to cost of revenues 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 Investments

Our investments in equity securities are comprised of investments in the common shares of NeoWave Inc. (“NeoWave”) and GameOn. If it has been determined that an investment has sustained an other-than-temporary decline in its value, the investment is written down to its fair value by taking a charge to earnings. We regularly evaluate our investments to identify other-than-temporary impairments of individual securities. We consider the following factors in determining whether an other-than-temporary decline in value has occurred: the length of time and extent to which the market value of the security has been less than its original cost, the financial condition, operating results, business plans, milestones and estimated future cash flows of the investee, and other specific factors affecting the market value. We have evaluated our investment in the common shares of NeoWave and GameOn. Our investment in the common shares of NeoWave was recorded as an impairment loss as we concluded that the current fair market value of the common shares of NeoWave was significantly less than the original cost or the carrying value before valuation and concluded that it was unlikely to recover the original cost or the carrying value before valuation of the NeoWave investment at any time in the foreseeable future. The impairment loss reflected in our statements of operations was ₩3,883 million and ₩483 million (US\$415 thousand) in 2008 and 2009, respectively. Significant

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management judgment is involved in evaluating whether there is an impairment. Any changes in assumptions could significantly affect the valuation and timing of recognition of impairment losses.

Fair value measurement on financial instruments

We adopted ASC 825, *Financial Instruments* (formerly referenced as the FASB's SFAS No. 159, *The Fair Value Option for Financial Assets and Financial Liabilities*). We have elected the fair value option for two of its investments in short-term available-for-sale securities that were acquired during the year ended December 31, 2008 and three of such investment that were acquired during the year ended December 31, 2009, respectively. Under the fair value option, unrealized gains and losses related to this investment are reflected in the consolidated statements of operations for the years ended December 31, 2008 and 2009.

The current investment in beneficiary certificates represents equity interests in a fund that is comprised of bonds, marketable equity securities and trust funds as of December 31, 2008 and 2009. The fair value of bonds is derived based on quoted prices in active markets, the fair value of marketable securities is derived based on quoted prices in active exchange markets and the fair value of trust funds is derived based on quoted prices in markets that are not active or other inputs that are observable. We have invested in multiple beneficiary certificates. Two and three of these beneficiary certificates contain embedded derivatives as of December 31, 2008 and 2009, respectively. We have determined that it is not practical to bifurcate the embedded derivatives and account for separately. Pursuant to ASC 825, we have elected the fair value option to account for these two and three securities as of December 31, 2008 and 2009, respectively. Accordingly, the entire change in estimated fair value of the two and three beneficiary certificates that contain embedded derivatives is included in other expense on the consolidated statement of operations for the years ended December 31, 2008 and 2009.

Income taxes

We account for income taxes under the provisions of ASC 740, *Income Taxes* (formerly referenced as the FASB's SFAS No. 109, *Accounting for Income Taxes*), Accounting for Income Taxes. Under SFAS No. 109, 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 recognized. Deferred taxes are determined based upon differences between the financial reporting and tax bases of assets and liabilities and carryforwards at currently applicable statutory tax rates for the years in which the differences are expected to be reversed and carryforwards are expected to be realized.

A valuation allowance is provided on deferred tax assets to the extent that it is more likely than not that such deferred tax assets will not be realized. The total income tax provision includes current tax expenses under applicable tax regulations and the change in the balance of deferred tax assets and liabilities.

Deferred income tax assets are recognized only to the extent that realization of the related tax benefit is more likely than not to occur. Realization of the 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 Korean economic environment, and the overall future industry outlook.

As of December 31, 2009, we have concluded that net deferred tax assets of Webzen and its subsidiaries will not be realized in the near future based on our historical and projected net and taxable income.

Under the Special Tax Treatment Control Law, we may claim a tax credit that can be carried forward for five years. In 2007 and 2008, we realized net losses, which were claimed for carried forward tax credit and in 2009, we posted a net profit. The statutory tax rate applied to us was 27.5% in 2007 and 2008, and 24.2% in 2009. Due to the amendment to the Korea corporate income tax law, the rate of 24.2% will be applied for the fiscal years from 2009 through 2011 and 22% for the fiscal year 2012 and thereafter. Our deferred income taxes as of December 31, 2009 were calculated based on the rate of 24.2% for fiscal years 2010 and 2011 and 22% thereafter for the amounts expected to be realized during the relevant fiscal year.

In addition, beginning January 1, 2007, we account for uncertainties related to income taxes in compliance with ASC 740, *Income Taxes* (formerly referenced as FIN 48, "Accounting for Income Tax Uncertainties.") Under ASC

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740, we evaluate our tax positions taken or expected to be taken in a tax return for recognition and measurement on our financial statements. Only those tax positions that meet the more likely than not threshold are recognized on the financial statements at the largest amount of benefit that is a greater than 50 percent likely of ultimately being realized. The Company did not have any unrecognized tax benefits at December 31, 2007 and there have been no changes during the years ended December 31, 2008 and 2009.

Recent Accounting Pronouncements

In January 2010, the FASB issued Accounting Standards Update 2010-06 (ASU 2010-06), which amends the disclosure requirements of ASC 820, *Fair Value Measurements and Disclosures*, as of January 1, 2010. ASU 2010-06 requires new disclosures for any transfers of fair value into and out of Level 1 and 2 fair value measurements and separate presentation of purchases, sales, issuances and settlements within the reconciliation of Level 3 unobservable inputs. We previously adopted ASC 820 on January 1, 2008 and January 1, 2009 for financial assets and liabilities and for nonfinancial assets and liabilities, respectively. ASU 2010-06 is effective for annual and interim periods beginning after December 15, 2009, except for the Level 3 reconciliation which is effective for annual and interim periods beginning after December 15, 2010. The adoption of ASU 2010-06 as of January 1, 2010 did not have a material effect on our financial condition or results of operations. We do not expect the adoption of ASU 2010-06 in relation to the Level 3 reconciliation to have a material impact on the Company's financial condition or results of operations.

In September 2009, the Emerging Issues Task Force (the "EITF") reached final consensus under ASU No. 2009-13 on the issue related to revenue arrangements with multiple deliverables. This issue addresses how to determine whether an arrangement involving multiple deliverables contains more than one unit of accounting and how arrangement consideration should be measured and allocated to the separate units of accounting. This issue is effective for our revenue arrangements entered into or materially modified on or after January 1, 2011. We will evaluate the impact of this issue on our financial statements when reviewing its new or materially modified revenue arrangements with multiple deliverables when it becomes applicable.

In June 2009, the FASB issued a statement which improves financial reporting by enterprises involved with variable interest entities. This statement requires companies to perform an analysis to determine whether the company's variable interest or interests give it a controlling financial interest in a variable interest entity. This statement will be effective as of the beginning of the annual reporting period that begins after November 15, 2009. We will evaluate the impact of this statement on our financial statements when reviewing any new variable interest entities or transactions when it becomes applicable.

In June 2009, the FASB issued a statement which improves the relevance, representational faithfulness, and comparability of the information that a reporting entity provides in its financial statements about a transfer of financial assets as well as the effects of a transfer on its financial position, financial performance, and cash flows and a transferor's continuing involvement, if any, in transferred financial assets. The statement requires that a transferor recognize and initially measure at fair value all assets obtained (including a transferor's beneficial interest) and liabilities incurred as a result of a transfer of financial assets accounted for as a sale. The statement will be effective as of the beginning of annual reporting period that begins after November 15, 2009. We believe the adoption of this pronouncement will not have a material impact on our financial statements as we have not transferred our financial assets.

[Table of Contents](#)**Results of Operations****2009 compared to 2008**

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

| | For the year ended December 31, | | |
|--|---|----------------|-----------------|
| | 2008 | 2009 | 2009(1) |
| | (in millions of Won and thousands of US\$) | | |
| | (unaudited) | | |
| Online game subscriptions | ₩ 22,478 | ₩ 19,833 | \$ 17,043 |
| Royalties and license fees | 10,298 | 10,845 | 9,320 |
| Service fees | — | 717 | 616 |
| Total net revenues | <u>32,776</u> | <u>31,395</u> | <u>26,979</u> |
| Cost of revenues | <u>15,102</u> | <u>15,634</u> | <u>13,435</u> |
| Gross profit | 17,674 | 15,761 | 13,544 |
| Selling, general and administrative expenses | 24,590 | 13,761 | 11,825 |
| Research and development expenses | 1,816 | 2,227 | 1,914 |
| Impairment charges | 505 | — | — |
| Operating loss | (9,237) | (227) | (195) |
| Interest income | 3,364 | 2,232 | 1,919 |
| Foreign currency gain (loss), net | 3,210 | (148) | (127) |
| Gain (loss) on disposal of property and equipment | — | 935 | 804 |
| Gain (loss) on disposal of available-for-sale securities | 34 | 212 | 182 |
| Gain (loss) on valuation of available-for-sale securities under ASC825 | (671) | 986 | 848 |
| Loss on impairment of available-for-sale securities | (3,883) | (483) | (415) |
| Others, net | 156 | 938 | 804 |
| Income (loss) before income tax expenses | (7,027) | 4,445 | 3,820 |
| Income tax expenses | 802 | 1,055 | 907 |
| Net income (loss) | (7,829) | 3,390 | 2,913 |
| Net income (loss) attributable to non-controlling interest | (154) | 81 | 69 |
| Net income (loss) attributable to parent company | <u>₩ (7,675)</u> | <u>₩ 3,309</u> | <u>\$ 2,844</u> |

(1) For convenience, the Won amounts are expressed in U.S. dollars at the rate of ₩1,163.65 to US\$1.00, the noon buying rate in effect on December 31, 2009, as announced by the Federal Reserve Bank of New York.

The following table summarizes our results of operations as a percentage of our total net revenues for the periods indicated.

| | For the year ended | |
|--|--|---------------|
| | December 31, | |
| | 2008 | 2009 |
| | (as a percentage of total net revenues) | |
| Online game subscriptions | 68.6% | 63.2% |
| Royalties and license fees | 31.4% | 34.5% |
| Service fees | 0.0% | 2.3% |
| Total net revenues | <u>100.0%</u> | <u>100.0%</u> |
| Cost of revenues | 46.1% | 49.8% |
| Gross profit | <u>53.9%</u> | <u>50.2%</u> |
| Selling, general and administrative expenses | 75.0% | 43.8% |
| Research and development expenses | 5.5% | 7.1% |
| Impairment charges | 1.5% | 0.0% |
| Operating loss | (28.2%) | (0.7%) |
| Interest income | 10.3% | 7.1% |
| Foreign currency gain (loss), net | 9.8% | (0.5%) |
| Gain (loss) on disposal of property and equipment | 0.0% | 3.0% |
| Gain (loss) on disposal of available-for-sale securities | 0.1% | 0.7% |
| Gain (loss) on valuation of available-for-sale securities under ASC825 | (2.0%) | 3.1% |
| Loss on impairment of available-for-sale securities | (11.8%) | (1.5%) |

| | | |
|--|----------------|--------------|
| Others, net | <u>0.5%</u> | <u>3.0%</u> |
| Income (loss) before income tax expenses | (21.4%) | 14.2% |
| Income tax expenses | <u>2.4%</u> | <u>3.4%</u> |
| Net income (loss) | (23.9%) | 10.8% |
| Net income (loss) attributable to non-controlling interest | <u>(0.5%)</u> | <u>0.3%</u> |
| Net income (loss) attributable to parent company | <u>(23.4%)</u> | <u>10.5%</u> |

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Revenues. Our net revenues decreased 4.2% from ₩32,776 million in 2008 to ₩31,395 (US\$26,979 thousand) million in 2009 mainly due to a 11.8% decrease in online subscription revenue of MU and SUN, and related PC cafe revenue. This decrease in revenue can be explained by migration of subscribers to newly published games of our competitors. This decrease in online subscription revenue was partially offset by 5.3% increase in royalties and license fees from ₩10,298 million in 2008 to ₩10,845 million (US\$9,320 thousand) in 2009, mainly as a result of increased revenues from the Japan and Vietnam. This decrease in online subscription revenue was also partially offset by service revenue of ₩717 million (US\$616 thousand), mainly as a result of providing marketing and logistical support to NHN Games.

Cost of revenues. Our cost of revenues increased 3.5% from ₩15,102 million in 2008 to ₩15,634 million (US\$13,435 thousand) in 2009, primarily due to:

- a 11.1% increase in wages, bonuses and employee benefits from ₩6,924 million in 2008 to ₩7,691 million (US\$6,609 thousand) in 2009, mainly due to an increase in the number of employees in revenue generating departments, mostly in the service department, an increase in incentive payments and additional costs associated with benefits such as health insurance premiums;
- a 82.1% increase in fees and service charges from ₩770 million in 2008 to ₩1,401 million (US\$1,204 thousand) in 2009, mainly due to an increase in outsourcing of customer service personnel and content delivery network service fees for SUN global portal; and
- an additional cost of ₩589 million (US\$506 thousand) associated with service revenue, which we did not incur in 2008.

These increases in cost of revenue were partially offset by

- a 15.1% decrease in Internet Data Center (“IDC”) expense from ₩591 million in 2008 to ₩502 million (US\$431 thousand) in 2009, mainly due to a decrease in IDC usage associated with the decrease in revenue generated from MU through 9Webzen;
- a 85.3% decrease in cost of merchandise sold, from ₩68 million in 2008 to ₩10 million (US\$9 thousand) in 2009, due to a decrease in sales of character and packages related to game contents; and
- a decrease 21% in travel, entertainment and office supplies, from ₩72 million in 2008 to ₩57 million (US\$49 thousand) in 2009, due to cost cutting measures.

As a percentage of total net revenues, cost of revenues increased from 46.1% in 2008 to 49.8% in 2009.

Selling, general and administrative expenses. Selling, general and administrative expenses consist of sales commissions paid to independent promotional agents that target our Internet cafe subscribers in Korea, commissions paid to providers of settlement services, administrative expenses and related personnel expenses of executive and administrative staff, and marketing and promotional expenses and related personnel expenses. Selling, general and administrative expenses decreased 44% from ₩24,590 million in 2008 to ₩13,761 million (US\$11,825 thousand) in 2009, primarily due to:

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- a 36.4% decrease in cost associated with payroll, bonuses and employee benefits from ₩9,364 million in 2008 to ₩5,952 million (US\$5,115 thousand) in 2009, due to a decrease in number of general and administrative personnel by 17.7% compared to the prior year and the impact of general cost cutting measures;
- a 80.8% decrease in marketing expense from ₩3,824 million in 2008 to ₩735 million (US\$632 thousand) in 2009, due to a reduction in PC cafe related marketing material production and promotional activities associated with games; and
- a 48.1% decrease in fees and commissions from ₩5,504 million in 2008 to ₩2,857 million (US\$2,455 thousand) in 2009, mainly due to a decrease of commissions and fee payments to payment solution providers, which resulted from a decrease of online game subscription revenues, and not incurring M&A consulting related expenses as in 2008.

These decreases were partially offset by a 137.2% increase in stock compensation expense from ₩289 million in 2008 to ₩686 million (US\$590 thousand) in 2009, mainly due to an increase in stock compensation to certain members of the management and senior managers.

As a percentage of net revenues, selling, general and administrative expenses decreased from 75.0% in 2008 to 43.8% in 2009.

Research and development expenses. Research and development expenses incurred prior to the establishment of technological feasibility are included in this item. Research and development expenses in 2009 increased 22.7% from ₩1,816 million in 2008 to ₩2,227 million (US\$1,914 thousand) in 2009, mainly due to a one-time reimbursement of ₩12,309 million from Realtime Worlds Inc. (“RTW”) recorded as research and development income in 2008. Offsetting this was an 82.3% reduction in payroll, bonuses and retirement benefits from ₩2,551 million in 2008 to ₩453 million (US\$389 thousand) in 2009 resulting from cost-cutting measures as well as reduction in service charges of ₩9,166 million (US\$7,877 thousand) to Red 5 Studio regarding T-Project in 2008.

Impairment charges. We realized an impairment charge of ₩505 million in 2008, while there were no such charges in 2009. This impairment charge in 2008 was mainly due to the impairment of equipment, capitalized leasehold improvements and certain other assets of Webzen China and Webzen America as the two entities ceased to conduct activities generating revenue and the relevant assets had not alternative use.

Interest income. Our interest income is mainly generated from cash equivalents and short-term financial instruments and it has decreased by 33.7% from ₩3,364 million in 2008 to ₩2,232 million (US\$1,919 thousand) in 2009. This year's decrease in mainly due to a fall of average interest rates on these assets, despite the increase in balance of our interest-generating assets.

Foreign currency gain (loss), net. We incurred a net foreign currency loss of ₩148 million (US\$127 thousand) in 2009 compared to a net gain of ₩3,210 million in 2008. This was mainly due to a decrease in valuation of foreign currency denominated assets (including account receivables and long-term loans), as Korean Won appreciated against other major currencies including U.S. dollar in 2009.

Gain on disposal of property and equipment. We realized net gain on disposal of property and equipment of ₩935 million (US\$804 thousand) in 2009. The gain on disposal of property and equipment in 2009 was mainly due to the sale of office space at Daelim Acrotel Building in Dogok-dong, Seoul.

Gain on disposal of available-for-sale securities. Our gain on disposal of available-for-sale securities increased 523.5% from ₩34 million in 2008 to ₩212 million (US\$182 thousand) in 2009. The increase was mainly due to the gains we realized when we sold the common shares of GameOn, other beneficial certificates and other available-for-sale securities.

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Loss on impairment of available-for-sale securities. We realized loss from impairment of available-for-sale securities of ₩483 million (US\$415 thousand) in 2009 compared to ₩3,883 million in 2008. Our loss on impairment of available-for-sale securities in 2008 and 2009 was fully attributable to the loss in valuation of the common shares of NeoWave we hold. The original cost of investment in NeoWave's securities was ₩4,550 million when we acquired the securities in February 2008. We recorded loss on the investment in NeoWave securities of ₩3,883 million and ₩483 million (US\$415 thousand) in 2008 and 2009, respectively, which represents the difference between the value on our book and the fair market value at the relevant period end.

Others, net. Other income increased from ₩156 million in 2008 to ₩938 million (US\$804 thousand) in 2009, which was mainly attributable to ₩666 million (US\$572 thousand) of sub-lease income realized by Webzen America in 2009. We realized a gain of ₩159 million (US\$137 thousand) as a result of exemption of debt of 9Webzen in 2009. We also realized a loss of ₩106 million (US\$91 thousand) on valuation of derivatives product held by us in 2009 compared to a gain of ₩145 million in 2008, due to the reduction in NeoWave's share price.

Income taxes. Income tax expenses increased 31.5% from ₩802 million in 2008 to ₩1,055 million (US\$907 thousand) in 2009, mainly due to a ₩155 million (US\$133 thousand) increase of foreign withholding tax for overseas license and royalty revenue and to a ₩99 million (US\$85 thousand) increase of income tax expenses relating to the valuation allowance for unrealized gain on available-for-sale securities.

Net income (loss) attributable to non-controlling interest. Non-controlling interest represents the net income from 9Webzen, our 70%-held subsidiary, and Flux, our 55.4%-held subsidiary. Net income attributable to non-controlling interest increased from net loss of ₩154 million in 2008 to net income of ₩81 million (US\$69 thousand) in 2009, mainly due to net income of ₩80 million (US\$69 thousand) of the aforementioned subsidiaries in 2009 and net loss of ₩471 million of the aforementioned subsidiaries in 2008.

Net income (loss) attributable to parent company. As a result of the factors discussed above, we recorded a net income attributable to parent company of ₩3,309 million (US\$2,844 thousand) in 2009 compared to a net loss attributable to parent company of ₩7,675 million in 2008.

2008 compared to 2007

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

| | For the year ended December 31, | |
|---|--|---------------|
| | 2007 | 2008 |
| | (in millions of Won) | |
| Online game subscriptions | ₩ 22,884 | ₩ 22,478 |
| Royalties and license fees | 6,213 | 10,298 |
| Total net revenues | <u>29,097</u> | <u>32,776</u> |
| Cost of revenues | <u>17,505</u> | <u>15,102</u> |
| Gross profit | 11,592 | 17,674 |
| Selling, general and administrative expenses | 22,848 | 24,590 |
| Research and development expenses | 23,164 | 1,816 |
| Impairment charges | — | 505 |
| Operating loss | (34,420) | (9,237) |
| Interest income | 3,503 | 3,364 |
| Foreign currency gain (loss), net | 92 | 3,210 |
| Gain on disposal of property and equipment | 3,931 | — |
| Loss on valuation of available-for-sale securities under ASC825 | — | (671) |

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| | For the year ended December 31, | |
|---|--|-------------|
| | 2007 | 2008 |
| | (in millions of Won) | |
| Gain on disposal of available-for-sale securities | 3,755 | 34 |
| Loss on impairment of available-for-sale securities | — | (3,883) |
| Others, net | (118) | 156 |
| Loss before income tax expenses | (23,257) | (7,027) |
| Income tax expenses | 2,579 | 802 |
| Net loss | (25,836) | (7,829) |
| Net loss attributable to non-controlling interest | (242) | (154) |
| Net loss attributable to parent company | ₩ (25,594) | ₩ (7,675) |

The following table summarizes our results of operations as a percentage of our total net revenues for the periods indicated.

| | For the year ended | |
|---|---|-------------|
| | December 31, | |
| | 2007 | 2008 |
| | (as a percentage of total net revenues) | |
| Online game subscriptions | 78.6% | 68.6% |
| Royalties and license fees | 21.4% | 31.4% |
| Total net revenues | 100.0% | 100.0% |
| Cost of revenues | 60.2% | 46.1% |
| Gross profit | 39.8% | 53.9% |
| Selling, general and administrative expenses | 78.5% | 75.0% |
| Research and development expenses | 79.6% | 5.5% |
| Impairment charges | 0.0% | 1.5% |
| Operating loss | (118.3%) | (28.2%) |
| Interest income | 12.0% | 10.3% |
| Foreign currency gain (loss), net | 0.3% | 9.8% |
| Gain (loss) on disposal of property and equipment | 13.5% | 0.0% |
| Loss on valuation of available-for-sale securities under ASC825 | 0.0% | 2.0% |
| Gain on disposal of available-for-sale securities | 12.9% | 0.1% |
| Loss on impairment of available-for-sale securities | 0.0% | (11.8%) |
| Others, net | (0.4%) | (0.5%) |
| Income (loss) before income tax expenses | (79.9%) | (21.4%) |
| Income tax expenses | 8.9% | 2.4% |
| Net loss | (88.8%) | (23.9%) |
| Net loss attributable to non-controlling interest | 0.8% | 0.5% |
| Net loss attributable to parent company | (88.0%) | (23.4%) |

Revenues. Our net revenues increased 12.7% from ₩29,097 million in 2007 to ₩32,776 million in 2008 due to a 65.7% increase in royalties and license fees from ₩6,213 million in 2007 to ₩10,298 million in 2008 as royalties and license fees from Soul of the Ultimate Nation (SUN) increased from ₩3,287 million in 2007 to ₩7,197 million in 2008, mainly as a result of increased revenues from the PRC and commercialization of the game in Japan. This increase in royalties and license fees was partially offset by a 1.8% decrease in online game subscriptions from

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₩22,884 million in 2007 to ₩22,478 million in 2008 as online game subscription from Soul of the Ultimate Nation (SUN) and MU decreased during the period.

Cost of revenues. Our cost of revenues for 2008 decreased 13.7% from ₩17,505 million in 2007 to ₩15,102 million in 2008, primarily due to:

- a 14.3% decrease in wages and salaries, including severance benefits, from ₩8,231 million in 2007 to ₩7,055 million in 2008 as our workforce in the operation and maintenance division of MU and Soul of the Ultimate Nation (SUN) decreased by 19.8% as a part of our cost-cutting measures;
- a 23.4% decrease in depreciation from ₩3,131 million in 2007 to ₩2,397 million in 2008 as we disposed of equipments and office fixtures when we decreased our headquarters' office space in 2008; and
- a 41.8% decrease in fees and service charges from ₩1,323 million in 2007 to ₩770 million in 2008 mainly due to a decrease in outsourcing service fees, as we decreased the number of outsourcing workforce that worked on customer relations for Soul of the Ultimate Nation (SUN) and quality assurance during the previous year.

As a percentage of total net revenues, cost of revenues decreased from 60.2% in 2007 to 46.1% in 2008.

Selling, general and administrative expenses. Selling, general and administrative expenses consist of sales commissions paid to independent promotional agents that target our Internet cafe subscribers in Korea, commissions paid to providers of settlement services, administrative expenses and related personnel expenses of executive and administrative staff, and marketing and promotional expenses and related personnel expenses. Selling, general and administrative expenses increased 7.6% from ₩22,848 million in 2007 to ₩24,590 million in 2008 primarily due to:

- a 63.4% increase in fees and commissions from ₩3,369 million in 2007 to ₩5,504 million in 2008 mainly due to an increase in professional fees related to defending a hostile acquisition attempt in 2008; and
- a 68.4% increase in marketing expenses from ₩2,271 million in 2007 to ₩3,824 million in 2008 (as a percentage of total revenues, our marketing expenses increased from 7.8% in 2007 to 11.7% in 2008) mainly due to the advertisement costs related the launch of third closed beta test and open beta test of our new product, Huxley.

These increases were partially offset by a 15.3% decrease in payroll costs and retirement benefit costs from ₩10,462 million in 2007 to ₩8,859 million in 2008, as the number of general and administrative personnel decreased 30.1% compared to the prior year.

As a percentage of net revenues, selling, general and administrative expenses decreased from 78.5% in 2007 to 75.0% in 2008.

Research and development expenses. Research and development expenses incurred prior to the establishment of technological feasibility are included in this item. Research and development expenses in 2008 decreased 92.2% from ₩23,164 million in 2007 to ₩1,816 million in 2008, despite the advance payment of ₩979 million to Red 5 Studios for T-Project, partly due to a ₩12,309 million setoff to the research and development expenses, which reflects the amount RTW reimbursed or agreed to reimburse us for our earlier advance payments when we terminated a game development agreement with it, and a decrease of ₩7,194 million attributable various cost-cutting measures in research and development departments including decrease in wages and salaries paid and outsourcing fees paid.

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Impairment charges. We realized an impairment charge of ₩505 million in 2008, while there were no such charges in previous periods. This impairment charge in 2008 was mainly due to the impairment of equipment, capitalized leasehold improvements and certain other assets of Webzen China and Webzen America as the two entities ceased to conduct activities generating revenue and the relevant assets had not alternative use.

Interest income. Our interest income is mainly generated from cash equivalents and short-term financial instruments. Interest income decreased 4.0% from ₩3,503 million in 2007 to ₩3,364 million in 2008, mainly due to a decrease of cash and cash equivalents and short-term financial instruments. During the same period, the balance of our cash and cash equivalents and short-term financial instruments decreased from ₩74,904 million as of December 31, 2007 to ₩53,346 million as of December 31, 2008, while the average interest rate on these assets increased.

Foreign currency gain and loss. Our net foreign currency gain increased significantly from ₩92 million in 2007 to ₩3,210 million in 2008. This was mainly due to an increase of valuation of foreign currency denominated assets (including account receivables and long-term loans), as the Korean Won significantly depreciated against other major currencies including the U.S. dollar in 2008.

Gain on disposal of property and equipment. We realized net gain on disposal of property and equipment of ₩3,931 million in 2007, but no such gain in 2008. The gain on disposal of property and equipment in 2007 was mainly due to the sale of office space at the Daelim Acrotel Building in Dogok-dong, Seoul.

Gain on disposal of available-for-sale securities. Our gain on disposal of available-for-sale securities decreased 99.1% from ₩3,755 million in 2007 to ₩34 million in 2008. The net gain in 2007 of ₩2,320 million was from sale of common shares of GameOn and ₩1,435 million from disposal of beneficial certificates and other available-for-sale securities.

Loss on impairment of available-for-sale securities. We realized loss from impairment of available-for-sale securities of ₩3,883 million in 2008 from an other-than-temporary decrease in value of investment in NeoWave Inc. We did not incur any loss on impairment of available-for-sale securities in 2007.

Income taxes. Income tax expenses decreased 68.9% from ₩2,579 million in 2007 to ₩802 million in 2008, mainly due to a decrease of income tax expenses relating to the valuation allowance for unrealized gain on available-for-sale securities. The income tax expenses in 2007 were attributable to an increase in the valuation allowance recorded in 2007, due to a decrease in the deferred tax liabilities recorded in equity in 2006 related to available for sale securities.

Net loss attributable to non-controlling interest. Non-controlling interest represents the net income (loss) from 9Webzen, our 70%-held subsidiary acquired in 2002 and Flux, our 55.4%-held subsidiary acquired in 2003, attributable to third-party non-controlling interest holders.

Net loss attributable to parent company. As a result of the factors discussed above, our net loss attributable to parent company decreased from ₩25,594 million in 2007 to ₩7,675 million in 2008.

Impact of inflation

In view of our operating history, we believe that inflation in Korea and our other principal markets has not had a material impact on our results of operations. Inflation in Korea was 2.5% in 2007, 4.7% in 2008 and 2.8% in 2009.

Impact of Foreign Currency Fluctuations

See “Item 11. Quantitative and Qualitative Disclosures about Market Risk — Foreign currency risk.”

[Table of Contents](#)**Government, Economic, Fiscal, Monetary or Political Factors**

See “Item 3. Key Information — 3.D. Risk Factors — Risks Related to The Republic of Korea,” “Item 4. Information on the Company — 4.B. Business Overview — Laws and Regulations” and “Item 10. Additional Information — 10.E. Taxation.”

5.B. Liquidity and Capital Resources

Liquidity. The following table sets forth the summary of our cash flows for the periods indicated:

| | For the year ended December 31, | | |
|--|---|-------------|----------------|
| | 2008 | 2009 | 2009(1) |
| | (in millions of Won and thousands of US\$) | | |
| | (unaudited) | | |
| Net cash provided by (used in) operating activities | (13,916) | 15,876 | 13,644 |
| Net cash provided by (used in) investing activities | (2,868) | 7,411 | 6,369 |
| Net cash used in financing activities | (8,798) | (84) | (73) |
| Effect of exchange rate changes on cash and cash equivalents | 548 | (45) | (39) |
| Net increase (decrease) in cash and cash equivalents | (25,034) | 23,158 | 19,901 |
| Cash and cash equivalents at beginning of period | 66,857 | 41,823 | 35,941 |
| Cash and cash equivalents at end of period | 41,823 | 64,981 | 55,842 |

(1) For convenience, the Won amounts are expressed in U.S. dollars at the rate of ₩1,163.65 to US\$1.00, the noon buying rate in effect on December 31, 2009, as announced by the Federal Reserve Bank of New York.

In 2009, our primary sources of liquidity were existing cash on hand and short-term financial instruments.

Net cash provided by operating activities in 2009 was ₩15,876 million (US\$13,644 thousand), as our net income amounted to ₩3,390 million (US\$2,913 thousand), mainly due to our cost-cutting efforts. In addition, net cash provided by operating activities in 2009 reflects non-cash items such as depreciation and amortization expenses of ₩3,483 million (US\$2,993 thousand), a decrease in other receivables by ₩8,647 million (US\$7,431 thousand) and an increase in accounts payable and accrued expenses by ₩1,923 million (US\$1,653 thousand), partially offset by an increase in deferred income of ₩1,709 million (US\$1,468 thousand). We used ₩13,916 million in operating activities in 2008, as our net loss amounted to ₩7,829 million in 2008 and other receivables increased ₩8,570 million primarily due to the receivables recorded from our termination of agreement with RTW, partially offset by non-cash items such as depreciation and amortization.

Net cash provided by investing activities in 2009 was ₩7,411 million (US\$6,369 thousand), primarily due the ₩10,000 million (US\$8,594 thousand) decrease in short-term financial instruments and the ₩1,088 million (US\$935 thousand) net proceeds received by disposing property and equipment, partially offset by the ₩1,751 million (US\$1,505 thousand) net increase in leasehold and other deposits. Net cash used in investing activities in 2008 was ₩2,868 million, primarily due the ₩9,987 million increase in investment in available-for-sale securities and the ₩2,897 million increase in short-term financial instrument, partially offset by the ₩11,306 of leasehold deposit we received when we decreased our office space.

Net cash used in financing activities in 2009 was ₩84 million, primarily due to the ₩54 million (US\$47 thousand) used in repayment of capital lease liability under the terms of existing loan agreements and the ₩30 million (US\$26 thousand) decrease in short-term borrowing, which was partly attributable to the repayment of borrowing that had been incurred by Flux Co., Ltd. Net cash used in financing activities was ₩8,798 million in 2008, primarily due to the ₩6,617 million used in the acquisition of treasury stock and the ₩1,192 million net decrease in short-term borrowing, which was partly attributable to the repayment of borrowing that had been incurred by Webzen China.

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Capital resources. As of December 31, 2009, our primary source of liquidity was ₩64,981 million (US\$55,842 thousand) of cash and cash equivalents and ₩1,411 million (US\$ 1,212 thousand) of unrestricted short-term financial instruments. We believe that our available cash, cash equivalents and short-term financial instruments will be sufficient to meet our capital needs for at least the next 12 months. However, we cannot assure you that our business or operations will not change in a manner that would consume available capital resources more rapidly than anticipated. As of December 31, 2009, Webzen Taiwan has a L/C credit line up to US\$650 thousand from a local bank in Taiwan.

We expect to have capital expenditure requirements for the ongoing expansion into other markets, including hardware expenditures for the continuous expansion and upgrading of our existing server equipment, for which we expect to make approximately ₩4.8 billion in capital expenditures in 2010. The amount and timing of any investments have not yet been determined and will depend on our ability to identify suitable acquisition targets.

5.C. Research and Development, Patents and Licenses

Our research and development activities comprises mostly of development of new games and services. Since 2007, we have implemented a series of cost-cutting measures. We significantly reduced our workforce, including game developers, and as a result the number of employees in game development, web development and system engineering teams decreased from 414 as of December 31, 2008 to 398 as of December 31, 2009. In April 2009, the development and maintenance of Parfait Station was outsourced to NHN Games. In early 2009, we also negotiated with Red 5 Studios to reduce the amount we invest in T-project development in exchange for lower profit share in the U.S. and European market after commercialization. On May 28, 2009, an amendment to the original publishing agreement was made to waive our obligation to make any additional payments relating to T-project in exchange for Red 5 Studios' publishing rights in the United States and Europe and lower profit share worldwide after commercialization. We incurred ₩2,227 million (US\$1,914 thousand), ₩1,816 million and ₩23,262 million as research and development expenses for the years ended December 31, 2009, 2008 and 2007, respectively.

5.D. Trend Information

See “—5.A. Operating Results—Overview.”

5.E. Off-balance Sheet Arrangements

We have provided guarantees of ₩226 million (US\$194 thousand) as of December 31, 2009 to lending institutions for certain loans extended to our employees for their purchase of our common shares. The guarantees are secured by a cash deposit with the lending institution.

We opened a stand-by letter of credit account at Hana Bank for our business in Taiwan, which will remain current until December 18, 2010. In return, Hana Bank provided a guarantee of up to US\$650 thousand for Webzen Taiwan for its borrowings from a local bank in Taiwan.

We do not have any outstanding hedging contracts. See “Item 11. Quantitative and Qualitative Disclosures about Market Risk — Foreign currency risk.”

5.F. Contractual Obligations

The tables below set forth the maturities of contractual cash obligations as of December 31, 2009.

| | Payments due by period | | | | |
|--------------------------------|------------------------|------------------|-----------|-----------|---------------|
| | Total | Less than 1 year | 1-3 years | 3-5 years | After 5 years |
| | (in millions of Won) | | | | |
| Contractual obligations | | | | | |
| Operating lease obligations | 3,666 | 1,679 | 1,987 | — | — |
| Capital lease obligations | 22 | 22 | — | — | — |
| Purchase obligations | — | — | — | — | — |

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Employees and executive officers with one year or more of service are entitled to receive a lump-sum payment upon termination of their employment with us based on the length of service and their rate of payment at the time of termination. We accrued ₩3,046 million (US\$2,618 thousand) as accrued severance benefits as of December 31, 2009.

Item 6. Directors, Senior Management and Employees

6.A. Directors and Senior Management

The following table sets forth the names, ages and positions at our company and other positions held by our Directors and officers as of June 4, 2010:

| Name | Age | Position |
|-----------------|-----|--|
| Chang Keun Kim | 40 | Chief Executive Officer and Director (Representative Director) |
| Byoung Gwan Kim | 38 | Chief Executive Officer and Director (Representative Director) |
| Hyun Sung Kim | 39 | Director |
| In Joon Hwang | 45 | Director |
| Wook Jeong | 38 | Director |
| Chang Won Rhee | 48 | Outside Director and a member of the Audit Committee |
| Seung Han Ha | 44 | Outside Director and a member of the Audit Committee |
| Hyuk-Yun Kim | 40 | Outside Director and a member of the Audit Committee |
| Hwi Joon Shin | 34 | Chief Financial Officer |

Chang Keun Kim is the Co-Representative Director and the Chief Executive Officer serving since October 2008. He served as Business Department Manager of NHN Hangame Division and Group Manager of NHN Publishing Business Group. Mr. Kim had received a bachelor's degree in business administration from Seoul National University and a master's degree and doctoral degree in business administration from Korea Advanced Institute of Science and Technology.

Byoung Gwan Kim is the Co-Representative Director and Chief Executive Officer, serving in that capacity since being elected as such at the Board of Directors held on June 4, 2010. He was previously our Chief Strategy Officer. He is also the chief executive officer of NHN Games. Mr. Kim received a bachelor's degree in business administration from Seoul National University and a master's degree in industrial business administration from Korea Advanced Institute of Science and Technology.

In Joon Hwang is a Director. He was newly elected Director at the extraordinary general shareholders meeting held on June 4, 2010. Mr. Hwang is also a director and as a chief financial officer of NHN Corp. He received a bachelor's degree in economics from Seoul National University and a master's degree in economics from New York University. He was a managing director at the Investment Banking Division of Woori Investment & Securities Co., Ltd.

Wook Jeong is a Director. He was newly elected Director at the extraordinary general shareholders meeting held on June 4, 2010. He is also a director of NHN Corp and the chief business officer of Hangame Business Division of NHN Corp. He received a bachelor's degree in 1998 from Seoul National University. He served as a management consultant at Accenture and as an executive director at Freechal Inc.

Hyun Sung Kim is a Director. He was newly elected Director at the extraordinary general shareholders meeting held on June 4, 2010. He is also a director and general counsel of NHN Corp. He was a Judge at Seoul Northern District Court and worked at DR& AJU Law firm previously.

Chang Won Rhee is an Outside Director and a member of the Audit Committee since October 2008. He is a partner attorney at Shin & Kim. Mr. Lee had received a bachelor's degree in law from Seoul National University and a master of law degree from Boston University.

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Seung Han Ha is an Outside Director and a member of the Audit Committee since October 2008. He is a certified public accountant and is an accountant at Shin & Kim. Mr. Ha received a bachelor's degree in business administration from Seoul National University and a master's degree in business administration from University of Illinois.

Hyuk-Yun Kim is an Outside Director and a member of the Audit Committee since March 2009. He is a certified public accountant at Kim & Chang since 2001. Mr. Kim worked at Sandong Accounting Firm from 1997 to 2000 as a certified public accountant. Mr. Kim received a bachelor's degree in business administration from Seoul National University and a master's degree in business taxation from University of Southern California.

Hwi Joon Shin is the Chief Financial Officer, serving in this capacity since August 2009. He is a certified public accountant and worked as an analyst at Citigroup and as an accountant at KPMG. He received a bachelor's degree in business administration from Seoul National University.

Chang Keun Kim, Byoung Gwan Kim, Chang Won Rhee and Seung Han Ha were elected as Directors at the extraordinary general meeting of shareholders held on October 24, 2008 after NHN Games purchased Common Shares from our prior controlling shareholders. Hyuk-Yun Kim was elected as an Outside Director at the annual general meeting of shareholders held on March 27, 2009. On August 24, 2009, Mr. Hyung-Cheol Kim resigned as the CFO and Mr. Hwi Joon Shin was appointed as the CFO. Hyun Sung Kim, In Joon Hwang and Wook Jeong were elected as Directors at the extraordinary general meeting of shareholders held on June 4, 2010.

Chang Won Rhee and Seung Han Ha were re-elected as our Outside Directors and members of the Audit Committee at the extraordinary general meeting of shareholders held on June 4, 2010. In accordance with the Korean Commercial Code provisions and our Articles of Incorporation, their term of office expires on June 3, 2013.

6.B. Compensation

We have not extended any loans or credit to any of our Directors or executive officers, and we have not provided guarantees for borrowings by any of these persons. For the year ended December 31, 2009, the aggregate amount of compensation paid by us to all Directors and executive officers was ₩1,322 million (US\$1,136 thousand). In addition, our shareholders approved the grant of stock options to purchase an aggregate of 200,000 common shares to one registered Director at our general meeting of shareholders held on March 27, 2009. In the shareholders meeting held on March 26, 2010, our shareholders approved an aggregate amount of up to ₩1.26 billion as compensation for our executive officers for the year 2011 and ratified the stock options to purchase 12,000 common shares that was granted by the Board of Directors to one non-registered officer on May 14, 2009.

Under the Korean Labor Standard Act, we are required to pay a severance amount to eligible employees, including Directors and officers, who voluntarily or involuntarily terminate their employment with us, including through retirement. The severance amount for an officer or Director equals the monthly salary at the time of his or her departure, multiplied by the number of continuous years of service, and further multiplied by a discretionary number set forth in our Severance Payment Regulation, which depending on the position of the officer or Director ranges from two to four. We have set aside or accrued ₩137 million (US\$118 thousand) to provide for such severance amount.

We maintain a Directors' and officers' liability insurance policy covering potential liabilities of our Directors and officers.

6.C. Board Practices

Board of Directors

Our board of Directors has the ultimate responsibility for the administration of our affairs. Our Articles of Incorporation, as currently in effect, provide for a board of Directors comprised of not less than three Directors. The Directors are elected at a general meeting of shareholders by a majority vote of the shareholders present or represented, so long as the affirmative votes also represent not less than 25% of all issued and outstanding shares with voting rights. For the purpose of electing a statutory auditor or auditors, a shareholder holding more than 3% of

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the issued and outstanding shares with voting rights may not exercise voting rights with respect to such shares in excess of 3%.

The term of office for our Directors is three years but is extendible to the close of the ordinary general meeting of shareholders convened in the last fiscal year of each term. The terms of Chang Keun Kim and Byoung Gwan Kim expire on October 23, 2011.

The term of office for our Outside Directors is three years but is extendible to the close of the ordinary general meeting of shareholders convened in the last fiscal year of each term. The terms of Hyuk-Yun Kim expire on March 26, 2011. Chang Won Rhee and Seung Han Ha were reelected as our Outside Directors and members of the Audit Committee at the extraordinary general shareholders meeting held on June 4, 2010. In accordance the Korean Commercial Code provisions and our Articles of Incorporation, their term of office expires on June 3, 2013. The term of office for our Outside Directors was changed from two years to three years at the extraordinary general meeting of shareholders held on June 4, 2010.

Under the Korean Commercial Code, a Director's term of office cannot exceed three years. However, Directors may serve any number of consecutive terms and may be removed from office at any time by a resolution adopted at a general meeting of shareholders. None of our Directors is party to a service contract with our company that provides for benefits upon termination of employment.

The board of Directors elects Representative Directors from its members. Under the Korean Commercial Code and our Articles of Incorporation, any Directors with a special interest in an agenda of a board meeting may not exercise his voting rights at that board meeting.

Independent Directors

Our ADSs are listed for quotation on the Nasdaq Market and we currently are subject to the Nasdaq listing requirements applicable to listed foreign companies. Under the Nasdaq listing requirements, Nasdaq Listing Rule 5605(b), a majority of the board of Directors should be comprised of independent directors. The independence standards under the Nasdaq rules exclude, among others, any person who is a current or former employee of a company (for the current year or the past three years) or of any of its affiliates, as well as any immediate family member of an executive officer of a listed company or of any of its affiliates. The Korea Financial Investment Service and Capital Market Act and regulations thereunder require companies listed on the KOSDAQ or KRX Stock Market to have at least one fourth of its board of Directors comprised of outside directors. Under Korean law, a director or officer of the company, any person who served as a director or an officer of the company during the past two years, certain family members of a director of the company or certain other affiliates of the company, do not qualify as an outside director. We elected three independent Outside Directors to comply with Korean law, but we do not satisfy the majority independent board requirement under Nasdaq Listing Rule 5605(b)(1).

Audit Committee

The Sarbanes-Oxley Act of 2002 directs the SEC to require U.S. national securities exchanges and national securities associations, such as the Nasdaq Global Market, to adopt rules prohibiting the listing of any security of an issuer that is not in compliance with the relevant audit committee requirements set forth in the Sarbanes-Oxley Act. The SEC adopted final rules relating to the audit committee requirements on April 9, 2003, and approved related proposed changes to the Nasdaq corporate governance rules on November 4, 2003. Nasdaq Listing Rule 5605(c), which sets forth the requirements for listing company's audit committees, requires that at least three independent directors who are able to read and understand fundamental financial statements serve on the committee.

Under the Korean Commercial Code, a company may elect between appointing a statutory internal auditor or establishing an audit committee.

To comply with the Sarbanes-Oxley Act and the SEC rules and regulations as well as the Nasdaq listing requirements regarding the audit committee, our board of Directors established an audit committee by amending our Articles of Incorporation at the general meeting of shareholders held in March 2004. Our Audit Committee is currently comprised of the following three independent Directors: Chang Won Lee, Seung Han Ha and Hyuk-Yun

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Kim. All of our independent Directors are financially literate and our board of Directors designated Seung Han Ha as an audit committee financial expert. The Audit Committee is responsible for examining internal transactions and potential conflicts of interest and reviewing company accounting and other relevant matters. Under the Korean Commercial Code, the Audit Committee has the right to request the board of Directors to convene a shareholders' meeting by providing a document that sets forth the agenda and reasons.

Difference between Nasdaq requirements and home country practices

In general, corporate governance principles for Korean companies are set forth in the Korean Commercial Code and the Capital Market and Financial Investment Business Act and, to the extent they are listed on KOSDAQ Market, the listing rules of KOSDAQ Market. Corporate governance principles under provisions of Korean law may differ in significant ways from corporate governance standards for U.S. Nasdaq-listed companies. Under the Nasdaq Listing Rule 5615(a)(3), foreign private issuers are permitted to follow certain home country corporate governance practices in lieu of the requirements of the Rule 5600 Series. Under the Rule, foreign private issuers must disclose alternative home country practices they follow. The following are the requirements of the Rule 5600 Series we do not follow and the descriptions of home country practices.

Under Rule 5250(d)(1), issuers are required to distribute to shareholders copies of annual reports containing audited financial statements within a reasonable period of time following the filing of the annual report with the SEC. We do not distribute our annual report to our shareholders. Instead, we make our annual report and audited non-consolidated financial statements available for inspection at our principal office and at all of our branch offices at least one week before the annual general meeting of shareholders. We also file our annual report on the Data Analysis Retrieval and Transfer System, or DART, an electronic disclosure system operated by FSS, in accordance with the rules under the Capital Market and Financial Investment Business Act.

Under Rule 5605(b)(2), issuers are required to have regularly scheduled meetings (executive sessions) at which only independent directors are present. We do not hold executive sessions of independent Directors, as such meetings are not required under Korean law. However, our three independent Directors serve on our Audit Committee and meet regularly.

Rule 5605(d)(1) requires that compensation of the chief executive officer and other executive officers must be determined, or recommended to the board, either by a majority of the independent directors or an independent compensation committee. We currently follow the home country practice, which allows the board of Directors to determine executive officers' compensations.

Under Rule 5605(e)(1), director nominees must either be selected, or recommended for the board's selection, either by a majority of the independent directors or an independent nominations committee. The Korean Commercial Code grants the power of nomination to the board of Directors, and we conduct our nomination process accordingly.

We, as a foreign issuer, have been granted an exemption by Nasdaq from the requirement that the minimum quorum for a shareholder meeting is 33 $\frac{1}{3}$ % of the outstanding common shares as required by Nasdaq Listing Rule 5620(c), on the basis that such requirement was inconsistent with our home country practice. Pursuant to our Articles of Incorporation, our shareholders may adopt resolutions at a general meeting by an affirmative majority vote of the voting shares present or represented at the meeting, where the affirmative votes also represent at least one-fourth of our total voting shares then issued and outstanding. Our quorum requirements comply with the requirements of the Korean Commercial Code and are consistent with that of other companies with common shares listed on KOSDAQ Market.

Rule 5620(b) requires issuers to solicit proxies and provide proxy statements for all meetings of shareholders and provide them to Nasdaq. Nasdaq is of the view that the proxy statements required under Rule 5620(b) should contain the information required by Section 14 of the United States Securities Exchange Act of 1934 (the "Exchange Act") and rules thereunder. The Capital Market and Financial Investment Business Act requires persons soliciting proxies to provide proxy materials, with information set forth in the rules, to shareholders prior to or at the same time as the solicitation and to file the proxy materials with the FSS before they are sent to the shareholders.

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However, the information required under the Korean rules is much less extensive than that required under the Exchange Act rules. We do provide to shareholders proxy statements prior to shareholder meetings, but the content of the materials is made in accordance with the rules under the Capital Market and Financial Investment Business Act.

Under Rule 5630(a), issuers shall conduct an appropriate review and oversight of all related party transactions on an ongoing basis by the audit committee or another independent body of the board of directors. Korean law does not have a comparable requirement, and our board of Directors reviews and approves related party transactions. Under the Korean Commercial Code and our Articles of Incorporation, however, any Director with a special interest in an agenda item of a board meeting may not exercise his voting rights at that board meeting.

Rule 5635(a) and (b) require issuers to obtain shareholder approval prior to the issuance of securities when the issuance or potential issuance will result in a change of control of the issuers, or prior to the issuance of securities in connection with the stock or assets of another company if certain conditions are met. We do not obtain shareholder approval for all of the cases provided in Rule 5605(i). However, under the Korean Commercial Code and our Articles of Incorporation, we do require approval by the holders of at least two-thirds of the voting shares present or represented at a meeting, where the affirmative votes also represent at least one-third of our total voting shares then outstanding, when we acquire all of the business of any other company or a part of the business of any other company that has a material effect on our business, issue new shares at a price below par value, transfer all or any significant part of our business, or effect a capital reduction.

6.D. Employees

As of December 31, 2009, we had 361 full-time employees. The following tables set forth the number of permanent employees at Webzen and its subsidiaries, for the dates indicated:

| | <u>2007</u> | <u>2008</u> | <u>2009</u> |
|---|-------------------|-------------------|-------------------|
| Employees | | | |
| Game development, web development and system engineering team | 450 | 229 | 219 |
| Game supporting team | 84 | 38 | 58 |
| International business, strategy and planning, management support and game marketing team | <u>138</u> | <u>147</u> | <u>121</u> |
| Total | <u><u>672</u></u> | <u><u>414</u></u> | <u><u>398</u></u> |

None of our employees is represented by a labor union or covered by a collective bargaining agreement. We consider our relations with our employees to be good.

As of December 31, 2009, our wholly-owned subsidiary, Webzen Taiwan had 39 full-time employees.

As of December 31, 2009, 9Webzen and its subsidiary employed 37 employees in China, none of whom is represented by a labor union or covered by a collective bargaining agreement.

Under the Korean Labor Standard Act, employees with more than one year of service are entitled to receive a lump sum payment upon voluntary or involuntary termination of their employment. The amount of the benefit equals the employee's monthly salary, calculated by averaging the employee's daily salary for the three months prior to the date of the employee's departure, multiplied by the number of continuous years of employment.

Pursuant to the Korean National Pension Law, we are required to prepay 4.5% of each employee's annual wages as part of our accrued severance payments to the National Pension Corporation. Our employees are also required to pay 4.5% of their annual wages to the National Pension Corporation. Our employees are entitled to receive an annuity in the event they lose, in whole or in part, their wage earning capability.

Hana Bank and Korea Exchange Bank extended loans to members of our employee stock ownership association. As of December 31, 2009, we have pledged short-term financial instruments in the amount of ₩226 million (US\$194 thousand) to guarantee these bank loans. We also had outstanding housing and other loans to our employees in the aggregate amount of ₩345 million (US\$296 thousand) as of December 31, 2009. We have not experienced any defaults under these

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loans to our employees. We provide these loans as a benefit to our employees and not as a requirement under Korean law. Our executive officers and Directors are not eligible for these loans.

6.E. Share Ownership

Some of our Directors and officers own our common shares. See “Item 7. Major Shareholders and Related Party Transactions—7.A. Major Shareholders.”

Stock Option Plan

Pursuant to our Articles of Incorporation and the Korean Commercial Code, stock options may be granted by either a special resolution of our shareholders or a resolution of our board of Directors, with the aggregate number of shares issuable in each case not to exceed 15% and 3%, respectively, of the total number of our then issued and outstanding common shares. Stock options may be granted to our executive officers and employees who have contributed or are qualified to contribute to our establishment, management and technical innovation. No stock options may be granted to any executive officer or employee who owns, or upon exercise of an option to purchase our common shares would own, directly or indirectly, 10% or more of our outstanding common shares.

According to our Articles of Incorporation, we may grant stock options that are exercisable to purchase Common Shares and our preferred shares. Such stock options can vest after two years from the stock option grant date and can be exercisable up to seven years (four years for options granted in 2007) from the date of the grant. The stock option may be cancelled by a resolution of our board of Directors:

- if the officer or employee who holds the option resigns voluntarily or is discharged from office prior to the vesting date;
- if the officer or employee is discharged or submitted to a disciplinary measure for causing damage to us by willful misconduct or by gross negligence; or
- in the event of the occurrence of any cause for cancellation of stock options specified in the stock option agreement.

On January 20, 2005, we granted stock options to our employees to purchase an aggregate of 118,800 Common Shares. All of the options granted on this date could be exercised between January 20, 2008 through January 19, 2010, at a purchase price of ₩24,100 per share. On April 14, 2005, we granted stock options to our employees to purchase an aggregate of 24,500 Common Shares. All of the options granted on this date could be exercised between April 14, 2008 through April 13, 2010 at a purchase price of ₩24,100 per share. On April 12, 2006, we granted stock options to our employees to purchase an aggregate of 41,000 Common Shares. All of the options granted on this date could be exercised between April 12, 2008 through April 11, 2010 at a purchase price of ₩24,100 per share. Options for 18,000 shares of the total 41,000 shares were granted to two executive officers. On July 18, 2007, we granted stock options to our employees to purchase an aggregate of 114,000 Common Shares. All of the options granted on this date can be exercised between July 12, 2009 through July 11, 2011 at a purchase price of ₩16,000 per share. On October 12, 2007, we granted stock options to our employees to purchase an aggregate of 77,000 Common Shares. All of the options granted on this date can be exercised between October 12, 2009 through October 11, 2011 at a purchase price of ₩14,000 per share. On February 12, 2009, we granted stock options to our employees to purchase an aggregate of 131,400 Common Shares. All of the options granted on February 12, 2009 can be exercised from February 12, 2011 through February 11, 2013 at a purchase price of ₩6,800 per share. On March 27, 2009, we granted stock options to our directors and executive officers to purchase an aggregate of 213,000 Common Shares. All of the options granted on March 27, 2009 can be exercised from March 27, 2011 through March 26, 2013 at a purchase price of ₩8,300 per share. On March 26, 2010, we granted stock option to one executive officer to purchase 12,000 Common Shares. The option granted on March 26, 2010 can be exercised from May 14, 2011 through May 13, 2013 at a purchase price of ₩13,600 per share.

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As of June 25, 2010, options to purchase an aggregate of 468,400 Common Shares were outstanding. Our Directors or executive officers were granted options to purchase 212,000 of such Common Shares. With respect to the current Directors and executive officers, Mr. Chang Keun Kim was granted the option to purchase 200,000 Common Shares on March 27, 2009, exercisable from March 27, 2011 through March 26, 2013 at a purchase price of ₩8,300, and Mr. Hwi Joon Shin was granted the option to purchase 12,000 Common Shares on March 26, 2010, exercisable from May 14, 2011 through March 13, 2013 at a purchase price of ₩13,600.

As of June 25, 2010, options to purchase an aggregate of 155,150 NHN Games' common shares were outstanding. When the Merger is consummated, the stock options granted by NHN Games will become our obligation. We will satisfy this obligation by issuing new shares or utilizing treasury stock. As 1.57262712 of our Common Shares is to be issued in exchanged for each NHN Games common share under the merger agreement, we will be obligated to honor options to purchase 243,993 Common Shares after the date of merger.

Item 7. Major Shareholders and Related Party Transactions

7.A. Major Shareholders

The following table sets forth information as of June 28, 2010 known to us with respect to the beneficial ownership of our common shares by:

- each person who is the beneficial owner of more than 5% of our common shares;
- each of our Directors;
- each of our named executive officers; and
- all of our executive officers and Directors as a group.

The percentage in column (A) of the following table is based on 12,974,000 of our common shares issued as of June 28, 2010, and the percentage in column (B) is based on 11,856,948 of our common shares issued and outstanding as of the same date. The numbers of shares in the table include shares that can be acquired within 60 days through the exercise of any option, warrant or right or through conversion of any securities, or otherwise. None of our common shares entitles the holder to any preferential voting rights.

| | <u>Number of shares beneficially owned</u> | <u>Percentage beneficially owned (A)</u> | <u>Percentage beneficially owned (B)</u> |
|---|--|--|--|
| Directors and officers: | | | |
| Chang Keun Kim | 10,000 | 0.08% | 0.08% |
| Byoung Gwan Kim | 0 | 0.00% | 0.00% |
| Hyun Sung Kim | 0 | 0.00% | 0.00% |
| In Joon Hwang | 0 | 0.00% | 0.00% |
| Wook Jeong | 0 | 0.00% | 0.00% |
| Chang Won Rhee | 0 | 0.00% | 0.00% |
| Seung Han Ha | 0 | 0.00% | 0.00% |
| Hyuk-Yun Kim | 0 | 0.00% | 0.00% |
| Hwi Joon Shin | 0 | 0.00% | 0.00% |
| All executive officers and Directors as a group | <u>10,000</u> | <u>0.08%</u> | <u>0.08%</u> |
| Other major shareholders: | | | |
| NHN Games(1) | 3,469,784 | 26.74% | 29.26% |
| Nam-Ju Kim(1) | 398,636 | 3.07% | 3.36% |
| Kil-Saup Song(1) | 305,120 | 2.35% | 2.57% |
| Ki-Yong Cho(1) | 294,095 | 2.27% | 2.48% |
| All other major shareholders | <u>4,467,635</u> | <u>34.43%</u> | <u>37.67%</u> |

- (1) Nam-Ju Kim, Kil-Saup Song and Ki-Yong Cho reported to the FSS that the shares held by each of them are deemed to be co-held by NHN Games under Section 142 of the Capital Market and Financial Investment Business Act of Korea. The total number of shares held by these shareholders as of June 28, 2010 was 4,467,635 shares or 34.43% of the issued shares (or 37.67% of the issued and outstanding shares).

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Since May 2008, NHN Games purchased Common Shares from various shareholders including our prior controlling shareholders. See Item 4. Information on the Company – 4.A. History and Development of the Company. As a result, the number of Common Shares held by NHN Games increased to 3,469,784 shares or 29.26% of the outstanding Common Shares as of June 28, 2010. In addition, NHN Games entered into an arrangement with Nam-Ju Kim, Ki-Yong Cho, Kil-Saup Song, Hyung-Cheol Kim and Chang Keun Kim that they would have a good faith discussion with NHN Games before exercising any voting rights of the Common Shares and that they shall exercise voting rights together in the same direction in accordance with the discussion for matters relating to changing or influencing control of our company. In August 2009, Hyung-Cheol Kim resigned from his post as the CFO and director of Webzen and withdrew from the group and such arrangement. Counting the shares held by such individuals, NHN Games effectively controlled 37.76% of our outstanding Common Shares as of June 28, 2010. Such share holding gives NHN Games the power to significantly affect the actions that require shareholder approval under Korean law and our articles of incorporation, including the election and removal of any member of our board of directors, mergers, consolidations and other business combinations and changes to our articles of incorporation.

According to JPMorgan Chase Bank, depository for our ADSs, as of December 31, 2009, 1,357,290 Common Shares were held in the form of ADSs, representing 11.5% of total outstanding Common Shares.

When the Merger is consummated, each common share of NHN Games will be exchanged for 1.57262712 Common Shares. This exchange of shares will change our shareholding structure.

Following table sets forth the beneficial ownership of NHN Games' common shares by each owner as of May 6, 2010.

| | <u>Number of Shares beneficially owned</u> | <u>Percentage beneficially owned</u> |
|--------------------------------------|--|--|
| NHN Corp | 6,000,000 | 46.88% |
| Byoung Gwan Kim | 5,978,450 | 46.71% |
| Employee Stock Ownership Association | 461,550 | 3.61% |
| Other shareholders | <u>360,000</u> | <u>2.80%</u> |
| Total issued and outstanding shares | <u><u>12,800,000</u></u> | <u><u>100.00%</u></u> |

Following table, which has been prepared as if the Merger had been consummated on June 28, 2010, sets forth the hypothetical breakdown of the beneficial ownership of the Common Shares by:

- each person who is the beneficial owner of more than 5% of Common Shares;
- each of our Directors;
- each of our named executive officers; and
- all of our executive officers and Directors as a group.

| | <u>Number of shares beneficially owned (1)</u> | <u>Percentage beneficially owned (2)</u> | <u>Percentage beneficially owned (3)</u> |
|--------------------------------|--|--|--|
| Directors and officers: | | | |
| Chang Keun Kim | 10,000 | 0.03% | 0.03% |
| Byoung Gwan Kim | 9,401,872 | 28.40% | 32.97% |
| Hyun Sung Kim | 0 | 0.00% | 0.00% |
| In Joon Hwang | 0 | 0.00% | 0.00% |

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| | <u>Number of shares beneficially owned (1)</u> | <u>Percentage beneficially owned (2)</u> | <u>Percentage beneficially owned (3)</u> |
|---|--|--|--|
| Wook Jeong | 0 | 0.00% | 0.00% |
| Chang Won Rhee | 0 | 0.00% | 0.00% |
| Seung Han Ha | 0 | 0.00% | 0.00% |
| Hyuk-Yun Kim | 0 | 0.00% | 0.00% |
| Hwi Joon Shin | 0 | 0.00% | 0.00% |
| All executive officers and Directors as a group | <u>9,411,872</u> | <u>28.43%</u> | <u>33.00%</u> |
| Other major shareholders: | | | |
| NHN Corp | 9,435,762 | 28.50% | 33.09% |

- (1) The number of shares beneficially owned includes shares that can be acquired within 60 days through the exercise of any option, warrant or right or through conversion of any securities, or otherwise. None of Common Shares entitles the holder to any preferential voting rights.
- (2) The percentage is based on 33,103,627 of Common Shares issued as of June 28, 2010 (under assumption that the Merger was consummated on such date).
- (3) The percentage is based on 28,516,788 of Common Shares issued and outstanding as of June 28, 2010 under (assumption that the Merger was consummated on such date).

7.B. Related Party Transactions*Contribution to Webzen Taiwan*

We opened a stand by letter of credit at Hana Bank until December 18, 2010 for our business in Taiwan and, in turn, Hana Bank provided a payment guarantee of US\$650,000 for Webzen Taiwan's loan from a local bank in Taiwan.

Loan to Webzen America

We extended a US\$50,000 aggregate amount loan to Webzen America on March 24, 2009. The term was for three years and the interest rate was 5%. Webzen America will use the proceeds of the loan for general corporate use. We also have agreed to extend the maturity of first round long term loan of US\$1,500,000 on April 18, 2009. The term was for two years and interest rate of 5% was maintained. During the fiscal year ended December 31, 2009, the largest amount outstanding of the loan to Webzen America from us was US\$4 million.

Contracts with NHN Games or its Affiliates

In March 2009, we entered into a channeling agreement with NHN Corp. Under the agreement, we distribute our game Soul of the Ultimate Nation (SUN) in Korea through NHN Corp.'s online game portal, www.hangame.com, and use NHN Corp.'s virtual cash (Han Coin) settlement system in exchange for fees and 20% of profit sharing amount generated through the portal.

In April 2009, we entered into a service agreement with NHN Games to have it develop and maintain our game Parfait Station. Under the agreement, NHN Games undertook to develop our discontinued online game Parfait Station, deliver by a certain date a version that is ready to be commercialized and maintain the game after commercialization in exchange for certain installment payments (₩3.0 billion in total) during the development stage and 20-50% of net revenue generated from the game after commercialization.

In May 2009, we entered into a three-year exclusive license agreement with NHN USA Inc. to distribute Soul of the Ultimate Nation (SUN) in the United States, Canada, Mexico and the United Kingdom through www.ijji.com. Under the agreement, we are to receive software development and installation fees in the amount of US\$300,000, 30% of net revenue generated in the licensed territory as running royalty (with minimum guarantee amounts) and additional incentives when certain milestone sales figures are achieved.

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In June 2009, we entered into a outsourcing agreement with NHN Games where we are to provide services relating to strategy, marketing, promotion and businesses abroad. NHN Games is to pay ₩93.8 million per month for such services. The agreement became effective on December 31, 2009, and will be automatically renewed for one year unless a party notifies the other of its intent to terminate the agreement 30 days prior to the end of each contract period.

In August 1, 2009, we entered into a joint venture agreement with NHN Games where we will provide MU and SUN online and NHN Games will provide Archlord and R2 through a global game portal called webzen.com. We will transfer any revenue generated on NHN Games' title every month. The term of the agreement is to end on July 31, 2012, and will be automatically renewed for one year unless a party notifies its intent to terminate the agreement one month prior to the end of each contract period.

In February 2010, we entered into a publishing agreement with NHN Games to service Battle Territory, a first-person shooter game developed by NHN Games. We will pay ₩1,750 million to NHN Games as a license fee and divide equally the profit generated by the offering of Battle Territory.

7.C. Interests of Experts and Counsel

Not applicable.

Item 8. Financial Information

8.A. Consolidated Statements and Other Financial Information

All relevant financial statements are included in "Item 18. Financial Statements."

Legal proceedings

In December 2009, we filed suit against The9 in Seoul District Court in Korea for return of the trademark "MU." Under the trademark transfer agreement between us and The9, The9 had the obligation to transfer all trademark related to MU. We filed this suit to regain control over the trademark that we registered under The9 for ease of service in China.

Dividend policy

Since our inception on April 28, 2000, we have declared or paid dividends on our common shares once. On February 22, 2005, the board of Directors passed a resolution to pay dividends, and the shareholders approved it at our annual general meeting of shareholders on March 18, 2005. The record date was December 31, 2004, and the amount was ₩250 per common share. We plan to have a similar dividend policy in the future, but any decision to pay dividends in the future will be subject to a number of factors, including the interests of our shareholders, cash requirements for future capital expenditures and investments, as well as relevant industry and market practice.

Holders of outstanding common shares on a dividend record date will be entitled to the full dividend declared without regard to the date of issuance of the common shares or any subsequent transfer of the common shares. Payment of dividends in respect of a particular year, if any, will be made in the year following approval by our shareholders at the annual general meeting of shareholders, subject to certain provisions of the Korean Commercial Code.

Subject to the terms of the deposit agreement for the ADSs, holders of ADSs will be entitled to receive dividends on common shares represented by ADSs to the same extent as the holders of common shares, less the fees and expenses payable under the deposit agreement in respect of, and any Korean tax applicable to, such dividends. The depositary will generally convert the Won it receives into U.S. dollars and distribute the U.S. dollar amounts to holders of ADSs.

8.B. Significant Changes

Please see Item 4. Information on the Company — 4.A. History and Development of the Company.

[Table of Contents](#)**Item 9. The Offer and Listing****9.A. Market Price Information**

With the enactment of the Korea Stock and Futures Exchange Act, which came into effect on January 27, 2005, the three existing spot and futures exchanges (which were the Korea Stock Exchange, Korean Futures Exchange, and KOSDAQ) and Kosdaq Committee, a sub organization of Korea Stock Dealers Association, were merged and integrated into a newly established joint stock company called KRX. KRX is organized into five divisions: the Administrative Service Division, the Stock Market Division, referred to as KRX Stock Market, the Kosdaq Market Division, referred to as the KRX KOSDAQ Market, the Futures Market Division, referred to as the KRX Futures Market, and the Market Surveillance Division. The KRX, headquartered in Pusan, has one branch located in Seoul.

Our common shares are traded on the KOSDAQ under the code 069080. Our common shares were listed on the KOSDAQ on May 23, 2003. The KOSDAQ composite index is computed by taking the aggregate market capitalization of all companies included in the index as a percentage of the market capitalization as of the base date, July 1, 1996, multiplied by 1,000.

The most widely followed price index of stocks quoted on stock exchanges in Korea is the Korea Composite Stock Price Index, or KOSPI, an index of all equities listed on KRX Stock Market. The KOSPI is computed by aggregating the market capitalization of all listed companies and (subject to certain adjustments) by expressing this aggregate as a percentage of the aggregate market capitalization of all listed companies as of the base date (January 4, 1980).

The following table sets forth, for the periods indicated:

- the high and low closing sales price for our common shares as reported on the KOSDAQ;
- the average daily trading volume of our common shares;
- the high and low of the daily closing values of the KOSDAQ composite index; and
- the high and low of the daily closing values of the KOSPI.

| | Price per common share | | Average daily trading volume | KOSDAQ | | KOSPI | |
|----------------|------------------------|--------|------------------------------|--------|--------|----------|----------|
| | High | Low | | High | Low | High | Low |
| 2005 | | | | | | | |
| First quarter | 24,600 | 18,000 | 263,224 | 515.04 | 390.40 | 1,022.79 | 870.84 |
| Second quarter | 20,100 | 16,750 | 143,108 | 503.21 | 423.30 | 1,010.80 | 911.30 |
| Third quarter | 19,700 | 14,350 | 170,236 | 571.95 | 492.66 | 1,231.22 | 1,018.02 |
| Fourth quarter | 32,150 | 17,050 | 429,491 | 747.96 | 573.19 | 1,379.37 | 1,140.72 |
| 2006 | | | | | | | |
| First quarter | 34,400 | 19,000 | 417,607 | 754.97 | 601.33 | 1,421.79 | 1,297.43 |
| Second quarter | 25,400 | 15,000 | 232,418 | 704.57 | 559.37 | 1,464.70 | 1,203.86 |
| Third quarter | 17,100 | 11,800 | 190,944 | 614.80 | 539.81 | 1,374.30 | 1,233.42 |
| Fourth quarter | 13,600 | 11,200 | 131,734 | 622.17 | 539.10 | 1,442.28 | 1,319.40 |
| 2007 | | | | | | | |
| First quarter | 13,200 | 11,500 | 151,901 | 648.99 | 571.04 | 1,470.03 | 1,355.79 |
| Second quarter | 14,900 | 12,050 | 141,347 | 819.97 | 651.78 | 1,807.85 | 1,459.53 |
| Third quarter | 17,500 | 12,600 | 157,562 | 828.22 | 673.48 | 2,004.22 | 1,638.07 |
| Fourth quarter | 13,550 | 8,920 | 123,602 | 818.26 | 692.02 | 2,064.85 | 1,772.88 |
| 2008 | | | | | | | |
| First quarter | 12,800 | 9,810 | 70,295 | 719.25 | 600.10 | 1,863.90 | 1,574.44 |
| Second quarter | 15,700 | 8,980 | 174,586 | 655.80 | 590.19 | 1,888.88 | 1,674.92 |
| Third quarter | 11,250 | 6,550 | 68,248 | 580.77 | 481.14 | 1,666.46 | 1,387.75 |
| Fourth quarter | 6,230 | 3,965 | 60,131 | 440.95 | 261.19 | 1,439.67 | 938.75 |
| 2009 | | | | | | | |
| First quarter | 9,450 | 5,750 | 162,073 | 421.44 | 339.76 | 1,243.80 | 1,018.81 |
| Second quarter | 19,950 | 8,890 | 565,079 | 562.57 | 430.97 | 1,435.70 | 1,233.36 |
| Third quarter | 18,800 | 10,500 | 198,005 | 536.97 | 476.05 | 1,718.88 | 1,378.12 |
| Fourth quarter | 12,950 | 10,000 | 125,853 | 518.78 | 451.67 | 1,685.59 | 1,524.50 |

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| | Price per common share | | Average daily trading volume | KOSDAQ | | KOSPI | |
|-------------|------------------------|--------|------------------------------|--------|--------|----------|----------|
| | High | Low | | High | Low | High | Low |
| 2010 | | | | | | | |
| January | 14,150 | 10,900 | 354,962 | 553.10 | 496.57 | 1,722.01 | 1,602.43 |
| February | 13,600 | 11,800 | 195,234 | 516.23 | 487.41 | 1,628.90 | 1,552.79 |
| March | 12,550 | 11,450 | 104,310 | 527.58 | 507.59 | 1,700.19 | 1,615.12 |
| April(1) | 13,450 | 11,700 | 294,639 | 523.75 | 502.70 | 1,752.20 | 1,705.30 |
| May | 13,250 | 11,700 | 195,403 | 524.98 | 449.96 | 1,721.21 | 1,560.83 |

(1) Trading of the Common Shares was halted on April 15, 2010 5:55pm till April 16, 2010 4:36pm.

Nasdaq Market

The ADSs are listed on the Nasdaq Market under the symbol “WZEN.”

As a result of a 3-for-1 stock split in June 2004, the ADR ratio changed so that ten ADSs represent three shares. According to JPMorgan Chase Bank, depository for our ADSs, as of December 31, 2009, 1,357,290 shares of our common shares were held in the form of ADSs, representing 11.5% of total outstanding common shares.

The following table provides the high and low closing sale prices and the average daily trading volume of our ADSs on the Nasdaq Market based on information provided by www.adr.com.

| Calendar period | High (US\$) | Low (US\$) | Average daily trading volume (ADSs) |
|-----------------|-------------|------------|-------------------------------------|
| 2005 | | | |
| First quarter | 6.99 | 5.30 | 108,220 |
| Second quarter | 6.08 | 4.85 | 76,770 |
| Third quarter | 5.74 | 4.28 | 84,870 |
| Fourth quarter | 9.34 | 4.86 | 122,820 |
| 2006 | | | |
| First quarter | 10.34 | 6.01 | 144,930 |
| Second quarter | 8.20 | 4.82 | 129,770 |
| Third quarter | 5.35 | 3.58 | 77,850 |
| Fourth quarter | 4.22 | 3.59 | 101,180 |
| 2007 | | | |
| First quarter | 4.45 | 3.68 | 86,388 |
| Second quarter | 4.86 | 3.95 | 69,879 |
| Third quarter | 5.30 | 4.01 | 110,738 |
| Fourth quarter | 4.54 | 2.91 | 97,529 |
| 2008 | | | |
| First quarter | 4.06 | 2.74 | 46,718 |
| Second quarter | 4.40 | 2.50 | 48,714 |
| Third quarter | 3.18 | 1.37 | 35,845 |
| Fourth quarter | 1.30 | 0.64 | 28,588 |
| 2009 | | | |
| First quarter | 2.18 | 0.83 | 14,741 |
| Second quarter | 4.68 | 1.87 | 31,904 |
| Third quarter | 3.96 | 2.55 | 10,291 |
| Fourth quarter | 3.27 | 2.53 | 10,070 |
| 2010 | | | |
| January | 3.60 | 2.80 | 17,219 |
| February | 3.42 | 2.89 | 9,739 |
| March | 3.17 | 3.00 | 19,335 |
| April | 3.75 | 3.00 | 24,332 |
| May | 3.40 | 2.63 | 7,754 |

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Not applicable.

9.C. Markets

See “—9.A. Market Price Information.”

9.D. Selling Shareholders

Not applicable.

9.E. Dilution

Not applicable.

9.F. Expenses of the Issue

Not applicable.

Item 10. Additional Information**10.A. Share Capital**

Not applicable.

10.B. Articles of Incorporation

The section below provides summary information relating to the material terms of the capital stock of our company and our Articles of Incorporation. It also includes a brief summary of certain provisions of the Securities and Exchange Act, the Commercial Code and related laws of Korea, all as currently in effect.

Objectives

Article 2 of our Articles of Incorporation states our objectives, among other things, as follows:

- to develop and distribute online games and software; and
- to engage in the Internet business, software consulting, value-added communication services, character business, and publishing business.

General

Our total authorized share capital is 60,000,000 shares, which consists of common shares and preferred shares (together, referred to as “shares”) each with a par value of ₩500 per share. Under our Articles of Incorporation, holders of preferred shares are entitled to dividends of 3% or more of the par value of such shares, the exact rate to be determined by our board of Directors at the time of issuance. Our total authorized share capital changed from 40,000,000 shares to 60,000,000 shares at the extraordinary general meeting of shareholders held on June 4, 2010.

Under our Articles of Incorporation, we are authorized to issue preferred shares numbering up to one-half of our total shares issued.

As of June 28, 2010, 12,974,000 common shares were issued, and 11,856,948 common shares were outstanding. We have not issued any preferred shares. All of our issued and outstanding shares are fully paid and non-assessable and are in registered form. Pursuant to our Articles of Incorporation, we may issue additional common shares without further shareholder approval.

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Dividends

We may pay dividends to our shareholders in proportion to the number of shares owned by each shareholder. The common shares represented by the ADSs have the same dividend rights as our other common shares, except for the fees and expenses payable by the ADS holders under the deposit agreement with respect to such dividends.

We may declare annual dividends at our annual general meeting of shareholders, which is held within three months after the end of each fiscal year or declare quarterly dividends within 45 days of March 31, June 30 and September 30. We pay dividends shortly after declaration. We may distribute the annual dividend in cash or in shares and quarterly dividend only in cash. However, a dividend in shares must be distributed at par value. If the market price of the dividended shares is less than par value, dividends in shares may not exceed one-half of the annual dividends. We have no obligation to pay any dividend unclaimed for five years from the dividend payment date.

Under the Korean Commercial Code, we may pay an annual dividend only out of the excess of our net assets, on a non-consolidated basis, over the sum of:

- our stated capital,
- the total amount of our capital surplus reserve and legal reserve accumulated up to the end of the relevant dividend period, and
- the legal reserve to be set aside for the annual dividend.

We may not pay an annual dividend unless we have set aside as a legal reserve an amount equal to at least 10% of the cash portion of the annual dividend, or unless we have an accumulated legal reserve of not less than one-half of our stated capital. In addition, as a company registered with the KOSDAQ, we are required under the relevant Korean laws and regulations to set aside a certain amount every fiscal year as a reserve until our capital ratio is at least 30%. We may not use our legal reserve to pay cash dividends but may transfer amounts from our legal reserve to capital stock or use our legal reserve to reduce an accumulated deficit.

Distribution of Bonus Shares

In addition to paying dividends in shares out of our retained or current earnings, we may also distribute to our shareholders an amount transferred from our capital surplus or legal reserve to our stated capital in the form of bonus shares. We must distribute such bonus shares to all our shareholders in proportion to their existing shareholdings.

Preemptive Rights and Issuance of Additional Shares

We may issue authorized but unissued shares at the time and, unless otherwise provided in the Korean Commercial Code, on such terms as our board of Directors may determine. We must offer new shares on uniform terms to all shareholders who have preemptive rights and are listed on our shareholders' register as of the relevant record date.

We may issue new shares pursuant to a board resolution to persons other than existing shareholders, who in these circumstances will not have preemptive rights if the new shares are issued:

- to increase our capital through a general public offering pursuant to a resolution of the board of Directors in accordance with the provisions of Article 165-6 of the Korean Financial Investment Service and Capital Market Act;
- to the members of the employee stock ownership association when less than 20% of the offering is made to such members;

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- to induce foreign direct investment necessary for business in accordance with the Foreign Investment Promotion Act or to domestic companies conducting the business of technology credit guarantees or venture investment;
- to domestic or overseas financial institutions for the purpose of raising funds on an emergency basis;
- to an allied company as necessary for the development of technology;
- upon exercise of a stock option in accordance with Article 165-7 of the Korean Financial Investment Service and Capital Market Act or exercise of employee stock option pursuant to Article 32, Clause 2 of the Employee Welfare Act; and
- in the form of depositary receipts in accordance with Article 165-16 of the Korean Financial Investment Service and Capital Market Act.

We must give public notice of preemptive rights regarding new shares and their transferability at least two weeks before the relevant record date. We will notify the shareholders entitled to subscribe for newly issued shares of the subscription deadline at least two weeks prior to such deadline. If a shareholder fails to subscribe by the deadline, the shareholder's preemptive rights shall lapse. Our board of Directors may determine how to distribute shares for which preemptive rights have not been exercised, as well as fractional shares.

General Meeting of Shareholders

We hold the annual general meeting of shareholders within three months after the end of each fiscal year. Subject to a board resolution or court approval, we may hold an extraordinary general meeting of shareholders:

- as necessary;
- at the request of shareholders holding an aggregate of 3% or more of our outstanding shares for at least six months; or
- at the request of our statutory auditor.

We must give shareholders written notice setting out the date, place and agenda of the meeting at least two weeks prior to the general meeting of shareholders. However, for holders of not more than 1% of the total number of issued and outstanding voting shares, we may give notice by placing at least two public notices in at least two daily newspapers at least two weeks in advance of the meeting. Currently, we use The Korea Economic Daily News and Maeil Business Newspaper for this purpose. Shareholders not on the shareholders' register as of the record date are not entitled to receive notice of the general meeting of shareholders or attend or vote at the meeting. Holders of preferred shares, unless enfranchised, are not entitled to receive notice of or vote at general meetings of shareholders.

Our shareholders meetings are held at our head office or other adjacent areas as deemed necessary.

Voting Rights

Holders of our common shares are entitled to one vote for each common share. However, common shares held by us (i.e., treasury shares) or by any corporate entity in which we have, directly or indirectly, greater than a 10% interest, do not exercise voting rights. The Korean Commercial Code permits cumulative voting pursuant to which each common share entitles the holder thereof to multiple voting rights equal to the number of Directors to be elected at such time. A holder of common shares may exercise all voting rights with respect to his or her shares cumulatively to elect one Director. However, our shareholders have decided not to adopt cumulative voting.

Our shareholders may adopt resolutions at a general meeting by an affirmative majority vote of the voting shares present or represented at the meeting, where the affirmative votes also represent at least one-fourth of our total voting shares then issued and outstanding. However, under the Korean Commercial Code and our Articles of Incorporation, the following matters require approval by the holders of at least two-thirds of the voting shares

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present or represented at a meeting, where the affirmative votes also represent at least one-third of our total voting shares then issued and outstanding:

- amending our Articles of Incorporation;
- removing a Director;
- effecting a capital reduction;
- effecting any dissolution, merger or consolidation with respect to Webzen;
- transferring all or any significant part of our assets and/or business;
- acquiring all of the business of any other company or a part of the business of any other company having a material effect on our business; or
- any other matters for which such resolution is required under relevant laws and regulations.

In general, holders of preferred shares (other than enfranchised preferred shares) are not entitled to vote on any resolution or receive notice of any general meeting of shareholders. However, in the case of amendments to our Articles of Incorporation, any merger or consolidation, any capital reductions or in some other cases that affect the rights or interests of the preferred shares, approval of the holders of such class of shares is required. We must obtain the approval, by a resolution, of holders of at least two-thirds of the preferred shares present or represented at a class meeting of the holders of such class of shares, where the affirmative votes also represent at least one-third of our total issued and outstanding shares of such class. In addition, if we are unable to pay dividends on preferred shares as provided in our Articles of Incorporation, the holders of preferred shares will become enfranchised and will be entitled to exercise voting rights until the dividends are paid. The holders of enfranchised preferred shares have the same rights as holders of voting shares to request, receive notice of, attend and vote at a general meeting of shareholders.

Shareholders may exercise their voting rights by proxy. Under our Articles of Incorporation, the person exercising the proxy does not have to be a shareholder. A person with a proxy must present a document evidencing a power of attorney in order to exercise such voting rights.

Holders of ADRs will exercise their voting rights through the ADR depository. Subject to the provisions of the deposit agreement, ADR holders will be entitled to instruct the depository on how to vote the common shares underlying their ADSs.

Rights of Dissenting Shareholders

In some limited circumstances, including the transfer of all or any significant part of our business and our merger or consolidation with another company, dissenting shareholders have the right to require us to purchase their shares. To exercise this right, shareholders must submit to us a written notice of their intention to dissent before the applicable general meeting of shareholders. Within 20 days after the relevant resolution is passed, the dissenting shareholders must request us in writing to purchase their shares. We are obligated to purchase the shares of dissenting shareholders within one month after the expiration of the 20-day period. The purchase price for the shares is required to be determined through negotiations between us and the dissenting shareholders. If we cannot agree on a price through negotiation, the purchase price will be the average of (1) the weighted average of the daily share prices on the KOSDAQ for the two-month period before the date of the adoption of the relevant board of Directors resolution, (2) the weighted average of the daily share price on the KOSDAQ for the one-month period before the date of the adoption of the relevant board of Directors resolution and (3) the weighted average of the daily share price on the KOSDAQ for the one-week period before such date of the adoption of the relevant board of Directors resolution. However, the FSC may adjust this price if we or at least 30% of the dissenting shareholders do not accept the purchase price. Holders of ADSs will not be able to exercise dissenter's rights unless they withdraw the underlying common shares and become our direct shareholders.

[Table of Contents](#)***Register of Shareholders and Record Dates***

Our transfer agent, Hana Bank, maintains the register of our shareholders at its office located at 43-2 Yoido-dong, Youngdeungpo-ku, Seoul, Korea. It registers transfers of shares on the register of shareholders on presentation of the share certificates.

The record date for annual dividends is December 31 of each year. For the purpose of determining shareholders entitled to annual dividends, the register of shareholders may be closed for the period from January 1 to January 31 of each year. Further, for the purpose of determining the shareholders entitled to some other rights pertaining to the shares, we may, on at least two weeks' public notice, set a record date and/or close the register of shareholders for not more than three months. The trading of shares and the delivery of share certificates may continue while the register of shareholders is closed.

Annual Report

At least one week before the annual general meeting of shareholders, we must make our annual report and audited non-consolidated financial statements available for inspection at our principal office and at all of our branch offices. In addition, copies of annual reports, the audited financial statements and any resolutions adopted at the general meeting of shareholders will be available to our shareholders.

Under the Korean Financial Investment Service and Capital Market Act, we must file with the FSC and the KRX, an annual report within 90 days after the end of our fiscal year and interim reports with respect to the three-month period, six-month period and nine-month period from the fiscal year within 45 days following the end of each period. Copies of these reports are or will be available for public inspection at the FSC and the KSDA.

Transfer of Shares

Under the Korean Commercial Code, the transfer of shares is effected by delivery of share certificates. However, to assert shareholders' rights against us, the transferee must have his or her name and address registered on our register of shareholders. For this purpose, a shareholder is required to file his or her name, address and seal with our transfer agent. A non-Korean shareholder may file a specimen signature in place of a seal, unless he is a citizen of a country with a sealing system similar to that of Korea. In addition, a non-resident shareholder must appoint an agent authorized to receive notices on his or her behalf in Korea and file a mailing address in Korea. The above requirement does not apply to the holders of ADSs.

Under current Korean regulations, Korean securities companies and banks, including licensed branches of non-Korean securities companies and banks, investment trust companies, futures trading companies, and internationally recognized foreign custodians and the Korea Securities Depository may act as agents and provide related services for foreign shareholders. Certain foreign exchange controls and securities regulations apply to the transfer of shares by non-residents or non-Koreans.

Acquisition of Shares by Us

We may not acquire our own common shares except in limited circumstances, such as reduction in capital and acquisition of our own common shares for the purpose of granting stock options to our officers and employees. Under the Korean Commercial Code and the Korean Financial Investment Service and Capital Market Act, except in the case of a reduction of capital (in which case we must retire the common shares immediately), we must resell any common shares acquired by us to a third party within a reasonable time. Notwithstanding the foregoing restrictions, under the Korean Financial Investment Service and Capital Market Act, we may acquire our common shares through purchases on the KOSDAQ market or through a tender offer. We may also acquire interests in our common shares through agreements with trust companies, securities investment trust companies and securities investment companies. The aggregate purchase price for the common shares may not exceed the total amount available for distribution of dividends at the end of the preceding fiscal year less the amounts of dividends and legal reserve required to be set aside for that fiscal year and treasury shares acquired year-to-date, subject to certain procedural requirements. Corporate entities in which we own a 50% or greater equity interest may not acquire our common

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shares. See “Item 16E. Purchase of Equity Securities by the Issuer and Affiliated Purchasers” for information on share repurchases by us.

Liquidation Rights

In the event of our liquidation, after payment of all debts, liquidation expenses and taxes, our remaining assets will be distributed among shareholders in proportion to their shareholdings.

10.C. Material Contracts

- In April 2009, we entered into a service agreement with NHN Games to have it develop and maintain our game Parfait Station. Under the agreement, NHN Games undertook to develop our discontinued online game Parfait Station, deliver by a certain date a version that is ready to be commercialized and maintain the game after commercialization in exchange for certain installment payments (₩3.0 billion in total) during the development stage and 20-50% of net revenue generated from the game after commercialization.
- In May 2009, we entered into a three-year exclusive license agreement with NHN USA to distribute Soul of the Ultimate Nation (SUN) in the United States, Canada, Mexico and the United Kingdom through www.ijji.com. Under the agreement, we are to receive software development and installation fees in the amount of US\$300,000, 30% of net revenue generated in the licensed territory as running royalty (with minimum guarantee amounts) and additional incentives when certain milestone sales figures are achieved.
- On May 2009, an amendment to the original publishing agreement was made to waive our obligation to make any additional payments relating to T-project partly in exchange for Red 5 Studios’ publishing rights in the United States and Europe. Under the amendment, Red 5 Studios will pay us 10% of the revenue from the United States and Europe for five years after commercialization and an additional 5% of such revenue (with quarterly cap of US\$2,083,333 with respect to the 5% additional revenue) for the first three-year period after commercialization. We will remain the exclusive publisher of the game in all other markets throughout the world, but we are to pay Red 5 Studios 50% of such revenue from other markets for five years after commercialization.
- On July 31, 2009, we entered into a sales agreement with KINX and sold our office space in 467-6, Dogok-dong, Kangnam-gu, Seoul, Korea for ₩2,480 million.
- On August 1, 2009, we entered into a joint venture agreement with NHN Games where we will provide MU and SUN online and NHN Games will provide Archlord and R2 through a global game portal called webzen.com. We will transfer any revenue generated on NHN Games’ title every month. The term of the agreement is to end on July 31, 2012, and will be automatically renewed for one year unless a party notifies the other of its intent to terminate the agreement one month prior to the end of each contract period.
- On December 31, 2009, Webzen Taiwan, our subsidiary, entered into an internet game distribution and service agreement with NHN Games Corp. to provide R2 in Taiwan. Webzen Taiwan will pay NHN Games Corp. 40% of all revenue excluding fees paid to third parties for distribution.
- On February 12, 2010, we entered into a publishing agreement with NHN Games to service Battle Territory, a game developed by NHN Games. We will pay ₩1,750 million NHN Games as license fee and divide equally the profit generated by the offering of Battle Territory.
- On April 16, 2010, we entered into a channeling agreement with NHN Corp. where NHN Corp. will offer Huxley: The Dystopia through Hangame, a major game portal owned and operated by NHN Corp. We will pay NHN Corp. 40% of the profit.

The above agreements are online game publishing rights, game development and license agreements that were entered into in the ordinary course of our business.

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10.D. Exchange Controls

General

The Korean Foreign Exchange Transaction Law and the Presidential Decree and regulations under such Act and Decree (collectively, the “Foreign Exchange Transaction Laws”) regulate investment in Korean securities by non residents and issuance of securities outside Korea by Korean companies. Under the Foreign Exchange Transaction Laws, non residents may invest in Korean securities only to the extent specifically allowed by such laws or otherwise permitted by the MOFE. The FSC has also adopted, pursuant to its authority under the Korean Financial Investment Service and Capital Market Act, regulations that restrict investment by foreigners in Korean securities.

Under the Foreign Exchange Transaction Laws, if the government deems that certain emergency circumstances, including, but not limited to, extreme difficulty in stabilizing the balance of payments or substantial disturbance in the Korean financial and capital markets, are likely to occur, it may impose any necessary restrictions, such as requiring foreign investors to obtain prior approval from the MOFE for the acquisition of Korean securities or for the repatriation of dividends or sales proceeds arising from Korean securities or from disposition of such securities.

Reporting Requirements for Holders of Substantial Interests

Any person whose direct or beneficial ownership of shares (whether in the form of shares or ADSs), certificates representing the right to subscribe for shares, certain equity related debt securities, such as convertible bonds, exchangeable bonds and bonds with warrants, and certain derivatives-combined securities whose underlying assets are the above-mentioned securities (collectively, the “Equity Securities”), together with the Equity Securities beneficially owned by certain related persons or by any person acting in concert with such person that account for 5% or more of the total outstanding Equity Securities, is required to report the status, purpose (in terms of whether the purpose of shareholding is to affect control over management of the issuer), forms (direct ownership or beneficial ownership) of such holding and major contracts with regard to the Equity Securities held by the person to the FSC and the KRX within five business days after reaching the 5% ownership interest threshold. In addition, any change (1) in the ownership interest subsequent to such report which equals or exceeds 1% of the total outstanding Equity Securities, (2) in the shareholding purpose, (3) in the major contracts with regard to the relevant Equity Securities, or (4) in the shareholding form is required to be reported to the FSC and the KRX within five business days from the date of such change. However, the reporting deadline of such reporting requirement is extended for investors who hold shares for purposes other than management control and for the Government, municipal authorities, the Bank of Korea and certain public institutions to the tenth day of the month immediately following the month in which the shares were acquired or the shareholdings were otherwise changed. Those who report that the purpose of their shareholding is to affect control over management of the issuer are prohibited from exercising their voting rights and acquiring additional shares during the period from the day any event subject to the above reporting requirements occurs to five days subsequent to the report. Any investor who has filed the above report is required to send a copy of the report to the issuer of the Equity Securities immediately.

Violation of these reporting requirements may subject a person to criminal sanctions, such as fines or imprisonment, and may result in a loss of voting rights with respect to the ownership of Equity Securities exceeding 5%. Furthermore, the FSC may issue an order to dispose of such non-reported Equity Securities.

Restrictions Applicable to ADSs

No Korean governmental approval is necessary for the sale and purchase of ADSs in the secondary market outside Korea or for the withdrawal of shares underlying ADSs and the delivery inside Korea of shares in connection with such withdrawal, provided that a foreigner who intends to acquire such shares must obtain an Investment Registration Card from the Financial Supervisory Service as described below. The acquisition of such shares by a foreigner must be reported immediately by the foreigner or his standing proxy in Korea to the Governor of the FSS (the “Governor”).

Persons who have acquired shares as a result of the withdrawal of shares underlying the ADSs may exercise their preemptive rights for new shares, participate in free distributions and receive dividends on shares without any further governmental approval.

[Table of Contents](#)***Restrictions Applicable to Shares***

As a result of amendments to the Foreign Exchange Transaction Laws and FSC regulations (together, the “Investment Rules”) adopted in connection with the stock market opening from January 1992 and after that date, foreigners may invest, with certain exceptions and subject to certain procedural requirements, in all shares of Korean companies, whether listed on KRX Stock Market or KOSDAQ Market, unless prohibited by specific laws. Foreign investors may trade shares listed on KRX Stock Market or KOSDAQ Market only through KRX Stock Market or the KOSDAQ Market, except in limited circumstances, including:

- odd lot trading of shares;
- acquisition of shares by exercise of warrant, conversion right under equity linked securities or withdrawal right under depositary receipts issued outside of Korea by a Korean company (“Converted Shares”);
- acquisition of shares by foreign companies as a result of merger;
- acquisition of shares as a result of inheritance, donation, bequest or exercise of shareholders’ rights, including preemptive rights or rights to participate in free distributions and receive dividends;
- acquisition of shares offered and subscribed overseas for listing on foreign securities exchanges;
- over the counter transactions between foreigners of a class of shares for which the ceiling on aggregate acquisition by foreigners, as explained below, has been reached or exceeded;
- acquisition of underlying shares by an overseas depositary in relation to the issuance of depositary receipts;
- disposition of shares through the exercise of a dissenting shareholder’s appraisal right;
- acquisition of shares by direct investment pursuant to the Foreign Investment Promotion Act and disposition of shares so acquired;
- acquisition or disposition of shares through a tender offer; and
- acquisition or disposition of shares through the electronic over the counter market brokerage companies.

For over the counter transactions between foreigners outside KRX Stock Market or KOSDAQ Market involving shares with respect to which the limit on aggregate foreign ownership has been reached or exceeded, an investment broker such as a securities company licensed in Korea must act as an intermediary. Odd lot trading of shares outside KRX Stock Market or KOSDAQ Market must involve an investment trader such as a securities company licensed in Korea as the other party. Foreign investors are prohibited from engaging in margin transactions by using securities borrowed from securities companies in Korea with respect to shares that are subject to a foreign ownership limit.

The Investment Rules require a foreign investor who wishes to invest in shares on KRX Stock Market or KOSDAQ Market (including Converted Shares) to register its identity with the FSS prior to making any such investment; however, such registration requirement does not apply to foreign investors who acquire Converted Shares with the intention of selling such Converted Shares within three months from the date of acquisition thereof. Upon registration, the FSS will issue to the foreign investor an Investment Registration Card, which must be presented each time the foreign investor opens a brokerage account with a securities company. Foreigners eligible to obtain an Investment Registration Card include foreign nationals who are individuals residing abroad for more than six months, foreign governments, foreign municipal authorities, foreign public institutions, international organizations incorporated under international covenants, corporations incorporated under foreign laws and certain foreign funds and partnerships. All Korean offices of a foreign corporation as a group are treated as a separate foreigner from the offices of the corporation outside Korea. However, a foreign corporation or depositary issuing depositary receipts may obtain one or more Investment Registration Cards in its name in certain circumstances as described in the relevant regulations.

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Upon a foreign investor's purchase of shares through the KRX Stock Market or KOSDAQ Market, no separate report by the investor is required, because the Investment Registration Card system is designed to control and oversee foreign investment through a computer system. However, a foreign investor's acquisition or sale of shares outside the KRX Stock Market (as discussed above) must be reported by the foreign investor or its standing proxy to the Governor at the time of each such acquisition or sale. A foreign investor must ensure that any acquisition or sale by it of shares outside KRX Stock Market or KOSDAQ Market, in the case of trades in connection with a tender offer, odd lot trading of shares or trades of a class of shares for which the aggregate foreign ownership limit has been reached or exceeded, is reported to the Governor by the securities company engaged to facilitate such transaction. A foreign investor must appoint one or more standing proxies from among the Korea Securities Depository, foreign exchange banks (including domestic branches of foreign banks), investment traders (such as securities companies), investment brokers (such as securities companies), collective investment business companies (such as asset management companies), and foreign custodians meeting certain requirements to act as a standing proxy to exercise shareholders' rights, place an order to sell or purchase shares or perform any matter related to the foregoing activities if the foreign investor does not perform these activities itself. However, a foreign investor may be exempted from complying with these standing proxy rules with the approval of the Governor in circumstances where such compliance is made impracticable, including cases where such compliance would contravene the laws of the home country of such foreign investor.

Certificates evidencing shares of Korean companies must be kept in custody with an eligible custodian in Korea. Only foreign exchange banks (including domestic branches of foreign banks), investment traders (such as securities companies), investment brokers (such as securities companies), collective investment business companies (such as asset management companies), foreign custodians meeting certain requirements and the Korea Securities Depository are eligible to act as a custodian of shares for a nonresident or foreign investor. A foreign investor must ensure that its custodian deposits such shares with the Korea Securities Depository. However, a foreign investor may be exempted from complying with this deposit requirement with the approval of the Governor in circumstances where such compliance is made impracticable, including cases where such compliance would contravene the laws of the home country of such foreign investor.

Under the Investment Rules, with certain exceptions, foreign investors may acquire shares of a Korean company without being subject to any foreign investment ceiling. As one such exception, designated public corporations are subject to a 40% ceiling on the acquisition of shares by foreigners in the aggregate. Furthermore, an investment by a foreign investor of not less than 10% of the outstanding shares of a Korean company is defined as a direct foreign investment under the Foreign Investment Promotion Law, which is, in general, subject to the report to, and acceptance by, the MKE, which delegates its authority to the Korea Trade Investment Promotion Agency, or foreign exchange banks (including domestic branches of foreign banks) under the relevant regulations. The acquisition of shares of a Korean company by a foreign investor may also be subject to certain foreign shareholding restrictions in the event that such restrictions are prescribed in each specific law which regulates the business of such Korean company. For example, we are currently subject to a foreign shareholding ceiling of 49%, pursuant to the Telecommunications Business Law. A foreigner who has acquired shares in excess of this ceiling may not exercise its voting rights with respect to the shares exceeding this limit, and the MKE may take corrective action pursuant to the Telecommunications Business Law.

Under the Foreign Exchange Transaction Laws, a foreign investor who intends to acquire shares must designate a foreign exchange bank at which it must open a foreign currency account and a Won account exclusively for stock investments. No approval is required for remittance into Korea and deposit of foreign currency funds in the foreign currency account. Foreign currency funds may be transferred from the foreign currency account at the time required to place a deposit for, or settle the purchase price of, a stock purchase transaction to a Won account opened at a securities company. Funds in the foreign currency account may be remitted abroad without any governmental approval.

Dividends on shares are paid in Won. No governmental approval is required for foreign investors to receive dividends on, or the Won proceeds of the sale of, any such shares to be paid, received and retained in Korea. Dividends paid on, and the Won proceeds of the sale of, any such shares held by a nonresident of Korea must be deposited either in a Won account with the investor's securities company or his Won account. Funds in the investor's Won account may be transferred to his foreign currency account or withdrawn for local living expenses

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up to certain limitations. Funds in the Won account may also be used for future investment in shares or for payment of the subscription price of new shares obtained through the exercise of preemptive rights.

Securities companies (including domestic branches of foreign securities companies) in Korea are allowed to open foreign currency accounts and Won accounts with foreign exchange banks exclusively for accommodating foreign investors' stock investments in Korea. Through such accounts, these securities companies may enter into foreign exchange transactions on a limited basis, such as conversion of foreign currency funds and Won funds, either as a counterparty to or on behalf of foreign investors, without such investors having to open their own accounts with foreign exchange banks.

10.E. Taxation

Korean Taxation

The following is a summary of material Korean tax consequences to owners of our ADSs and common shares that are non-resident individuals or non-Korean corporations without a permanent establishment in Korea to which the relevant income is attributable. Such non-resident individuals or non-Korean corporations will be referred to as non-resident holders below. The statements regarding Korean tax laws set forth below are based on the laws in force and as interpreted by the Korean taxation authorities as of the date hereof. This discussion is not exhaustive of all possible tax considerations which may apply to a particular investor, and prospective investors are advised to satisfy themselves as to the overall tax consequences of the acquisition, ownership and disposition of our Common Shares or ADSs, including specifically the tax consequences under Korean law, the laws of the jurisdiction of which they are resident, and any tax treaty between Korea and their country of residence, by consulting their own tax advisers.

Dividends on the Shares or ADSs

We will deduct Korean withholding tax from dividends paid to you at a rate of 27.5%. If you are a resident in a country that has entered into a tax treaty with Korea, you may qualify for a reduced rate of Korean withholding tax.

For example, if you are a qualified resident of the United States for purposes of the tax treaty between the United States and Korea and you are the "beneficial owner" of a dividend, a reduced withholding tax rate of 16.5%, including local surtax, generally will apply. If you are a beneficial owner of ADSs, you will generally be entitled to benefits under the tax treaty between the United States and Korea if you:

- are an individual U.S. resident, a U.S. corporation (or other entity treated as a United States corporation for United States tax purposes) or in the case of a person acting as a partner or fiduciary, only to the extent your income is subject to taxation in the United States as the income of a U.S. resident;
- are not deemed to be a resident of Korea for purposes of the tax treaty between the United States and Korea;
- are not subject to any anti-treaty shopping article that applies in limited circumstances; and
- do not hold ADSs in connection with the conduct of business in Korea through a permanent establishment or the performance of independent personal services in Korea through a fixed base.

In order to obtain the benefits of a reduced withholding tax rate under a tax treaty, you must submit to us, prior to the dividend payment date, such evidence of tax residence as may be required by the Korean tax authorities. Holders of ADSs may submit evidence of tax residence to us through the depository for the ADSs. Holders of common shares may submit evidence of tax residence to us through the Korea Securities Depository. Excess taxes withheld generally are not recoverable even if you subsequently produce evidence that you were entitled to have tax withheld at a lower rate.

If we distribute to you bonus shares representing a transfer of certain capital reserves or asset revaluation reserves into paid-in capital, that distribution may be subject to Korean tax.

[Table of Contents](#)*Taxation of Capital Gains*

You are exempt from Korean taxation on capital gains realized upon sale of shares through the KRX Stock Market or KOSDAQ if you have owned, together with certain related parties, less than 25% of our total issued and outstanding shares at any time during the year of sale and the five calendar years before the year of sale, provided that you have no permanent establishment in Korea (whether or not such capital gains are attributable to the permanent establishment). If you are a resident of the United States for purposes of the tax treaty between the United States and Korea, you will be exempt, subject to certain limited exceptions, from Korean taxation on the capital gains realized by the disposition of common shares or ADSs. Further, the Korean taxation authorities have issued a tax ruling confirming that capital gains earned by a non-Korean holder (whether or not it has a permanent establishment in Korea) from the transfer of ADSs outside of Korea are exempt from Korean taxation by virtue of the Special Tax Treatment Control Law of Korea.

If you are subject to tax on capital gains with respect to the sale of ADSs, or of shares which you acquired as a result of a withdrawal, your gain will be calculated based on your cost of acquiring the ADSs representing such shares, although there are no specific Korean tax provisions or rulings on this issue. In the absence of the application of a tax treaty which exempts or reduces the rate of tax on capital gains, the amount of Korean tax imposed on your capital gains will be the lesser of 11% (including resident surtax) of the gross realization proceeds and, subject to the production of satisfactory evidence of the acquisition cost and transfer expenses of the ADSs, 27.5% (including resident surtax) of the net capital gains. The gain is calculated as the gross realization proceeds less the acquisition cost and transfer expenses.

If you sell your common shares or ADSs, the purchaser or, in the case of the sale of shares through a licensed securities company in Korea, the licensed securities company, is required to withhold Korean tax from the sales price in an amount equal to 11% of the gross realization proceeds and to make payment thereof to the Korean tax authority, unless you establish your entitlement to an exemption from taxation under an applicable tax treaty or produce satisfactory evidence of your acquisition and transfer costs for the ADSs. In order to obtain the benefit of an exemption or reduced rate of tax pursuant to a tax treaty, you must submit to the purchaser or the securities company (or through the depository), as the case may be, the application for tax exemption along with a certificate of your tax residency issued by a competent authority of your tax residence country prior to or at the time of payment. Excess taxes withheld are generally not recoverable even if you subsequently produce evidence that you were entitled to have taxes withheld at a lower rate.

Inheritance Tax and Gift Tax

If you die while holding an ADS or transfer an ADS as a gift, it is unclear whether, for Korean inheritance and gift tax purposes, you will be treated as the owner of the common shares underlying the ADSs. If you are treated as the owner of the common shares, the heir or the donee (or you, if the donee fails to pay) will be subject to Korean inheritance or gift tax presently at the rate of 10% to 50%, provided that the value of such common shares or ADSs is greater than a specified amount.

Securities Transaction Tax

You will not pay a securities transaction tax on your transfer of ADSs. If you transfer shares, you will be subject to a securities transaction tax at the rate of 0.15% and an agriculture and fishery special tax at the rate of 0.15% of the sale price of the shares when traded on the Korea Stock Exchange. If you transfer shares through KOSDAQ, you will be subject to a securities transaction tax at the rate of 0.3% of the sales price of the shares and will not be subject to an agriculture and fishery special tax. If your transfer of shares is not made on the KRX Stock Market or KOSDAQ, subject to certain exceptions, you will be subject to a securities transaction tax at the rate of 0.5% and will not be subject to an agriculture and fishery special tax.

The securities transaction tax and the agriculture and fishery special tax are not applicable if (i) shares are listed on a designated foreign stock exchange (e.g., New York Stock Exchange or Nasdaq Market) and (ii) the sale of shares takes place on such exchange.

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According to a tax ruling issued by the Korean tax authorities, foreign shareholders are not subject to a securities transaction tax upon the deposit of underlying shares and receipt of depositary shares or upon the surrender of depositary shares and withdrawal of originally deposited underlying shares. However, questions have been raised as to whether this ruling is also applied to the surrender of depositary shares. Although the tax authorities recently issued another tax ruling indicating that securities transaction tax would be imposed “when depositary shares which were issued upon deposit with an overseas depositary of stock issued by a Korean company are later converted into the underlying stock,” except for particular type of transaction mentioned in such ruling issued by the Korean tax authorities, it is not clear as to whether, on whom, when and in what amount the securities transaction tax will be imposed in the case of withdrawals of underlying shares by holders of depositary shares other than initial holders. Accordingly, there can be no assurance that the holders of ADSs other than initial holders will not be subject to the securities transaction tax when they withdraw the shares upon surrendering the ADSs.

U.S. Federal Income Tax Considerations

The following is a description of the material U.S. federal income tax consequences to the U.S. holders described below of owning and disposing of common shares or ADSs, but it does not purport to be a comprehensive description of all tax considerations that may be relevant to a particular person’s decision to hold such securities. This discussion applies only if you hold common shares or ADSs as capital assets for tax purposes. In addition, it does not describe all of the tax consequences that may be relevant in light of your particular circumstances, including alternative minimum tax consequences and tax consequences applicable to U.S. holders subject to special rules, such as:

- certain financial institutions;
- dealers or traders in securities who use a mark-to-market method of tax accounting;
- persons holding common shares or ADSs as part of a hedging transaction, straddle, wash sale, conversion transaction or integrated transaction or persons entering into a constructive sale with respect to the common shares or ADSs;
- persons whose functional currency for U.S. federal income tax purposes is not the U.S. dollar;
- entities classified as partnerships for U.S. federal income tax purposes;
- tax-exempt entities, including an “individual retirement account” or “Roth IRA”;
- persons that own or are deemed to own ten percent or more of our voting stock;
- persons who acquired our common shares or ADSs pursuant to the exercise of an employee stock option or otherwise as compensation; or
- persons holding shares in connection with a trade or business conducted outside of the United States.

If an entity that is classified as a partnership for U.S. federal income tax purposes holds common shares or ADSs, the U.S. federal income tax treatment of a partner will generally depend on the status of the partner and the activities of the partnership. Partnerships holding common shares or ADSs and partners in such partnerships should consult their tax advisers as to the particular U.S. federal income tax consequences of holding and disposing of the common shares or ADSs.

This discussion is based on the Internal Revenue Code of 1986, as amended (the “Code”), administrative pronouncements, judicial decisions and final, temporary and proposed Treasury regulations and the current income tax treaty in effect between the United States and the Republic of Korea (the “Treaty”), all as of the date hereof. These laws are subject to change, possibly on a retroactive basis. It is also based in part on representations by the depositary and assumes that each obligation under the deposit agreement and any related agreement will be performed in accordance with its terms.

The discussion below applies to you only if you are a U.S. holder. You are a U.S. holder if you are a beneficial owner of common shares or ADSs who is eligible for benefits under the Treaty and are, for U.S. federal tax purposes:

- a citizen or resident of the United States;

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- a corporation, or other entity taxable as a corporation, created or organized in or under the laws of the United States or any political subdivision thereof; or
- an estate or trust the income of which is subject to U.S. federal income taxation regardless of its source.

In general, if you own ADSs, you will be treated as the owner of the underlying shares represented by those ADSs for U.S. federal income tax purposes. Accordingly, no gain or loss will be recognized if you exchange ADSs for the underlying shares represented by those ADSs.

The U.S. Treasury has expressed concerns that parties to whom American depositary shares are released before delivery of shares to the depository (“pre-release”), or intermediaries in the chain of ownership between holders and the issuer of the security underlying the American depositary shares, may be taking actions that are inconsistent with the claiming of foreign tax credits for U.S. holders of American depositary receipts. Such actions would also be inconsistent with the claiming of the reduced rate of tax, described below, applicable to dividends received by certain non-corporate holders. Accordingly, the analysis of the creditability of Korean taxes and the availability of a lower rate of tax for dividends received by certain non-corporate holders, each described below, could be affected by actions taken by parties to whom ADSs are pre-released.

Please consult your own tax advisers concerning the U.S. federal, state, local and foreign tax consequences of owning and disposing of common shares or ADSs in your particular circumstances.

Passive Foreign Investment Company Considerations

Based on the price of our common shares and ADSs during our 2009 taxable year and the amount of passive assets, including cash and cash equivalents, held by us throughout that year, we believe that we may have been a passive foreign investment company (“PFIC”) for our 2009 taxable year. Further, there is a significant risk that we will be a PFIC in future taxable years.

In general, a non-U.S. corporation will be considered a PFIC for any taxable year in which (i) 75% or more of its gross income consists of passive income or (ii) 50% or more of the average quarterly value of its assets consists of assets that produce, or are held for the production of, passive income. For purposes of the above calculations, a non-U.S. corporation that directly or indirectly owns at least 25% by value of the shares of another corporation is treated as if it held its proportionate share of the assets of such other corporation and received directly its proportionate share of the income of such other corporation. Passive income generally includes dividends, interest, rents, royalties and capital gains.

If we are a PFIC for any taxable year during which a U.S. holder holds common shares or ADSs, such U.S. holder is subject to adverse U.S. federal income tax rules. In general, gain recognized upon a disposition (including, under certain circumstances, a constructive disposition) of common shares or ADSs by such U.S. holder is allocated ratably over the holder’s holding period for such common shares or ADSs. The amounts allocated to the taxable year of disposition and to years before we became a PFIC would be taxed as ordinary income. The amount allocated to each other taxable year would be subject to tax at the highest rate in effect for such taxable year for individuals or corporations, as appropriate, and an interest charge would be imposed on the tax attributable to such allocated amounts. Similar rules apply to any distribution received by such U.S. holder on its common shares or ADSs in excess of 125% of the average of the annual distributions on such common shares or ADSs received during the preceding three years or the holder’s holding period, whichever is shorter.

If we are a PFIC for any year during which a U.S. holder holds common shares or ADSs, we generally will continue to be treated as a PFIC with respect to the holder for all succeeding years during which the U.S. holder holds common shares or ADSs, even if we cease to meet the threshold requirements for PFIC status. U.S. holders should consult their tax advisers regarding the potential availability of a “deemed sale” election that would allow them to eliminate this continuing PFIC status under certain circumstances.

Under certain attribution rules, if we are a PFIC, U.S. holders will be deemed to own their proportionate share of any direct or indirect subsidiaries or other entities in which we own an equity interest that are also PFICs (“lower-

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tier PFICs”), and will generally be subject to U.S. federal income tax as if such holders directly held the shares of such lower-tier PFICs.

Alternatively, a U.S. holder may make a mark-to-market election with respect to the common shares or ADSs (but not with respect to the shares of any lower-tier PFICs) if the common shares or ADSs are “regularly traded” on a “qualified exchange.” The common shares or ADSs will be treated as “regularly traded” in any calendar year in which more than a de minimis quantity of common shares or ADSs are traded on a qualified exchange on at least 15 days during each calendar quarter. Our ADSs are traded on the NASDAQ Market, which is a qualified exchange.

If a U.S. holder makes the mark-to-market election, for each year in which we are a PFIC, the holder will generally include as ordinary income the excess, if any, of the fair market value of the common shares or ADSs at the end of the taxable year over their adjusted tax basis, and will be permitted an ordinary loss in respect of the excess, if any, of the adjusted tax basis of the common shares or ADSs over their fair market value at the end of the taxable year (but only to the extent of the net amount of previously included income as a result of the mark-to-market election). If a U.S. holder makes the election, the holder’s tax basis in the common shares or ADSs will be adjusted to reflect any such income or loss amounts. Any gain or loss recognized on the sale or other disposition of common shares or ADSs in a year when we are a PFIC will be treated as ordinary income or loss (but in the case of a loss, only to the extent of the net amount of previously included income as a result of the mark-to-market election). U.S. holders should consult their own tax advisers regarding the availability and advisability of making a mark-to-market election in their particular circumstances.

We will not make available the information necessary for U.S. holders to make a Qualified Electing Fund election.

If a U.S. holder owns common shares or ADSs during any year in which we are a PFIC, the holder must file an annual return with respect to us and any lower-tier PFICs. In addition, the preferential dividend rates discussed below with respect to dividends paid to certain non-corporate U.S. holders does not apply if we are a PFIC for a taxable year in which we pay a dividend or the prior taxable year.

U.S. holders should consult their own tax advisers concerning our PFIC status and the tax considerations relevant to an investment in a PFIC.

Taxation of Distributions

Subject to the passive foreign investment company rules described above, distributions paid on common shares or ADSs, other than certain pro rata distributions of common shares, will be treated as dividends to the extent paid out of our current or accumulated earnings and profits (as determined under U.S. federal income tax principles). Because we do not maintain calculations of our earnings and profits under U.S. federal income tax principles, we expect that distributions will generally be reported to U.S. holders as dividends. Subject to applicable limitations and the discussion above regarding concerns expressed by the U.S. Treasury, under current law, certain dividends paid to certain non-corporate U.S. holders in taxable years beginning before January 1, 2011 will be taxable at a maximum rate of 15%. However, such dividends will not be eligible for the reduced rates of taxation if we are a PFIC for the taxable year in which we pay the dividend or the prior taxable year. The amount of a dividend will include any amounts withheld by us or our paying agent in respect of Korean taxes. The dividend will be treated as foreign source dividend income to you and will not be eligible for the dividends received deduction generally allowed to U.S. corporations under the Code.

Dividends paid in Won will be included in your income in a U.S. dollar amount calculated by reference to the exchange rate in effect on the date of your (or in the case of ADSs, the depository’s) receipt of the dividend, regardless of whether the payment is in fact converted into U.S. dollars. If the dividend is converted into U.S. dollars on the date of receipt, you generally should not be required to recognize foreign currency gain or loss in respect of the dividend income. You may have foreign currency gain or loss if you do not convert the dividend into U.S. dollars on the date of its receipt.

Korean taxes withheld from cash dividends on common shares or ADSs at the rate provided in the Treaty will be creditable against your U.S. federal income tax liability, subject to applicable limitations that may vary depending

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upon your circumstances and subject to the discussion above regarding concerns expressed by the U.S. Treasury. Korean taxes withheld in excess of the rate provided in the Treaty will not be eligible for credit against your U.S. federal income tax liability until you exhaust all effective and practical remedies to recover such excess withholding, including the seeking of competent authority assistance from the U.S. Internal Revenue Service. See “— Korean Taxation — Dividends on the Shares or ADSs” for a description of how you can secure the Treaty rate for withholding on dividends paid by us. The limitation on foreign taxes eligible for credit is calculated separately with respect to specific classes of income. The rules governing foreign tax credits are complex and, therefore, you should consult your own tax adviser regarding the availability of foreign tax credits in your particular circumstances. Instead of claiming a credit, you may, at your election, deduct otherwise creditable Korean taxes in computing your taxable income, subject to generally applicable limitations under U.S. law.

Sale and Other Disposition of Common Shares or ADSs

Subject to the passive foreign investment company rules described above, for U.S. federal income tax purposes, gain or loss you realize on the sale or other disposition of common shares or ADSs will be capital gain or loss, and will be long-term capital gain or loss if you held the common shares or ADSs for more than one year. The amount of your gain or loss will be equal to the difference between the amount realized on the sale or other disposition and your tax basis in the common shares or ADSs disposed of. Such gain or loss will generally be U.S. source gain or loss for foreign tax credit purposes.

Information Reporting and Backup Withholding

Information returns may be filed with the U.S. Internal Revenue Service (the “IRS”) in connection with the payment of dividends and sales proceeds. You may be subject to backup withholding tax on these payments if you fail to provide your taxpayer identification number to the paying agent and comply with certain certification procedures or otherwise establish an exemption from backup withholding.

The amount of any backup withholding from a payment to you will be allowed as a credit against your U.S. federal income tax liability and may entitle you to a refund, provided that the required information is timely furnished to the IRS.

Recently enacted legislation requires U.S. individuals (or certain entities formed by or for U.S. individuals) to report to the IRS information with respect to assets held in accounts maintained by non-U.S. financial institutions when certain conditions are met, generally beginning in 2011. Investors who fail to report required information could be subject to substantial penalties. You should consult your tax advisers regarding this legislation.

10.F. Dividends and Paying Agents

Not applicable.

10.G. Statements by Experts

Not applicable.

10.H. Documents on Display

We are subject to the information requirements of the Exchange Act, and, in accordance therewith, we file with the SEC annual reports on Form 20-F within six months of our fiscal year-end, and provide to the SEC other material information on Form 6-K. These reports and other information can be inspected at the public reference room at Room 1580, 100 F Street, N.E., Washington, D.C. 20549. You can also obtain copies of the material from the public reference room or by calling at 1-800-732-0330 or writing the SEC upon payment of a prescribed fee. Our SEC filings, including the annual reports on Form 20-F, are also available on the SEC’s website at www.sec.gov. As a foreign private issuer, we are exempt from the rules under the Exchange Act prescribing the furnishing and content of proxy statements to shareholders and Webzen’s executive officers, Directors and principal shareholders are exempt from the reporting and short-swing profit recovery provisions contained in Section 16 of the Exchange Act.

We will furnish to JPMorgan Chase Bank, as depositary for the ADSs, our annual reports, which will include a review of operations and annual audited financial statements prepared in accordance with U.S. GAAP and all notices of shareholders’ meetings and other reports and communications that are made generally available to our shareholders. The depositary will make these notices, reports and communications available to holders of ADSs and will, upon our request, arrange for the mailing of these documents to all holders of record of ADSs.

On June 18, 2010, we announced our intention to delist our ADSs from NASDAQ Global Market and to deregister and terminate our reporting obligations with the SEC. We have provided a written notice to NASDAQ of the intent to delist and will arrange in due course, after consultation with NASDAQ, the date on which our ADSs will no longer be traded on NASDAQ Global Market. We plan to maintain an American Depositary Receipt program on a Level I basis, which will allow investors to hold their securities in the form of ADSs. We filed a Form 25 with the SEC on June 28, 2010 to delist from NASDAQ Global Market and terminate registration under Section 12(b) of the Exchange Act and intend to file a Form 15F to suspend, and eventually terminate, registration under Sections 12(g) and 15(d) of the Exchange Act. Once we file a Form 15F, our reporting obligations under the Exchange Act will be suspended and over time terminated.

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Not applicable.

Item 11. Quantitative and Qualitative Disclosures about Market Risk

Market risk is the risk of loss related to adverse changes in market prices, including interest rates and foreign exchange rates, of financial instruments. In the normal course of our business, we are subject to market risk associated with interest rate movements, credit risk and currency movements on non-Won denominated assets and liabilities and license and royalty revenues.

Foreign currency risk. We have exposure to some foreign currency exchange-rate fluctuations on cash flows from our subsidiaries and licensee partners denominated in U.S. dollars, Japanese Yen, NT dollars or Chinese RMB. For example, our revenues may be impacted by exchange rate fluctuations in the U.S. dollars, Japanese Yen, NT dollars or Chinese RMB when revenues at overseas subsidiaries or royalty payments are translated into Korean Won. Foreign exchange fluctuation could also affect the value of our assets. As of December 31, 2009, we had approximately ₩708 million or US\$609 thousand in foreign currencies such as U.S. Dollar, NT Dollar and Chinese RMB out of ₩64,981 million (US\$55,842 thousand) of total cash or cash equivalents. We do not expect any material change with respect to our net income as a result of a 10% hypothetical exchange rate change.

As of December 31, 2009, we had Japanese Yen denominated accounts receivables of ₩1,279 million (US\$1,099 thousand), which represented 25.2% of our total consolidated accounts receivables balance, U.S. dollar denominated accounts receivables of ₩916 million (US\$787 thousand), which represented 18.1% of our total consolidated accounts receivables balance, and NT dollars denominated accounts receivables of ₩144 million (US\$124 thousand), which represented 2.8% of our total consolidated accounts receivables balance. We also had Chinese RMB denominated accounts payable of ₩198 million (US\$170 thousand), which represented 8.2% of our total consolidated accounts payable balance. As these balances all have short maturities, exposure to foreign currency fluctuations on these balances is not significant. For example, a hypothetical 10% appreciation of the Won against the Japanese Yen, U.S. dollars, NT dollars and Chinese RMB, in the aggregate, would reduce our cash flows by ₩214 million (US\$184 thousand).

In 2009, ₩15,536 million (US\$13,351 thousand) of our revenue was derived from currencies other than the Won, primarily from the Japanese Yen in the amount of ₩6,996 million (US\$6,012 thousand), the U.S. dollar in the amount of ₩3,785 million (US\$3,253 thousand), the NT dollar in the amount of ₩3,022 million (US\$2,597 thousand), and the Chinese RMB in the amount of ₩1,733 million (US\$1,489 thousand). A hypothetical 10% depreciation in the exchange rates of these foreign currencies against the Won in 2009 would have reduced our revenue by ₩1,554 million (US\$1,335 thousand).

Credit Risk. As our cash and cash equivalents are placed with local financial institutions, we face a potential credit risk that the financial institutions may become insolvent and be unable to repay our principal and interest in a timely manner. To manage our risk, we select a number of major financial institutions which we believe to be of high credit quality and allocate our cash holdings among such institutions. However, due to the current economic downturn and the volatile financial markets, it is difficult for us to predict the financial condition of the Korean banking sector and the financial institutions that manage our cash holdings and we may be materially impacted by any widespread failure in the Korean banking sector in the future.

Interest rate risk. Our exposure to risk from changes in interest rates relates primarily to our investments in short-term financial instruments and other investments. Investments in both fixed rate and floating rate interest earning instruments carry some interest rate risk. The fair value of fixed rate securities may fall due to a rise in interest rates, while floating rate securities may produce less income than expected if interest rates fall. Partly as a result of this, our future interest income may fall short of expectations due to changes in interest rates or we may suffer losses in principal if we are forced to sell securities that have fallen in estimated fair value due to changes in interest rates. However, as substantially all of our cash equivalents consist of bank deposits and short-term money

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market instruments, we do not expect any material change with respect to our net income as a result of a 10% hypothetical interest rate change.

Substantially all of our short-term financial instruments consist of time deposits and money market deposit accounts. We do not believe that we are subject to any material market risk exposure on our short-term financial instruments, as they are readily convertible to cash and have short maturities. We do not have any derivative financial instruments hedging interest rate risk.

Item 12. Description of Securities Other than Equity Securities

Not applicable.

PART II**Item 13. Defaults, Dividend Arrearages and Delinquencies**

None.

Item 14. Material Modifications to the Rights of Security Holders and Use of Proceeds***14.A. to D. Material Modifications to the Rights of Security Holders***

On February 3, 2004, JPMorgan Chase Bank, as depositary for the ADSs, and we entered into the first amendment to the deposit agreement governing the ADSs, under which we reduced the total number of our common shares on deposit at any time with the depositary from 1,500,000 to 1,300,000. In connection with our 3-to-1 stock split on June 10, 2004, we entered into the second amendment to the deposit agreement to change the ratio of our common shares to ADSs from 1:10 to 3:10 and adjust the maximum number of common shares that may be accepted for deposit from 1,300,000 to 3,900,000. The second amendment went into effect on July 10, 2004. On December 9, 2008, we filed on Form F-6 the form of third amendment to the deposit agreement to reflect an aggregate fee of US\$0.02 per ADR per calendar year for services by JPMorgan Chase Bank in administering the ADRs.

14.E. Use of Proceeds

We completed our initial public offering of 8,700,000 ADSs, representing 870,000 common shares (2,610,000 shares after the 3-to-1 stock split) on the Nasdaq Market, in December 2003, pursuant to our registration statement on Form F-1 (File No. 333-110321), which the SEC declared effective on December 12, 2003. In the offering, we sold the ADSs at a price of \$11.17 per ADS, which resulted in aggregate net proceeds to us of approximately US\$92 million, after deducting underwriting discounts and commissions and paying offering expenses of approximately US\$4.86 million. The managing underwriter in the offering was J.P. Morgan Securities, Inc.

As of December 31, 2009, we have used a total of approximately ₩19 billion, or approximately US\$18 million, of our IPO proceeds. ₩12,120 million (US\$10,416 thousand) was used for the development of new games, ₩3,824 million (US\$3,286 thousand) was used for advertisement and marketing, ₩1,661 million (US\$1,427 thousand) was used for equipment and computer software and ₩2,233 million (US\$1,919 thousand) was used for office rent. As of December 31, 2009, we have spent all of the proceeds from our initial public offering of the ADSs. None

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of the proceeds from our initial public offering of ADSs were paid to our Directors or officers or any other affiliates of us.

Item 15. Controls and Procedures

Disclosure Controls and Procedures

Our management, with the participation of our Chief Executive Officer and Chief Financial Officer, evaluated the effectiveness of our disclosure controls and procedures (as defined in Rules 13a-15(e) and 15d-15(e) under the Exchange Act) as of December 31, 2009. Our disclosure controls and procedures are designed to ensure that the information we are required to disclose in the reports that we file or submit under the Exchange Act is (i) recorded, processed, summarized and reported within the time periods specified in the Securities and Exchange Commission's rules and forms and (ii) accumulated and communicated to our management, including the Chief Executive Officer and Chief Financial Officer, as the principal executive and financial officers, respectively, to allow timely decisions regarding required disclosures. Based on that evaluation, our Chief Executive Officer and Chief Financial Officer concluded that our disclosure controls and procedures were effective as of the end of the period covered by this report.

Management's Report on Internal Control Over Financial Reporting

Our management is responsible for establishing and maintaining adequate internal control over financial reporting. Internal control over financial reporting is defined in Rule 13a-15(f) or 15d-15(f) promulgated under the Exchange Act as a process designed by, or under the supervision of, our Chief Executive Officer and Chief Financial Officer, as our principal executive and principal financial officers, and effected by our board of Directors, management and other personnel, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles and includes those policies and procedures that:

- pertain to the maintenance of records that in reasonable detail accurately and fairly reflect the transaction and dispositions of our assets;
- provide reasonable assurance that transactions are recorded as necessary to permit preparation of financial statements in accordance with generally accepted accounting principles, and that our receipts and expenditures are being made only in accordance with authorizations of our management and Directors; and
- provide reasonable assurance regarding prevention or timely detection of unauthorized acquisition, use or disposition of our assets that could have a material effect on the financial statements.

Because of its inherent limitations, internal control over financial reporting may not prevent or detect misstatements. Projections of any evaluation of effectiveness to future periods are subject to the risk that controls may become inadequate because of changes in conditions, or that the degree of compliance with the policies or procedures may deteriorate.

Our management evaluated the effectiveness of our internal control over financial reporting as of December 31, 2009 using the criteria in "Internal Control – Integrated Framework" issued by the Committee of Sponsoring Organizations (COSO) of the Treadway Commission.

Based on our evaluation, management concluded that, as of December 31, 2009, our internal control over financial reporting was effective. The effectiveness of our internal control over financial reporting as of December 31, 2009 has been audited by Samil PricewaterhouseCoopers, an independent registered public accounting firm, as stated in their report which is included in Item 18 of this Form 20-F.

[Table of Contents](#)***Changes in Internal Control Over Financial Reporting***

There were no changes in our internal control over financial reporting that occurred during the year ended December 31, 2009 that have materially affected, or are reasonably likely to materially affect, our internal control over financial reporting.

Item 16. Reserved.***16.A. Audit Committee Financial Expert***

The Audit Committee is comprised of the following three independent Directors: Chang Won Lee, Seung Han Ha and Hyuk-Yun Kim. All of our independent Directors are financially literate and our board of Directors designated Seung-Han Ha as an audit committee financial expert, who is an independent Director, as defined in Rule 10A-3 under the Exchange Act. The Audit Committee is responsible for examining internal transactions and potential conflicts of interest and reviewing accounting and other relevant matters.

16.B. Code of Ethics

We have adopted a code of ethics that applies to each member of our board of Directors and all employees, including our Chief Executive Officer and our Chief Financial Officer. The code of ethics was filed as exhibit 11.1 to the annual report on Form 20-F filed on June 25, 2004.

16.C. Principal Accountant Fees and Services***Fees Paid to Principal Accountant***

The following table sets forth the aggregate fees by category specified below in connection with certain professional services rendered by our principal external auditor for the periods indicated. We did not pay any other fees to our principal external auditor during the periods indicated below.

| | For the year ended December 31, | | |
|--------------------|--|-----------------------|--------------------|
| | 2008 | 2009 | |
| | Won | Won | US\$(1) |
| | | (in thousands) | |
| | | | (unaudited) |
| Audit fees(2) | 460,464 | 471,650 | 405 |
| Audit-related fees | — | — | — |
| Tax fees(3) | 108,464 | 9,000 | 8 |
| All other fees(4) | — | 64,000 | 55 |

- (1) For convenience, the Won amounts are expressed in U.S. dollars at the rate of ₩1,163.65 to US\$1.00, the noon buying rate in effect on December 31, 2009 as announced by the Federal Reserve Bank of New York.
- (2) Audit fees in the table above are the aggregate fees in connection with the audits of our annual financial statements, the review of our interim financial statements and assistance with and review of registration statements and periodic SEC filings.
- (3) Tax fees in the table above include the auditor's advisory service fees with respect to our tax return and for tax audit by the Korean tax authority.
- (4) Includes consulting fee related to introduction of IFRS

Audit Committee's Pre-Approval Policies and Procedures

Our Audit Committee rules set forth that all auditing services and non-auditing services provided to us by our independent auditors should be pre-approved by the Audit Committee.

16.D. Exemptions from the Listing Standards for Audit Committees

Not applicable.

[Table of Contents](#)**16.E. Purchase of Equity Securities by the Issuer and Affiliated Purchasers**

On April 12, 2007, our board of Directors approved a program to indirectly repurchase ₩9.0 billion worth of common stock through trust accounts and, during 2007, approved a program to directly repurchase 219,611 Common Shares and indirectly repurchase 536,005 Common Shares and sell 1,033,654 Common Shares. During 2008, we directly and indirectly repurchased 635,741 Common Shares. At end of December 31, 2008, we held 1,117,052 Common Shares as treasury stock. The purpose of the share repurchase programs were to stabilize the stock price and to accumulate treasury stock for future stock option grants. There were no purchases of our common stock made by us directly or indirectly through trust accounts from January 1, 2009 until June 28, 2010.

16.F. Change in Registrant's Certifying Accountant**(a) Previous Independent Registered Public Accounting Firm**

On April 30, 2010, we dismissed Samil PricewaterhouseCoopers ("Samil PwC") as our independent registered public accounting firm. Currently Samil PwC continues to work on the US GAAP numbers for the fiscal year ended December 31, 2009 so the dismissal will take effect after such work is finalized. The dismissal of Samil PwC was approved by our Audit Committee on April 30, 2010.

The reports of Samil PwC on our financial statements as of and for the fiscal years ended December 31, 2009 and 2008 did not contain an adverse opinion or disclaimer of opinion, nor were such reports qualified or modified as to uncertainty, audit scope or accounting principle.

During the two fiscal years ended December 31, 2009 and 2008 and in any subsequent interim period prior to the dismissal of Samil PwC and through June 30, 2010, we did not have any disagreements (as defined in Item 16F(a)(1)(iv) of Form 20-F and the related instructions to Item 16F) with Samil PwC on any matter of accounting principles or practices, financial statement disclosure, or auditing scope or procedure, which disagreement, if not resolved to the satisfaction of Samil PwC, would have caused Samil PwC to make reference to the subject matter of the disagreement in its reports on the financial statements for such years. During the two fiscal years ended December 31, 2009 and 2008 and in any subsequent interim period prior to the dismissal of Samil PwC and through June 30, 2010, there were no 'reportable events' as described in Item 16F(a)(1)(v) of Form 20-F.

We furnished a copy of this disclosure to Samil PwC and requested that Samil PwC furnish us with a letter addressed to the SEC stating whether it agrees with the above statements. We have received the requested letter from Samil PwC, dated June 30, 2010, a copy of which is filed as Exhibit 99.1 to this Form 20-F.

(b) New Independent Registered Public Accounting Firm

On April 30, 2010, our Audit Committee engaged KPMG Samjong Accounting Corp. ("KPMG") as our new independent registered public accounting firm to review our financial statements for the fiscal quarter ended March 31, 2010 and audit our financial statements for fiscal year ending December 31, 2010. The decision to engage KPMG as our independent registered public accounting firm was the result of a competitive selection process.

During the two most recent fiscal years, and in any subsequent interim period prior to the appointment of KPMG, we have not consulted with KPMG regarding (i) the application of

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accounting principles to a specified transaction, either completed or proposed, or the type of audit opinion that might be rendered on our financial statements, and no written report or oral advice was provided that KPMG concluded was an important factor considered by us in reaching a decision as to any accounting, auditing or financial reporting issue, or (ii) any matter that was either the subject of a disagreement with the previous independent registered public accounting firm or a reportable event.

16.G. Corporate Governance

See “Item 6. Directors, Senior Management and Employees – 6.C. Board Practices – Difference between Nasdaq requirements and home country practices.”

PART III**Item 17. Financial Statements**

Webzen has elected to provide financial statements and related information pursuant to Item 18.

Item 18. Financial Statements

The consolidated financial statements of Webzen and the report thereon by its independent auditor listed below are attached hereto as follows:

- (a) Consolidated Balance Sheets as of December 31, 2008 and 2009 (page F-3)
- (b) Consolidated Statements of Operations for the Years Ended December 31, 2007, 2008 and 2009 (page F-4)
- (c) Consolidated Statements of Changes in Equity for the Years Ended December 31, 2007, 2008 and 2009 (pages F-5 to F-6)
- (d) Consolidated Statements of Cash Flows for the Years Ended December 31, 2007, 2008 and 2009 (pages F-7 to F-8)
- (e) Notes to Consolidated Financial Statements (pages F-9 to F-34)

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| Consolidated Statements of Operations for the Years Ended December 31, 2007, 2008 and 2009 | F-4 |
| Consolidated Statements of Changes in Equity for the Years Ended December 31, 2007, 2008 and 2009 | F-5 - F-6 |
| Consolidated Statements of Cash Flows for the Years Ended December 31, 2007, 2008 and 2009 | F-7 - F-8 |
| Notes to Consolidated Financial Statements | F-9 - F-34 |

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Report of Independent Registered Public Accounting Firm

To the Board of Directors and the Shareholders of
Webzen Inc.:

In our opinion, the accompanying consolidated balance sheets and the related consolidated statements of operations, changes in equity and cash flows present fairly, in all material respects, the financial position of Webzen Inc. and its subsidiaries (the "Company") at December 31, 2009 and 2008, and the results of their operations and their cash flows for each of the three years in the period ended December 31, 2009 in conformity with accounting principles generally accepted in the United States of America. Also, in our opinion, the Company maintained, in all material respects, effective internal control over financial reporting as of December 31, 2009, based on criteria established in *Internal Control - Integrated Framework* issued by the Committee of Sponsoring Organizations of the Treadway Commission (COSO). The Company's management is responsible for these financial statements, for maintaining effective internal control over financial reporting and for its assessment of the effectiveness of internal control over financial reporting, included in "Management's Report on Internal Control over Financial Reporting" appearing under Item 15. Our responsibility is to express opinions on these financial statements and on the Company's internal control over financial reporting based on our integrated audits. We conducted our audits in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audits to obtain reasonable assurance about whether the financial statements are free of material misstatement and whether effective internal control over financial reporting was maintained in all material respects. Our audits of the financial statements included examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements, assessing the accounting principles used and significant estimates made by management, and evaluating the overall financial statement presentation. Our audit of internal control over financial reporting included obtaining an understanding of internal control over financial reporting, assessing the risk that a material weakness exists, and testing and evaluating the design and operating effectiveness of internal control based on the assessed risk. Our audits also included performing such other procedures as we considered necessary in the circumstances. We believe that our audits provide a reasonable basis for our opinions.

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As discussed in Note 2 to the consolidated financial statements, the Company changed the manner in which it accounts for noncontrolling interests in 2009.

A company's internal control over financial reporting is a process designed to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles. A company's internal control over financial reporting includes those policies and procedures that (i) pertain to the maintenance of records that, in reasonable detail, accurately and fairly reflect the transactions and dispositions of the assets of the company; (ii) provide reasonable assurance that transactions are recorded as necessary to permit preparation of financial statements in accordance with generally accepted accounting principles, and that receipts and expenditures of the company are being made only in accordance with authorizations of management and directors of the company; and (iii) provide reasonable assurance regarding prevention or timely detection of unauthorized acquisition, use, or disposition of the company's assets that could have a material effect on the financial statements.

Because of its inherent limitations, internal control over financial reporting may not prevent or detect misstatements. Also, projections of any evaluation of effectiveness to future periods are subject to the risk that controls may become inadequate because of changes in conditions, or that the degree of compliance with the policies or procedures may deteriorate.

/s/ Samil PricewaterhouseCoopers
Seoul, Korea
June 30, 2010

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Webzen Inc. and subsidiaries
Consolidated Balance Sheets
December 31, 2008 and 2009

(In millions of Korean Won and in thousands of U.S. dollars, except per share data)

| | 2008 | 2009 | (Note 3) 2009 (Unaudited) |
|---|------------------|------------------|---------------------------------|
| Assets | | | |
| Current assets: | | | |
| Cash and cash equivalents | ₩ 41,823 | ₩ 64,981 | \$ 55,842 |
| Short-term financial instruments | 11,523 | 1,411 | 1,212 |
| Available-for-sale securities (including ₩805 and ₩2,568 of securities at fair value under ASC 825 at December 31, 2008 and 2009, respectively - see Notes 2 and 4) | 5,116 | 7,400 | 6,360 |
| Accounts receivables, net of allowance of ₩633 and ₩527 at December 31, 2008 and 2009, respectively | 4,649 | 5,064 | 4,352 |
| Other receivables | 9,413 | 11,104 | 9,543 |
| Other current assets | 2,663 | 1,456 | 1,251 |
| Total current assets | <u>75,187</u> | <u>91,416</u> | <u>78,560</u> |
| Available-for-sale securities | 1,709 | 184 | 158 |
| Property and equipment, net | 9,109 | 5,929 | 5,095 |
| Leasehold and other deposits | 10,189 | 1,584 | 1,361 |
| Other non-current assets | 3,923 | 5,254 | 4,515 |
| Total assets | <u>₩ 100,117</u> | <u>₩ 104,367</u> | <u>\$ 89,689</u> |
| Liabilities and Equity | | | |
| Current liabilities: | | | |
| Accounts payable and accrued expenses | ₩ 2,196 | ₩ 3,843 | \$ 3,303 |
| Deferred income | 7,426 | 6,208 | 5,334 |
| Other current liabilities | 846 | 906 | 779 |
| Total current liabilities | <u>10,468</u> | <u>10,957</u> | <u>9,416</u> |
| Long-term deferred income | 3,391 | 2,729 | 2,345 |
| Accrued severance benefits | 3,012 | 3,046 | 2,618 |
| Guarantee deposits | 38 | 36 | 31 |
| Other non-current liabilities | 20 | - | - |
| Total liabilities | <u>16,929</u> | <u>16,768</u> | <u>14,410</u> |
| Commitments and contingencies | | | |
| Parent Company Stockholders' equity | | | |
| Preferred stock, ₩500 par value, 6,485,000 shares authorized at December 31, 2008 and 2009, no shares issued and outstanding at December 31, 2008 and 2009 | - | - | - |
| Convertible stock, ₩500 par value, 6,485,000 shares authorized at December 31, 2008 and 2009, no shares issued and outstanding at December 31, 2008 and 2009 | - | - | - |
| Common stock, ₩500 par value 27,030,000 shares authorized at December 31, 2008 and 2009, 12,974,000 shares issued and 11,856,948 shares outstanding at December 31, 2008 and 2009 | 6,487 | 6,487 | 5,575 |
| Additional paid-in capital | 133,954 | 134,728 | 115,780 |
| Accumulated deficit | (41,628) | (38,319) | (32,930) |
| Treasury stock, 1,117,052 shares at December 31, 2008 and 2009 | (13,406) | (13,406) | (11,520) |
| Accumulated other comprehensive loss | (2,219) | (1,915) | (1,646) |
| Total parent company's stockholders' equity | <u>83,188</u> | <u>87,575</u> | <u>75,259</u> |
| Non-controlling interest | - | 24 | 20 |
| Total equity | <u>₩ 83,188</u> | <u>₩ 87,599</u> | <u>\$ 75,279</u> |
| Total liabilities and equity | <u>₩ 100,117</u> | <u>₩ 104,367</u> | <u>\$ 89,689</u> |

The accompanying notes are integral part of these financial statements.

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Webzen Inc. and subsidiaries
Consolidated Statements of Operations
Years Ended December 31, 2007, 2008 and 2009

(In millions of Korean Won and in thousands of U.S. dollars, except earnings per share data)

| | 2007 | 2008 | 2009 | (Note 3) 2009 (Unaudited) |
|---|------------|------------|------------|---------------------------------|
| Net revenue | | | | |
| Online game subscriptions | ₩ 22,884 | ₩ 22,478 | ₩ 19,833 | \$ 17,043 |
| Royalties and license fees | 6,213 | 10,298 | 10,845 | 9,320 |
| Service fees | - | - | 717 | 616 |
| Total net revenues | 29,097 | 32,776 | 31,395 | 26,979 |
| Cost of revenues | 17,505 | 15,102 | 15,634 | 13,435 |
| Gross profit | 11,592 | 17,674 | 15,761 | 13,544 |
| Operating expenses | | | | |
| Selling, general and administrative expenses | 22,848 | 24,590 | 13,761 | 11,825 |
| Research and development expenses | 23,164 | 1,816 | 2,227 | 1,914 |
| Impairment charges | - | 505 | - | - |
| Operating loss | (34,420) | (9,237) | (227) | (195) |
| Other income (expenses) | | | | |
| Interest income | 3,503 | 3,364 | 2,232 | 1,919 |
| Foreign currency gains | 239 | 3,632 | 1,358 | 1,167 |
| Foreign currency losses | (147) | (422) | (1,506) | (1,294) |
| Gain (loss) on disposal of property and equipment | 3,931 | - | 935 | 804 |
| Gain (loss) on disposal of available-for-sale securities | 3,755 | 34 | 212 | 182 |
| Gain (loss) on valuation of available-for-sale securities under ASC 825 | - | (671) | 986 | 848 |
| Loss on impairment of available-for-sale securities | - | (3,883) | (483) | (415) |
| Others, net | (118) | 156 | 938 | 804 |
| Income (loss) before income tax expenses | (23,257) | (7,027) | 4,445 | 3,820 |
| Income tax expenses | 2,579 | 802 | 1,055 | 907 |
| Net income (loss) | (25,836) | (7,829) | 3,390 | 2,913 |
| Net income (loss) attributable to non-controlling interest | (242) | (154) | 81 | 69 |
| Net income (loss) attributable to parent company | ₩ (25,594) | ₩ (7,675) | ₩ 3,309 | \$ 2,844 |
| Basic earnings (loss) per share: | | | | |
| Net income (loss) attributable to parent company common shareholders | ₩ (2,078) | ₩ (641) | ₩ 279 | \$ 0.24 |
| Diluted earnings (loss) per share: | | | | |
| Net income (loss) attributable to parent company common shareholders | ₩ (2,078) | ₩ (641) | ₩ 278 | \$ 0.24 |
| Weighted average number of shares outstanding | | | | |
| Basic | 12,319,347 | 11,982,216 | 11,856,948 | 11,856,948 |
| Diluted | 12,319,347 | 11,982,216 | 11,885,846 | 11,885,846 |

The accompanying notes are integral part of these financial statements.

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Webzen Inc. and subsidiaries
Consolidated Statements of Changes in Equity
Years Ended December 31, 2007, 2008 and 2009

(In millions of Korean Won and in thousands of U.S. dollars, except number of shares)

| | Common Shares | Common Stock | Additional Paid-in Capital | Retained Earnings (Accumulated Deficit) | Loans to Employees Related to Employee Stock Purchase Plan | Treasury Stock | Accumulated Other Comprehensive Income (Loss) | Non- Controlling Interest in Subsidiary | Total |
|--|------------------|-----------------|----------------------------------|--|--|-------------------|---|--|----------|
| Balance at January 1, 2007 | 12,212,651 | ₩ 6,486 | ₩ 136,207 | ₩ (8,359) | ₩ (58) | ₩(14,237) | ₩ 5,357 | ₩ 298 | ₩125,694 |
| Exercise of stock options | 2,000 | 1 | 2 | - | - | - | - | - | 3 |
| Treasury stock purchase | (755,616) | - | - | - | - | (9,443) | - | - | (9,443) |
| Disposition of treasury stock | 1,033,654 | - | (2,725) | - | - | 16,891 | - | - | 14,166 |
| Loans to employees related to employee stock purchase plan | - | - | - | - | 58 | - | - | - | 58 |
| Stock-based compensation | - | - | 163 | - | - | - | - | - | 163 |
| Comprehensive loss: | | | | | | | | | |
| Net loss | - | - | - | (25,594) | - | - | - | (242) | (25,836) |
| Unrealized gain on available- for-sale securities, net of tax | - | - | - | - | - | - | (5,824) | - | (5,824) |
| Foreign currency translation Adjustments | - | - | - | - | - | - | (56) | 14 | (42) |
| Total comprehensive loss | | | | | | | | | (31,702) |
| Balance at December 31, 2007 | 12,492,689 | 6,487 | 133,647 | (33,953) | - | (6,789) | (523) | 70 | 98,939 |
| Treasury stock purchase | (635,741) | - | - | - | - | (6,617) | - | - | (6,617) |
| Stock-based compensation | - | - | 307 | - | - | - | - | - | 307 |
| Comprehensive loss: | | | | | | | | | |
| Net loss | - | - | - | (7,675) | - | - | - | (154) | (7,829) |
| Unrealized gain on available- for-sale securities, net of tax | - | - | - | - | - | - | (104) | - | (104) |
| Foreign currency translation Adjustments | - | - | - | - | - | - | (1,592) | 84 | (1,508) |
| Total comprehensive loss | | | | | | | | | (9,441) |
| Balance at December 31, 2008 | 11,856,948 | 6,487 | 133,954 | (41,628) | - | (13,406) | (2,219) | - | 83,188 |
| Stock-based compensation | - | - | 774 | - | - | - | - | - | 774 |
| Comprehensive income: | | | | | | | | | |
| Net income | - | - | - | 3,309 | - | - | - | 81 | 3,390 |
| Unrealized gain on available- for-sale securities, | | | | | | | | | |

| | | | | | | | | | |
|---|-------------------|----------------|------------------|-------------------|------------|------------------|------------------|-------------|-----------------|
| net of tax Foreign currency translation Adjustments | - | - | - | - | - | - | (299) | - | (299) |
| Total comprehensive income | | | | | | | 603 | (57) | 546 |
| Balance at December 31, 2009 | <u>11,856,948</u> | <u>₩ 6,487</u> | <u>₩ 134,728</u> | <u>₩ (38,319)</u> | <u>₩ -</u> | <u>₩(13,406)</u> | <u>₩ (1,915)</u> | <u>₩ 24</u> | <u>₩ 87,599</u> |

The accompanying notes are integral part of these financial statements.

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Webzen Inc. and subsidiaries
Consolidated Statements of Changes in Equity
Years Ended December 31, 2007, 2008 and 2009

(In thousands of U.S. dollars, except number of shares)

| | Common Shares | Common Stock | Additional Paid-in Capital | Retained Earnings (Accumulated Deficit) | Loans to Employees Related to Employee Stock Purchase Plan | Treasury Stock | Accumulated Other Comprehensive Income (Loss) | Non- Controlling Interest in Subsidiary | Total |
|---|-------------------|-----------------|----------------------------------|--|--|--------------------|---|--|------------------|
| (Note3) | | | | | | | | | |
| (Unaudited) | | | | | | | | | |
| Balance at December 31, 2008 | 11,856,948 | \$ 5,575 | \$ 115,115 | \$ (35,774) | \$ - | \$ (11,520) | \$ (1,907) | \$ - | \$ 71,489 |
| Stock-based compensation | - | - | 665 | - | - | - | - | - | 665 |
| Comprehensive income: | | | | | | | | | |
| Net income | - | - | - | 2,844 | - | - | - | 69 | 2,913 |
| Unrealized gain on available-for- sale securities, net of tax | - | - | - | - | - | - | (257) | - | (257) |
| Foreign currency translation Adjustments | - | - | - | - | - | - | 518 | (49) | 469 |
| Total comprehensive income | | | | | | | | | 3,125 |
| Balance at December 31, 2009 | <u>11,856,948</u> | <u>\$ 5,575</u> | <u>\$ 115,780</u> | <u>\$ (32,930)</u> | <u>\$ -</u> | <u>\$ (11,520)</u> | <u>\$ (1,646)</u> | <u>\$ 20</u> | <u>\$ 75,279</u> |

The accompanying notes are integral part of these financial statements.

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Webzen Inc. and subsidiaries
Consolidated Statements of Cash Flows
Years Ended December 31, 2007, 2008 and 2009

(In millions of Korean Won and in thousands of U.S. dollars)

| | 2007 | 2008 | 2009 | (Note 3) 2009 (Unaudited) |
|---|-----------------|-----------------|---------------|---------------------------------|
| Cash flows from operating activities | | | | |
| Net income (loss) | ₩ (25,836) | ₩ (7,829) | ₩ 3,390 | \$ 2,913 |
| Adjustments to reconcile net income (loss) to net cash provided by (used in) operating activities | | | | |
| Depreciation and amortization | 5,441 | 4,899 | 3,483 | 2,993 |
| Provision for accrued severance benefits | 1,287 | 1,592 | 896 | 770 |
| Stock compensation expense | 163 | 307 | 774 | 665 |
| Deferred income taxes | 2,209 | 12 | 174 | 149 |
| Gain on disposal of available-for-sale securities | (3,755) | (34) | (212) | (182) |
| Loss on impairment of available-for-sale securities | - | 3,883 | 483 | 415 |
| Gain on disposal of property and equipment | (3,931) | - | (935) | (804) |
| Impairment charges | - | 505 | - | - |
| Loss (gain) on foreign currency translation | (79) | (2,216) | 755 | 649 |
| Loss (gain) on valuation of available-for-sale securities under ASC 825 | - | 671 | (986) | (848) |
| Loss (gain) on valuation of derivatives | - | (145) | 106 | 91 |
| Others | (60) | (15) | 172 | 148 |
| Changes in operating assets and liabilities | | | | |
| Accounts receivable | (262) | 1,041 | (948) | (815) |
| Other receivables | (208) | (8,570) | 8,647 | 7,431 |
| Other current assets | (196) | (502) | 610 | 525 |
| Accounts payable and accrued expenses | 806 | (3,037) | 1,923 | 1,653 |
| Deferred income | 4,716 | (1,182) | (1,709) | (1,468) |
| Other current liabilities | 117 | (91) | 95 | 82 |
| Payment of severance benefits | (2,603) | (3,112) | (932) | (801) |
| Others | 165 | (93) | 90 | 78 |
| Net cash provided by (used in) operating activities | <u>(22,026)</u> | <u>(13,916)</u> | <u>15,876</u> | <u>13,644</u> |
| Cash flows from investing activities | | | | |
| Decrease (increase) in short-term financial instruments | (2,715) | (2,897) | 10,000 | 8,594 |
| Decrease (increase) in restricted cash | (2,390) | 2,458 | 130 | 112 |
| Acquisition of available-for-sale securities | (11,656) | (19,181) | (6,985) | (6,003) |
| Proceeds from sale of available-for-sale securities | 17,651 | 9,194 | 6,467 | 5,558 |
| Increase in loans to employees | (861) | (714) | (5) | (4) |
| Decrease in loans to employees | 1,533 | 922 | 742 | 638 |
| Purchase of property, equipment and intangible assets | (1,502) | (2,198) | (1,452) | (1,248) |
| Proceeds from sale of property and equipment | 7,625 | 194 | 2,540 | 2,182 |
| Increase in leasehold and other deposits | (7,420) | (52) | (1,794) | (1,541) |
| Decrease in leasehold and other deposits | 4,730 | 11,306 | 43 | 37 |
| Increase in capitalized software development cost | - | (2,008) | (1,259) | (1,082) |
| Acquisition of other non-current assets | - | - | (1,017) | (874) |
| Others, net | - | 108 | 1 | - |
| Net cash provided by (used in) investing activities | <u>4,995</u> | <u>(2,868)</u> | <u>7,411</u> | <u>6,369</u> |
| Cash flows from financing activities | | | | |
| Issuance of common stock | 3 | - | - | - |
| Increase (decrease) in short-term borrowings | 916 | (1,192) | (30) | (26) |
| Acquisition of treasury stock | (9,443) | (6,617) | - | - |
| Proceeds from sale of treasury stock | 14,166 | - | - | - |
| Increase in leasehold deposits received | 100 | 34 | - | - |
| Repayment of leasehold deposits received | - | (972) | - | - |

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Webzen Inc. and subsidiaries
Consolidated Statements of Cash Flows
Years Ended December 31, 2007, 2008 and 2009

(In millions of Korean Won and in thousands of U.S. dollars)

| | <u>2007</u> | <u>2008</u> | <u>2009</u> | <u>(Note 3)</u> <u>2009</u> <u>(Unaudited)</u> |
|--|-----------------|-----------------|-----------------|--|
| Repayment of capital lease liability | (44) | (51) | (54) | (47) |
| Loan to employees related to employee stock purchase plan | <u>58</u> | <u>-</u> | <u>-</u> | <u>-</u> |
| Net cash provided by (used in) financing activities | <u>5,756</u> | <u>(8,798)</u> | <u>(84)</u> | <u>(73)</u> |
| Effect of exchange rate changes on cash and cash equivalents | <u>(6)</u> | <u>548</u> | <u>(45)</u> | <u>(39)</u> |
| Net increase (decrease) in cash and cash equivalents | (11,281) | (25,034) | 23,158 | 19,901 |
| Cash and cash equivalents | | | | |
| Beginning of year | <u>78,138</u> | <u>66,857</u> | <u>41,823</u> | <u>35,941</u> |
| End of year | <u>₩ 66,857</u> | <u>₩ 41,823</u> | <u>₩ 64,981</u> | <u>\$ 55,842</u> |

The accompanying notes are integral part of these financial statements.

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Webzen Inc. and subsidiaries
Notes to Consolidated Financial Statements
December 31, 2008 and 2009

1. Description of business

Webzen Inc. is engaged in developing and distributing online games principally in the Republic of Korea and in other countries within Asia. Webzen was incorporated on April 28, 2000. Webzen's principal game product "MU" is a three-dimensional massive multi-player online role playing game ("MMORPG") first introduced in May 2001. On November 14, 2006, Webzen released a three-dimensional MMORPG game "SUN" in Korea.

Webzen conducts its business within one industry segment – the business of developing and distributing online game, software licensing and other related services.

On May 21, 2003, the Company issued 2,880,000 shares of its common shares at ₩10,667 per share to the public through an initial public offering in the Republic of Korea, which generated net proceeds of ₩29,529 million. The common stock of the Company was registered with the Korea Securities Dealers Automated Quotations ("KOSDAQ") on May 23, 2003.

On December 16, 2003, the Company issued 8,700,000 American Depository Share ("ADS") representing 2,610,000 common shares at \$11.17 per ADS to the public through an initial public offering in the United States, which generated net proceeds of ₩109,799 million. The ADS of the Company was registered with the National Association of Securities Dealers Automated Quotation ("NASDAQ") in the United States of America on December 16, 2003.

On October 24, 2008, NHN Games became a largest shareholder by acquiring 23.74% of the voting shares from various shareholders including the former controlling shareholders and additionally acquired 3% voting shares on June 18, 2009. As of December 31, 2009, NHN Games has the largest ownership and voting rights over the Company, with 26.74% of the voting shares.

2. Significant accounting policies

Basis of presentation

The accompanying consolidated financial statements have been prepared in accordance with accounting principles generally accepted in the United States of America ("US GAAP"). Significant accounting policies followed by the Company in the preparation of the accompanying financial statements are summarized below.

New Accounting Standard Adopted in 2009

Effective September 30, 2009, the Financial Accounting Standards Board ("FASB") established *The FASB Accounting Standards Codification*TM ("ASC") as the source of authoritative accounting to be applied by nongovernmental entities in the preparation of financial statements in conformity with US GAAP. Except for newly issued standards which have not been codified, references to codified literature have been updated to reflect this change.

Effective January 1, 2009, the Company, as required, adopted an amendment of ASC 810, *Consolidation* (formerly referenced as the FASB's SFAS No. 160, *Noncontrolling Interest in*

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Consolidated Financial Statements), which requires certain changes to be made to the presentation of our financial statements. This amendment requires classification of earnings attributable to noncontrolling interests (previously referred to as “minority interest”) as part of consolidated net earnings (₩(-)154 million and ₩81 million for 2008 and 2009, respectively) and includes the accumulated amount of noncontrolling interests as part of equity (₩24 million at December 31, 2009). The net earnings amounts the Company has previously reported are now presented as “Net income (loss) attributable to parent company” and, as required, earnings per share continues to reflect amounts attributable only to the parent company. Similarly, in the presentation of shareowners’ equity, the Company distinguishes between equity amounts attributable to parent company shareholders and amounts attributable to the noncontrolling interest – previously classified as minority interest outside of shareowners’ equity. In addition to these financial reporting changes, this guidance provides for significant changes in accounting related to noncontrolling interests; specifically, increases and decreases in the controlling financial interest in consolidated subsidiaries will be reported in equity similar to treasury stock transactions. If a change in ownership of a consolidated subsidiary results in loss of control and deconsolidation, any retained ownership interests are remeasured with the gain or loss reported in net earnings.

Principles of consolidation

The accompanying consolidated financial statements include the accounts of Webzen and its subsidiaries (the “Company”). All significant intercompany balances and transactions have been eliminated in consolidation.

Use of estimates

The preparation of consolidated financial statements in conformity with US GAAP requires management to make estimates and assumptions that affect the amounts reported in the accompanying consolidated financial statements and related disclosures. Although these estimates are based on management’s best knowledge of current events and actions that the Company may take in the future, actual results could differ from these estimates.

Revenue recognition

Revenue recognition for games subscriptions

For the online role playing game “MU,” online subscriptions typically involve prepaid fees, which are deferred and recognized based upon their actual usage. These subscriptions are typically short-term in nature, require no additional upgrades and minor customer support.

For the online role playing game “SUN” which was commercialized on November 14, 2006, the Company started to apply a free-to-pay model. Under this model, players can access the games free of charges but may purchase points for in-game premium features. The distribution of points to the end users typically is paid by cell phone or credit card. These payments are deferred when received and revenue is recognized over the life of the premium features or as the premium features is consumed.

Software licensing

The Company receives prepaid license fees in connection with its software licensing business. These revenues are deferred and recognized over the license period. If license agreements are renewed upon

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expiration of their terms, renewal license fees are deferred and recognized ratably over the new license period.

The Company generally provides its licensees with minimal post-contract customer support on its software products, consisting of access to a support hotline and occasional unspecified upgrades, or enhancements, which typically occur within one year of the beginning of the contract. The estimated costs of providing such support are insignificant and sufficient vendor-specific evidence does not exist to allocate the revenue from software and related integration projects to the separate elements of such projects, therefore all license revenue is recognized ratably over the life of the contract.

The Company also receives royalty income from its licensees, based upon a percentage of the licensees' revenue. The related royalty revenue is recognized on a monthly basis, when the licensees confirm their sales activity for the prior period.

Service fees

Revenue from the rendering of services is recognized on a monthly basis in accordance with the contract when the services have been rendered.

The Company depends on two key products, "MU Online" and "Soul of Ultimate Nation (SUN) Online," for most of its revenues.

For the years ended December 31, 2007, 2008 and 2009, the Company generated 74%, 65% and 63% of its total revenues from "MU Online," respectively. For the years ended December 31, 2007, 2008 and 2009, the Company generated 26%, 35% and 33% of its total revenues from "Soul of Ultimate Nation (SUN) Online," respectively.

For the years ended December 31, 2007, 2008 and 2009, the Company generated 89%, 84% and 85% of its total revenues from Korea, respectively. For the years ended December 31, 2007, 2008 and 2009, the Company generated 7%, 10% and 10% of its total revenues from Taiwan, respectively. For the years ended December 31, 2007, 2008 and 2009, the Company generated 4%, 6% and 5% of its total revenues from China, respectively.

Cash and cash equivalents

Cash equivalents consist of highly liquid investments with an original maturity from the date of purchase of three months or less.

Short-term financial instruments

Short-term financial instruments represent bank time deposits, with original maturities from the date of purchase greater than three months and less than one year. The carrying value of these financial instruments approximates fair market value due to the current nature of their maturities.

Restricted cash

As of December 31, 2008 and 2009, time deposits amounting to ₩346 million and ₩226 million, respectively, have been pledged to guarantee loans made to certain employees for the acquisition of stocks. The Company cannot withdraw these bank time deposits until the employees make full

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payment to the financial institutions of their loans. As of December 31, 2008 and 2009, in connection with development of game, bank time deposits of ₩30 million and nil, respectively, resulting from government grants is restricted for use only for the development of “Huxley.” These amounts are included within financial instruments in the accompanying consolidated balance sheets.

Available-for-sale securities

On January 1, 2008, the Company adopted ASC 825, *Financial Instruments* (formerly referenced as the FASB’s SFAS No. 159, *The Fair Value Option for Financial Assets and Financial Liabilities*). The Company has elected the fair value option for two and three of its investments in short-term available-for-sale securities that were acquired during the year ended December 31, 2008 and 2009, respectively. Under the fair value option, unrealized gains and losses related to this investment are reflected in the consolidated statements of operations for the year ended December 31, 2008 and 2009. The Company’s remaining investments in long-term available-for-sale securities are accounted for as available-for-sale securities pursuant to ASC 320, *Investments-Debt and Equity Securities* (formerly referenced as the Statement of Financial Accounting Standards No. 115, *Accounting for Certain Investments in Debt and Equity Securities*). The long-term available-for-sale securities are reported on the consolidated balance sheets within other non-current assets at their estimated fair market values with any changes in the estimated fair market values being recorded as a component of accumulated other comprehensive income, net of tax. The adoption of ASC 825 did not impact retained earnings as of January 1, 2008. Investments in available-for-sale securities that had been from the balance sheet date previously classified as available-for-sale as of December 31, 2007 continued to be classified as available-for-sale as of December 31, 2008.

Available-for-sale securities with maturities less than twelve months are classified as current assets on the consolidated balance sheets. Available-for-sale securities with maturities greater than twelve months are classified as non-current assets unless such securities are intended for use in current operations and the Company has the ability to liquidate such securities prior to maturity.

Accounting for derivative instruments

The Company applies the provision of ASC 815, *Derivative and Hedging* (formerly referenced as the FASB’s SFAS No. 133, *Accounting for Derivative Instruments and Hedging Activities*). This Statement requires recognizing all derivative instruments as either assets or liabilities measured at fair value.

Under ASC 815, the Company may designate a derivative instruments as hedging the exposure to variability in expected future cash flows that are attributable to a particular risk (a “cash flow hedge”) or hedging the exposure to changes in the fair value of an asset or a liability (a “fair value hedge”). Special accounting for qualifying hedges allows the effective portion of a derivative instrument’s gains and losses to offset related results on the hedged item in the consolidated statements of operations and requires that a company formally document, designate and assess the effectiveness of the transactions that receive hedge accounting treatment. Both at the inception of a hedge and on an ongoing basis, a hedge must be expected to be highly effective in achieving offsetting changes in cash flows of fair value attributable to the underlying risk being hedged. If the Company determines that a derivative instrument is no longer highly effective as a hedge, it discontinues hedge accounting prospectively and future changes in the fair value of the derivative are recognized in current earnings. The Company

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assesses hedge effectiveness at the end of year. The Company has not elected to designate any derivative instruments as hedges for the years ended December 31, 2007, 2008 and 2009.

In accordance with ASC 815, changes in the fair value of derivative instruments that are cash flow hedges are recognized in accumulated other comprehensive income (loss) and reclassified into earnings in the period in which the hedged item affects earnings. Ineffective portions of a derivative instrument's change in fair value are immediately recognized in earnings. Derivative instruments that do not qualify, or cease to qualify, as hedges must be adjusted to fair value and the adjustments are recorded through net income.

Property and equipment

Property and equipment are stated at cost, less accumulated depreciation. Depreciation for building, equipment, furniture and fixtures, vehicles and purchased software is computed using the straight-line method over the following estimated useful lives.

| | |
|-------------------------------|-----------|
| Building | 40 years |
| Computer and equipment | 3~4 years |
| Furniture and fixtures | 3~4 years |
| Vehicles | 5 years |
| Software-externally purchased | 3~5 years |

Leasehold improvements are amortized on a straight-line basis over the shorter of the estimated useful life of the assets, or the remaining lease term, whichever is shorter.

Significant renewals and additions are capitalized at cost. Maintenance and repairs are charged to income as incurred.

As of December 31, 2008, 85%, 13% and 2% of the Company's property and equipment are located in Korea, Taiwan and China, respectively. As of December 31, 2009, 91%, 7% and 2% of the Company's property and equipment are located in Korea, Taiwan and China, respectively.

Accounting for the impairment of long-lived assets

Long-lived assets and intangible assets that do not have indefinite lives are reviewed for impairment whenever events or changes in circumstances indicate that the carrying amount of the assets may not be recoverable. When the aggregate future cash flows (undiscounted and without interest changes) is less than the carrying value of the asset, an impairment loss is recognized, based on the fair value of the asset.

Capitalized software development costs

The Company capitalizes certain software development costs relating to online games that will be distributed to consumers through subscriptions or licenses. The Company accounts for software development in accordance with ASC 985, *Costs of Software to be Sold, Leased, or Marketed* (formerly referenced as the FASB's SFAS No. 86, *Accounting for the Costs of Computer Software to be Sold, Leased, or Otherwise Marketed*). Software development costs incurred prior to the establishment of technological feasibility are expensed when incurred and are included in research and

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development expense. Once a software product has reached technological feasibility, then all subsequent software development costs for that product are capitalized until that product is available for sale. Technological feasibility is evaluated on a product-by-product basis, but typically occurs when the online game has a proven ability to operate in a massively multi-player format. After an online game is released, the capitalized product development costs are amortized to expense based on current and future revenue with an annual minimum equal to the straight-line amortization over the remaining estimated economic life of the game not exceeding three years. This expense is recorded as a component of cost of revenues. The amortization expense related to capitalized software development costs was ₩750 million, ₩750 million and ₩634 million during the years ended December 31, 2007, 2008 and 2009, respectively.

For the year ended December 31, 2008 and 2009, HUXLEY online game development cost amounting to ₩2,239 million and ₩1,438 million, respectively, which was incurred during open beta test period was capitalized. HUXLEY online game is expected to be released in 2010.

The net amount of capitalized software development costs were ₩2,929 million and ₩3,733 million at December 31, 2008 and 2009, respectively. These amounts are included with other non-current assets on the consolidated balance sheets.

The Company evaluates the recoverability of capitalized software development costs on a product-by-product basis. Capitalized costs for those products that are cancelled are expensed in the period of cancellation. In addition, a charge to cost of revenue is recorded when management's forecast for a particular game indicates that unamortized capitalized costs exceed the net realizable value of that asset.

Management judgments and estimates are used in the assessment of when technological feasibility is established, as well as in the ongoing assessment of the recoverability of capitalized costs. Different estimates or assumptions could result in different reported amounts of capitalized product development costs, research and development expense, or cost of revenues. If a revised game sales forecast is less than management's current game sales forecast, or if actual game usage is less than management's forecast, the Company could record charges to write-down software development costs previously capitalized.

Research and development expenses

Research and development expenses consist primarily of payroll, depreciation expense, other overhead expenses and the cost of equipment purchased for research and development purpose.

In February 2005, the Company entered into a worldwide publishing rights contract for the online PC game APB with Real Time Worlds Ltd., ("RTW") a company based in Scotland. In June 2005, the Company entered into a worldwide publishing rights contract for the console version (XBox 360) of the online game APB. In addition, in January 2006, the Company entered into a worldwide publishing rights contract for the online PC game T-project with Red5 Studios, Inc. ("Red5"), a company based in United States of America. These contracts are for five years after the games are commercialized, and the Company has agreed to pay royalties for the exclusive world-wide distribution rights to the games. According to the contracts, RTW and Red5 are to develop the game and transfer the worldwide

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publishing rights to the Company in exchange for cash payments in advance of commercialization to be made in quarterly installments and future royalty payments. If a marketable game is developed, the Company will pay RTW and Red5 royalties based on certain percentage of revenues generated from the games.

The payments made in advance of commercialization by the Company will be used to offset against the future royalty payments. For the years ended December 31, 2007 and 2008, the Company paid ₩13,894 million and ₩9,166 million, respectively, in accordance with the terms of the contract. These payments were made prior to the establishment of technological and commercial feasibility, represent the development costs of the aforementioned games, and the recoverability of those costs were contingent upon successful development and commercialization of the games, and upon generating sufficient revenues from the games after commercialization. These payments were expensed and recorded as a research and development expense in the consolidated statements of operations for the years ended December 31, 2007 and 2008.

In April 2008, the Company entered into a termination agreement with RTW to terminate the aforementioned worldwide publishing rights contracts for the online PC game and the console version (XBox 360) of the online game APB. According to this agreement, the Company shall have no rights or licenses with respect to the game APB and the Company shall be compensated with payment in cash on \$10.4 million before December 31, 2008 and 15% of cash receipt following commercial release of the game APB for the first three years from commercial launch.

In June and July 2008, according to this agreement the Company was compensated with payment in cash on \$2.9 million and \$0.5 million, respectively. These amounts were recorded as an offset to research and development expense in the consolidated statement of operations. In addition, the Company recorded the remaining amount owed to the Company under the agreement of \$7.0 million as other receivables at December 31, 2008. This amount was recorded as an offset of research and development expense in the consolidated statement of operations. This receipt was collected on January 5, 2009. The Company did not record any royalty income related to the 15% of the revenue following commercial release as no such sales occurred as of December 31, 2008 and 2009.

In May 2009, the Company entered into an amendment of contract with Red5 to amend the aforementioned worldwide publishing rights contract for the online PC game T-project. According to this contract, Red 5 will have rights to publish the Game in the United States and Europe and pay 15% of the revenue for 3 years and thereafter 10% of the revenue for 2 years to the Company. The Company will have publishing rights in all of the countries throughout the world other than those in the United States or Europe, paying 50% of revenue for 5 years to Red 5. The Company is not required to make any additional development payment to Red 5.

Research and development costs regarding the development and maintenance of existing revenue generating games, included in the cost of revenues for the years ended December 31, 2007, 2008 and 2009 amounted to ₩7,369 million, ₩7,397 million and ₩7,740 million, respectively.

Research and development costs regarding the research and development activities for the new games that have not reached technological nor commercial feasibility, included in the operating expenses for

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the years ended December 31, 2007, 2008 and 2009 amounted to ₩23,164 million, ₩1,816 million and ₩2,227 million, respectively.

Advertising

The Company expenses advertising costs as incurred. Advertising expense was approximately ₩2,271 million, ₩3,824 million and ₩735 million for the years ended December 31, 2007, 2008 and 2009, respectively.

The Company enters into marketing arrangements with independent distribution agents to distribute its MU and SUN online game product to internet cafes in Korea. Under the terms of these agreements, the Company remits monthly cash payments to the agents based upon cash collections for the previous month. These agreements are typically 12 months in duration. The Company accounts for the revenue from sales through its distribution agents at the gross sales price and records a marketing expense, or sales commission, representing 20% for 2007, 2008 and 2009 of the gross selling price in accordance with the terms of the distribution agreement.

The Company expenses advertising costs for participating in trade shows during the period in which the show occurs. Expenses for advertising in online forums and industry publications are expensed in the period when the advertising is displayed. There were no significant advertising costs associated with online promotions, website or magazine advertising, or alliances with internet service providers.

Accrued severance benefits

Employees and directors with one year or more of service are entitled to receive a lump-sum payment upon termination of their employment with the Company based on the length of service and rate of pay at the time of termination. The annual severance benefit expense charged to operations is calculated based upon the net change in the accrued severance benefit payable at the balance sheet date.

Lease Transactions

The Company accounts for lease transactions as either operating leases or capital leases, depending on the terms of the underlying lease agreement. Equipments acquired under capital lease agreements, are recorded at cost as property and equipment, and depreciated using the straight-line method over their estimated useful lives. In addition, the aggregate lease payments are recorded as obligations under capital leases, net of the portion interest which is recognized over the lease period using the effective interest rate method.

Vehicles, housing and office space rented acquired under operating lease agreements are not included in property and equipment. The related lease rentals are charged to expense when incurred.

Foreign currency translation

The Company, including all of its subsidiaries, uses their local currencies as their functional currencies. The financial statements of the subsidiaries are translated into the Korean Won in accordance with ASC 830, *Foreign Currency Matters* (formerly referenced as the FASB's SFAS No.52, *Foreign Currency Translation*). All the assets and liabilities are translated to the Korean Won at the end-of-period exchange rates. Capital accounts are determined to be of a permanent nature and are translated using historical exchange rates. Revenues and expenses are translated using average exchange rates.

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Foreign currency translation adjustments arising from differences in exchange rates from period to period are included in the foreign currency translation adjustment account in accumulated comprehensive income (loss) of equity.

Foreign currency transactions

Gains and losses resulting from foreign exchanges transactions are included in foreign currency gains (losses) in other income (loss) in the accompanying consolidated statement of operations.

Fair values of financial instruments

The Company's carrying amounts of cash, cash equivalents, short-term financial instruments, receivables, accounts payable and accrued liabilities approximate fair value because of the short maturity of these instruments.

Stock-based compensation

The Company accounts for stock-based compensation under ASC 718, *Compensation-Stock Compensation* (formerly referenced as the FASB's SFAS No. 123(R), *Share-based payment*).

The Company uses a Black-Scholes model to determine the fair value of equity-based awards at the date of grant. Compensation cost for stock option grants are measured at the grant date based on the fair value of the award and recognized over the service period, which is usually the vesting period. As stock-based compensation expense recognized in the consolidated statement of operations for the years ended December 31, 2007, 2008 and 2009 are based on awards ultimately expected to vest, it has been reduced for estimated forfeitures. The Company estimates forfeitures at the time of grant and revised, if necessary, in subsequent periods if actual forfeitures differ from those estimates.

Income taxes

The Company accounts for income taxes under the provisions of ASC 740, *Income Taxes* (formerly referenced as the FASB's SFAS No. 109, *Accounting for Income Taxes*). Under ASC 740, income taxes are accounted for under the asset and liability method. Deferred taxes are determined based upon differences between the financial reporting and tax bases of assets and liabilities at currently enacted statutory tax rates for the years in which the differences are expected to reverse. A valuation allowance is provided on deferred tax assets to the extent that it is more likely than not that such deferred tax assets will not be realized. The total income tax provision includes current tax expenses under applicable tax regulations and the change in the balance of deferred tax assets and liabilities.

On January 1, 2007, the Company adopted the provisions of ASC 740, *Income Taxes* (formerly referenced as FASB Interpretation ("FIN") 48, *Accounting for Income Tax Uncertainties*), which prescribes a recognition threshold and measurement attribute for tax positions taken or expected to be taken in a tax return. This interpretation also provides guidance on de-recognition, classification, interest and penalties, accounting in interim periods, disclosure and transition. The evaluation of a tax position in accordance with this interpretation is a two-step process. In the first step, recognition, the Company determines whether it is more-likely-than-not that a tax position will be sustained upon examination, including resolution of any related appeals or litigation processes, based on the technical merits of the position. The second step addresses measurement of a tax position that meets the more-likely-than-not criteria.

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The tax position is measured at the largest amount of benefit that has a cumulative likelihood of greater than 50 percent of being realized upon ultimate settlement. Differences between tax positions taken in a tax return and amounts recognized in the financial statements will generally result in (a) an increase in a liability for income taxes payable or a reduction of an income tax refund receivable, (b) a reduction in a deferred tax asset or an increase in a deferred tax liability or (c) both (a) and (b). Tax positions that previously failed to meet the more-likely-than-not recognition threshold should be recognized in the first subsequent financial reporting period in which that threshold is met. Previously recognized tax positions that no longer meet the more-likely-than-not recognition threshold should be de-recognized in the first subsequent financial reporting period in which that threshold is no longer met. Use of a valuation allowance as described in ASC 740 is not an appropriate substitute for the de-recognition of a tax position. The requirement to assess the need for a valuation allowance for deferred tax assets based on sufficiency of future taxable income is unchanged by this interpretation.

Earnings per share

Basic earnings per share is computed by dividing net income available to common stockholders by the weighted average number of common shares outstanding for all periods. Diluted earnings per share is computed by dividing net income by the weighted average number of common shares outstanding, increased by common stock equivalents. Common stock equivalents are calculated using the treasury stock method and represent incremental shares issuable upon exercise of the Company's outstanding stock options. However, potential common shares are not included in the denominator of the diluted earnings per share calculation when inclusion of such shares would be anti-dilutive, such as in a period in which a net loss is recorded.

Recent accounting pronouncements

In January 2010, the FASB issued Accounting Standards Update 2010-06 (ASU 2010-06), which amends the disclosure requirements of ASC 820, "Fair Value Measurements and Disclosures," ("ASC 820") as of January 1, 2010. ASU 2010-06 requires new disclosures for any transfers of fair value into and out of Level 1 and 2 fair value measurements and separate presentation of purchases, sales, issuances and settlements within the reconciliation of Level 3 unobservable inputs. The Company previously adopted ASC 820 on January 1, 2008 and January 1, 2009 for financial assets and liabilities and for nonfinancial assets and liabilities, respectively. ASU 2010-06 is effective for annual and interim periods beginning after December 15, 2009, except for the Level 3 reconciliation which is effective for annual and interim periods beginning after December 15, 2010. The adoption of ASU 2010-06 as of January 1, 2010 did not have a material effect on the Company's financial condition or results of operations. The Company does not expect the adoption of ASU 2010-06 in relation to the Level 3 reconciliation to have a material impact on the Company's financial condition or results of operations.

In September 2009, the EITF reached final consensus under ASU No. 2009-13 on the issue related to revenue arrangements with multiple deliverables. This issue addresses how to determine whether an arrangement involving multiple deliverables contains more than one unit of accounting and how arrangement consideration should be measured and allocated to the separate units of accounting. This issue is effective for the Company's revenue arrangements entered into or materially modified on or after January 1, 2011. The Company will evaluate the impact of this issue on the Company's financial

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statements when reviewing its new or materially modified revenue arrangements with multiple deliverables when it becomes applicable.

In June 2009, the FASB issued a statement which improves financial reporting by enterprises involved with variable interest entities. This statement requires companies to perform an analysis to determine whether the company's variable interest or interests give it a controlling financial interest in a variable interest entity. This statement will be effective as of the beginning of the annual reporting period that begins after November 15, 2009. The Company will evaluate the impact of this statement on the Company's financial statements when it becomes applicable.

In June 2009, the FASB issued a statement which improves the relevance, representational faithfulness, and comparability of the information that a reporting entity provides in its financial statements about a transfer of financial assets as well as the effects of a transfer on its financial position, financial performance, and cash flows and a transferor's continuing involvement, if any, in transferred financial assets. The statement requires that a transferor recognize and initially measure at fair value all assets obtained (including a transferor's beneficial interest) and liabilities incurred as a result of a transfer of financial assets accounted for as a sale. The statement will be effective as of the beginning of annual reporting period that begins after November 15, 2009. The Company believes the adoption of this pronouncement will not have a material impact on the Company's financial statements as the Company does not currently transfer its financial assets.

3. Convenience Translation into United States Dollar Amounts

The Company reports its consolidated financial statements in the Korean Won. The United States dollar ("US dollar") amounts disclosed in the accompanying consolidated financial statements are presented solely for the convenience of the reader, and have been converted at the rate of 1,163.65 Korean Won to one US dollar, which is the noon buying rate of the US Federal Reserve Bank of New York in effect on December 31, 2009. Such translations should not be construed as representations that the Korean Won amounts represent, have been, or could be, converted into, US dollars at that or any other rate. The US dollar amounts are unaudited and are not presented in accordance with generally accepted accounting principles either in Korea or the United States of America.

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4. Available-for-sale securities

The cost, gross unrealized gains and fair value of available-for-sale securities as of December 31, 2008 and 2009 are as follows:

(In millions of Korean Won)

| | <u>Cost or carrying value</u> | <u>Gross unrealized gains</u> | <u>Gross unrealized losses</u> | <u>Fair value</u> |
|--|---------------------------------------|---------------------------------------|--|-------------------|
| As of December 31, 2008 | | | | |
| Current portion of available-for-sale: | | | | |
| Beneficiary certificates | ₩ 3,995 | ₩ 35 | ₩ 386 | ₩ 3,644 |
| Beneficiary certificates (accounted for at fair value under ASC 825) | 1,476 | - | 671 | 805 |
| Equity securities | 667 | - | - | 667 |
| | <u>6,138</u> | <u>35</u> | <u>1,057</u> | <u>5,116</u> |
| Non-current portion of available-for-sale: | | | | |
| Equity securities | 167 | 1,542 | - | 1,709 |
| | <u>₩ 6,305</u> | <u>₩ 1,577</u> | <u>₩ 1,057</u> | <u>₩ 6,825</u> |
| As of December 31, 2009 | | | | |
| Current portion of available-for-sale: | | | | |
| Beneficiary certificates | ₩ 3,977 | ₩ 92 | ₩ - | ₩ 4,069 |
| Beneficiary certificates (accounted for at fair value under ASC 825) | 2,480 | 115 | 27 | 2,568 |
| Equity securities | 138 | 625 | - | 763 |
| | <u>6,595</u> | <u>832</u> | <u>27</u> | <u>7,400</u> |
| Non-current portion of available-for-sale: | | | | |
| Equity securities | 184 | - | - | 184 |
| | <u>₩ 6,779</u> | <u>₩ 832</u> | <u>₩ 27</u> | <u>₩ 7,584</u> |

The current investment in equity securities are comprised of 822 shares of GameOn Co., Ltd. The Company owns 1.00% and 0.83% of shares of GameOn Co., Ltd. as of December 31, 2008 and 2009, respectively. The non-current investment in equity securities are comprised of 230,000 shares of NeoWave Inc. The Company owns 5.94% and 1.44% of shares of NeoWave Inc. as of December 31, 2008 and 2009, respectively.

The original cost of the investment in NeoWave Inc. securities was ₩4,550 million when the Company acquired the securities in February 2008. During 2008 and 2009, the Company concluded that the fair market value of NeoWave Inc. securities was significantly less than the original cost or the carrying value before valuation. In addition, the Company concluded that it was unlikely to recover the original cost or the carrying value before valuation of the NeoWave Inc. investment at any time in the foreseeable future. Accordingly, as of December 31, 2008 and 2009, the Company recorded an other-than-temporary loss on the investment in NeoWave Inc. securities of ₩3,883 million and ₩483

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million, which represents the difference between cost or carrying value before valuation and fair market value at December 31, 2008 and 2009, respectively.

The current investment in beneficiary certificates represents equity interests in a fund that is comprised of bonds, marketable equity securities and trust funds as of December 31, 2008 and 2009. The fair value of bonds is derived based on quoted prices in active markets, the fair value of marketable securities is derived based on quoted prices in active exchange markets and the fair value of trust funds is derived based on quoted prices in markets that are not active or other inputs that are observable. The Company has invested in multiple beneficiary certificates. Two and three of these beneficiary certificates contain embedded derivatives as of December 31, 2008 and 2009, respectively. The Company has determined that it is not practical to bifurcate the embedded derivatives and account for separately. Pursuant to ASC 825, the Company has elected the fair value option to account for these two and three securities as of December 31, 2008 and 2009, respectively. Accordingly, the entire change in estimated fair value of the two and three beneficiary certificates that contain embedded derivatives is included in other expense on the consolidated statement of operations for the years ended December 31, 2008 and 2009.

The Company classified the investment in equity securities and beneficiary certificates other than the investment of NeoWave Inc. as the current investment as those securities are intended for use in current operations and the Company has the ability to liquidate such securities within one year of the balance sheet date.

The ₩763 million of equity securities of GameOn Co., Ltd classified under short-term available-for-sale securities at December 31, 2009 had been classified as long-term available-for-sale securities in 2007 and 2008. However, as the Company sold securities of GameOn Co., Ltd in 2009 and the Company has the ability and intention to liquidate such securities within one year of the balance sheet date, the Company reclassified the those securities under a short-term available-for-sale.

The equity securities of NeoWave Inc. of ₩184 million had been classified as short-term available-for-sale securities at the time of acquisition. However, as the Company determined to hold the security until it recovers the original cost of NeoWave Inc. investment, which is unlikely to happen in the foreseeable future, it was reclassified to long-term available-for-sale securities during 2009.

Unrealized gains on the available-for-sale securities, net of tax, included in accumulated comprehensive income were ₩1,229 million and ₩544 million at December 31, 2008 and 2009, respectively. The deferred income tax liability amounts related to these unrealized gains were ₩348 million and ₩174 million at December 31, 2008 and 2009, respectively.

The Company sold securities of NeoWave Inc. and securities of GameOn Co., Ltd in 2008 and 2009, respectively, and sold out certain portions of beneficiary certificate in 2008 and 2009. Proceeds from the sales of available-for-sale securities were ₩17,651 million, ₩9,194 million and ₩6,467 million in 2007, 2008 and 2009, respectively. The gain on disposal of available-for-sale securities in 2007, 2008 and 2009 were ₩3,755 million, ₩35 million and ₩224 million, respectively, and loss on disposal of available-for-sale securities in 2008 and 2009 were ₩1 million and ₩12 million, respectively. These gains and losses were determined based on the average cost method.

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5. Allowance for Accounts Receivable

Changes in the allowance for accounts receivable for the years ended December 31, 2007, 2008 and 2009 are as follows:

(In millions of Korean Won)

| | <u>2007</u> | <u>2008</u> | <u>2009</u> |
|--------------------------------|----------------|--------------|--------------|
| Balance at beginning of year | ₩ 2,251 | ₩ 1,185 | ₩ 633 |
| Provision for allowances | - | - | 172 |
| Reversal of previous provision | (355) | (176) | - |
| Write-offs | (711) | (376) | (278) |
| Balance at end of year | <u>₩ 1,185</u> | <u>₩ 633</u> | <u>₩ 527</u> |

6. Property and equipment, net

Property and equipment as of December 31, 2008 and 2009 are as follows:

(In millions of Korean Won)

| | <u>2008</u> | <u>2009</u> |
|---|-----------------|-----------------|
| Land | ₩ 1,514 | ₩ 1,097 |
| Building | 3,363 | 2,234 |
| Computer and equipment | 16,564 | 15,907 |
| Furniture and fixtures | 3,185 | 1,684 |
| Vehicles | 103 | 66 |
| Software-externally purchased | <u>8,478</u> | <u>9,109</u> |
| | 33,207 | 30,097 |
| Less: accumulated depreciation and amortization | <u>(24,098)</u> | <u>(24,168)</u> |
| | <u>₩ 9,109</u> | <u>₩ 5,929</u> |

Depreciation and amortization expense for the years ended December 31, 2007, 2008 and 2009 were ₩4,670 million, ₩4,085 million and ₩2,849 million, respectively. The expected future amortization expense of externally purchased software for 2010, 2011, 2012, 2013 and 2014 are ₩552 million, ₩334 million, ₩268 million, ₩142 million and ₩29 million, respectively.

7. Impairment charges

During the year ended December 31, 2008, the Company recorded an impairment charge of ₩505 million for the leasehold improvements, equipment and certain other assets at its subsidiaries located in China and United States. The Company concluded that these assets were impaired as there had been no revenue activities at these subsidiaries. The Company concluded that there are no other alternative uses for these assets. No impairment charge was recorded for the years ended December 31, 2007 and 2009.

8. Derivatives

During 2008, the Company entered into a trading-purpose option contract related to the investment in NeoWave Inc. securities (see note 4). According to the terms of this contract, the put option allows the Company to sell NeoWave Inc. securities to counterparty at ₩20,000 per share for 180,000 shares, and the call option allows for the same counterparty to buy NeoWave Inc. securities from the Company at ₩21,000 per share for 180,000 shares. The estimated fair value of these derivatives related to this contract is as follows:

(In millions of Korean Won)

| | <u>Fair value</u> <u>2008</u> | <u>Fair value</u> <u>2009</u> |
|-------------|----------------------------------|----------------------------------|
| Put-option | ₩ 145 | ₩ 39 |
| Call-option | - | - |

Total ₩ 145 ₩ 39

These amounts are included within other current assets in the accompanying consolidated balance sheets.

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9. Fair value of financial instruments

The Company adopted ASC 820, *Fair Value Measurements and Disclosures* (formerly referenced as the FASB's SFAS No. 157 *Fair Value Measurements*) effective January 1, 2008, for all financial assets and liabilities as required. The adoption of ASC 820 was not material to the Company's financial position or results of operations.

As discussed in Note 2, the Company adopted ASC 825, which permits entities to choose to measure financial instruments and certain other items at fair value and consequently report unrealized gains and losses on these items in earnings. ASC 825 was effective for the Company's fiscal year beginning January 1, 2008. The Company has elected the fair value option to measure one of its investments in available-for-sale securities.

The estimated fair value of financial assets is determined by the Company, using available market information and valuation methodologies considered to be appropriate. However, considerable judgment is required in interpreting market data to develop the estimates of fair value.

The following methods and assumptions were used to estimate the fair value of each class of significant financial assets and financial liabilities:

(i) Cash and cash equivalents, short-term financial instruments, accounts receivable and accounts payable

The carrying amount approximates fair value because of the short maturities of these balances.

(ii) Available-for-sale securities

The fair value of market traded investments such as listed company's stocks, public bonds and other marketable securities are based on quoted market prices for those investments.

(iii) Available-for-sale securities with an embedded derivative feature

The investment in beneficiary certificates represents equity interests in a fund that is comprised of bonds and trust funds as of December 31, 2009. The fair value of bonds is derived based on quoted prices in active markets, and the fair value of trust funds is derived based on quoted prices in markets that are not active or other inputs that are observable. The trust fund portion of this investment contains an embedded derivative. The Company has determined that it is not practical to bifurcate the embedded derivative and account for separately. Pursuant to ASC 825, the Company has elected the fair value option to account for this investment. Accordingly, the entire change in estimated fair value in the beneficiary certificates is included in the consolidated statement of operations.

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(iv) Derivatives

The fair value of derivatives is estimated based on pricing models using current market rates, records and other inputs that are observable.

The Company's financial assets and liabilities are valued utilizing the market approach to measure fair value. The market approach uses prices and other relevant information generated by market transactions involving identical or comparable assets or liabilities. The standard describes a fair value hierarchy based on three levels of inputs that may be used to measure fair value which are the following:

- Level 1— Quoted prices in active exchange markets involving identical assets or liabilities.
- Level 2— Inputs other than Level 1 that are observable, either directly or indirectly, such as quoted prices for similar assets or liabilities; quoted prices in markets that are not active; or other inputs that are observable or can be corroborated by observable market data for substantially the full term of the assets or liabilities.
- Level 3— Unobservable inputs for the asset or liability, either directly or indirectly, and management assessments and inputs using a binomial lattice model as the valuation technique.

The following table summarizes the Company's financial assets and liabilities measured at fair value on a recurring basis in accordance with ASC 820 and ASC 825 as of December 31, 2008 and 2009, respectively:

(In millions of Korean Won)

| As of December 31, 2008, | Level 1 | Level 2 | Level 3 | Total |
|--|----------------|----------------|------------|----------------|
| Current portion of available-for-sale | | | | |
| Beneficiary certificates | ₩ - | ₩ 3,644 | ₩ - | ₩ 3,644 |
| Beneficiary certificates (accounted for at fair value under ASC 825) | - | 805 | - | 805 |
| Equity securities - manufacturing industry | 667 | - | - | 667 |
| Non-current portion of available-for-sale | | | | |
| Equity securities - online game industry | 1,709 | - | - | 1,709 |
| Derivatives - put option | - | 145 | - | 145 |
| Total | <u>₩ 2,376</u> | <u>₩ 4,594</u> | <u>₩ -</u> | <u>₩ 6,970</u> |
| As of December 31, 2009, | Level 1 | Level 2 | Level 3 | Total |
| Current portion of available-for-sale | | | | |
| Beneficiary certificates | ₩ - | ₩ 4,069 | ₩ - | ₩ 4,069 |
| Beneficiary certificates (accounted for at fair value under ASC 825) | - | 2,568 | - | 2,568 |
| Equity securities - online game industry | 763 | - | - | 763 |
| Non-current portion of available-for-sale | | | | |
| Equity securities - manufacturing industry | 184 | - | - | 184 |
| Derivatives - put option | - | 39 | - | 39 |
| Total | <u>₩ 947</u> | <u>₩ 6,676</u> | <u>₩ -</u> | <u>₩ 7,623</u> |

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10. Accrued severance benefits

Accrued severance benefits as of December 31, 2008 and 2009 are as follows:

(In millions of Korean Won)

| | <u>2008</u> | <u>2009</u> |
|-----------------------------------|----------------|----------------|
| Balance at beginning of year | ₩ 4,458 | ₩ 3,012 |
| Provisions for severance benefits | 1,666 | 920 |
| Severance payments | (3,112) | (932) |
| Transfer-in from related party | - | 46 |
| Balance at end of year | <u>₩ 3,012</u> | <u>₩ 3,046</u> |

It is estimated that no health and welfare benefits will be paid over the next ten years upon employees normal retirement ages.

11. Commitments and contingencies

The Company rents vehicles, housing and office space under operating leases, which expire at various dates through 2012.

Future minimum lease payments for all operating leases at December 31, 2009, are as follows:

(In millions of Korean Won)

| | |
|------|----------------|
| 2010 | ₩ 1,679 |
| 2011 | 1,484 |
| 2012 | 503 |
| | <u>₩ 3,666</u> |

Rent expense incurred was approximately ₩1,502 million, ₩1,768 million and ₩1,470 million for the years ended December 31, 2007, 2008 and 2009, respectively.

During 2007, the Company entered into capital lease agreements related to equipment. The assets and liabilities under the capital leases were ₩171 million at the inception of the leases which represented the present value of the minimum lease payments over the lease term. The Company's depreciation expense, with respect to the above lease agreements, was ₩47 million and ₩22 million for the years ended December 31, 2008 and 2009, respectively.

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Future minimum lease payments under capital lease agreements as of December 31, 2009 are as follows:

| <i>(In millions of Korean won)</i> | <u>Minimum lease payments</u> | <u>Interest</u> | <u>Lease liabilities (Present value)</u> |
|------------------------------------|-----------------------------------|-----------------|--|
| Within one year | ₩ 22 | ₩ - | ₩ 22 |

The Company entered into a stand-by Letter of credit agreement with a financial institution, which is effective until December 18, 2010. The financial institution provided a guarantee on borrowings by the Company's Taiwan subsidiary of up to \$650 thousand. There are no amounts outstanding under the letter of credit agreement as of December 31, 2009.

As of December 31, 2007, the Company was a defendant in two lawsuits claiming damages for breach of contract as a result of two contracts in which the Company had been a party. On May 7, 2009, the court returned a verdict against the plaintiffs. The aggregated claims amount to approximately ₩150 million and the Company expects the plaintiffs to appeal the cases to the higher court. Although there can be no assurance as to the outcome, the Company's management does not expect that the outcome in the above legal proceedings and claims, individually or collectively, will have a material adverse effect on the Company's financial condition, results of operations or cash flows.

12. Stockholders' equity

As of December 31, 2009, the Company is authorized to issue 40,000,000 shares, par value ₩500 per share, in registered form, which consists of common shares, non-voting preferred shares and common shares convertible into non-voting preferred shares. The Common shares are convertible at a rate of common share for preferred share. Under the articles of incorporation, holders of non-voting preferred shares are entitled to dividends of 3% or more of the par value, the actual dividend rate to be determined by the Company's board of directors at the time of issuance. In addition, the Company is authorized to issue the non-voting preferred shares up to 50% of the issued common shares and to issue convertible shares up to 50% of the issued common shares, less issued preferred shares.

All of the outstanding shares are fully paid and are in registered form. No non-voting preferred shares or convertible common shares were issued or outstanding as of December 31, 2009.

On February 2, 2006, September 4, 2006 and September 21, 2007, the Company issued 1,000 common shares, 1,000 common shares and 2,000 common shares at ₩1,394 per share to the Company's employees who exercised stock options which were granted on July 10, 2002.

Dividends

Dividends are generally proposed based on each year's earnings and are declared, recorded and paid in the subsequent year. In 2007, 2008 and 2009, the Company did not declared dividends.

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Accumulated deficit

Accumulated deficit consists of the following as of December 31, 2008 and 2009:

| <i>(In millions of Korean Won)</i> | <u>2008</u> | <u>2009</u> |
|---|-------------------|-------------------|
| Appropriated retained earnings | | |
| Legal reserve | ₩ 322 | ₩ 322 |
| Reserve for business rationalization | 118 | 118 |
| Reserve for small and medium size enterprise investment | 443 | 443 |
| Accumulated deficit before disposition | <u>(42,511)</u> | <u>(39,202)</u> |
| | <u>₩ (41,628)</u> | <u>₩ (38,319)</u> |

The Commercial Code of the Republic of Korea requires the Company to appropriate a portion of retained earnings as a legal reserve in an amount equal to a minimum of ten percent of its cash dividends until such reserve equals 50% of its capital stock. The reserve is not available for dividends, but may be transferred into capital stock through an appropriate resolution by the Company's Board of Directors or used to reduce accumulated deficit, if any, through an appropriate resolution by the Company's stockholders. Pursuant to the Special Tax Treatment Control Law of Korea, the Company was required to appropriate, as a reserve for business rationalization, amounts equal to the tax reductions arising from tax exemptions and tax credits. This reserve was not available for payment of cash dividends, but may be transferred into capital stock through an appropriate resolution by the Company's board of directors or used to reduce accumulated deficit, if any, through an appropriate resolution by the Company's stockholders. Effective for fiscal years beginning January 1, 2002, the Special Tax Treatment Control Law of Korea was amended and, subject to an appropriate resolution by the Company's stockholders, this reserve became available for payment of cash dividends.

Pursuant to the Korean tax laws, when determining taxable income, small and medium sized companies, such as the Company, are eligible to claim a tax deduction for the amounts of retained earnings appropriated to reserves. These amounts are not available for dividends until they are used for the specified purposes or reversed.

13. Treasury stock

During 2005, the Company established a treasury stock fund of ₩9,000 million according to the resolution of its board of directors on April 14, 2005. During 2009, the Company renewed the contract amounts of this fund up to ₩6,319 million. The Company acquired 755,616 shares at an aggregate cost of ₩9,443 million and 635,741 shares at an aggregate cost of ₩6,617 million during 2007 and 2008, respectively, on the open market or through the trust funds. The Company disposed of 1,033,654 shares of treasury stock at an aggregate proceeds of ₩14,166 million during 2007, resulting in decrease in additional paid-in capital amounting to ₩2,725 million. There was no disposal of treasury stock during 2009.

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14. Stock purchase option plan

On July 10, 2002, the Company's shareholders approved the stock purchase option plan (the "Plan"). The Plan provides for the grant of incentive stock options to employees and directors. Additionally, the total number of options may not exceed 15% of the total number of the Company's issued shares. On July 10, 2002, January 20, 2005, April 14, 2005, April 12, 2006, July 18, 2007, October 12, 2007, February 12, 2009, March 27, 2009 and May 14, 2009 the Company granted certain employees options to purchase 14,000 shares of the Company's common stock at an exercise price of ₩1,394 per share, 118,800 shares at an exercise price of ₩24,100, 24,500 shares at an exercise price of ₩24,100, 41,000 shares at an exercise price of ₩24,100, 114,000 shares at an exercise price of ₩16,000, 77,000 shares at an exercise price of ₩14,000, 131,400 shares at an exercise price of ₩6,800, 213,000 shares at an exercise price of ₩8,300 and 12,000 shares at an exercise price of ₩13,600, respectively. During 2005, 2006, 2007 and 2009, options were granted with exercise prices of not less than the fair market value of the common shares on the grant date.

The fair value of the options at the date of the grant is estimated using the Black-Sholes option pricing model. In accordance with the Plan, options are vested at the conclusion of three years (two years for options granted in 2006, 2007 and 2009) of continued employment. Upon vesting, options are exercisable between three to six years (two to four years for options granted in 2006, 2007 and 2009) from the grant date.

The following table summarizes the stock options activity under the Plan:

| | Weighted- Average Number of Stock Options | Weighted Average Exercise Price Per Share | Weighted Average Fair Value of Shares Granted |
|---|--|--|--|
| <i>(in Korean Won, except number of stock options data)</i> | | | |
| Stock options outstanding as of December 31, 2007 | 256,800 | ₩ 17,760 | ₩ 6,749 |
| Options granted | - | - | - |
| Options exercised | - | - | - |
| Options canceled/forfeited | (24,000) | 16,338 | 6,927 |
| Stock options outstanding as of December 31, 2008 | 232,800 | ₩ 17,906 | ₩ 6,731 |
| Options granted | 356,400 | 7,925 | 3,907 |
| Options exercised | - | - | - |
| Options canceled/forfeited | (73,400) | 17,684 | 7,268 |
| Stock options outstanding as of December 31, 2009 | <u>515,800</u> | <u>₩ 11,041</u> | <u>₩ 4,703</u> |

As of December 31, 2009, the weighted-average remaining contractual life of outstanding options was 2.41 years.

The entire award vests at the end of three years (two years for options granted in 2006, 2007 and 2009) from the grant date. Generally, options granted in 2005 become exercisable in periodic installments,

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with 50% of options exercisable for one year from the third anniversary of the grant date and the rest 50% of options for one year from the fourth anniversary of the grant date. Of the options granted in 2005, 31,900 options are fully exercisable by April 13, 2010. Options granted in 2006 and 2007 become exercisable in periodic installments, with 50% of options exercisable for one year from the second anniversary of the grant date and the rest 50% of options for one year from the third anniversary of the grant date. Of the options granted in 2006 and 2007, 41,500 options are exercisable by July 17, 2010. In addition, options granted in 2009 become exercisable for two years from second anniversary of the grant date.

The total compensation expenses relating to the remaining stock options of ₩2,039 million are recognized over the remaining vesting period on a straight line basis. For the years ended December 31, 2007, 2008 and 2009, the Company recognized a compensation expense of ₩163 million, ₩307 million and ₩774 million, respectively, for the shares granted. There were 65,900 exercisable options at December 31, 2009.

The fair value for each option was estimated at the grant date, using a Black-Scholes option pricing model, with the following assumptions:

| | <u>2006</u> | <u>2007</u> | <u>2009</u> |
|---------------------------------------|-------------|-------------|-------------|
| Expected dividend yield | 0% | 0% | 0% |
| Risk-free interest rate | 4.85% | 5.43% | 3.19% |
| Expected volatility | 55.56% | 56.21% | 74.94% |
| Expected life (in years from vesting) | 2.5 years | 2.5 years | 2.0 years |
| Expected forfeitures | 41% | 42% | 34% |
| Fair value of stock | ₩ 24,700 | ₩ 14,868 | ₩ 8,712 |

Expected volatilities are based on historical volatility of the Company's stock.

There were no stock options granted in 2008.

15. Income taxes

Income tax expense consists of the following:

| <i>(In millions of Korean Won)</i> | <u>2007</u> | <u>2008</u> | <u>2009</u> |
|------------------------------------|----------------|--------------|----------------|
| Current | | | |
| Domestic | ₩ - | ₩ 63 | ₩ - |
| Foreign | 370 | 727 | 881 |
| | <u>370</u> | <u>790</u> | <u>881</u> |
| Deferred | | | |
| Domestic | 2,209 | 12 | 174 |
| Foreign | - | - | - |
| | <u>2,209</u> | <u>12</u> | <u>174</u> |
| Total income tax expense | <u>₩ 2,579</u> | <u>₩ 802</u> | <u>₩ 1,055</u> |

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The tax effects of temporary differences that give rise to significant portions of the deferred income tax assets and deferred income tax liabilities at December 31, 2008 and 2009 are as follows:

(In millions of Korean Won)

| | <u>2008</u> | <u>2009</u> |
|--|-----------------|-----------------|
| Current deferred income tax assets (liabilities) | | |
| Allowance for accounts receivable | ₩ 197 | ₩ 193 |
| Deferred income | 194 | 153 |
| Available-for-sale securities | 1,024 | (174) |
| Accrued expense | 693 | 959 |
| Unrealized foreign exchange gains | (943) | (341) |
| Income tax loss carryforward | 2,686 | 997 |
| Tax credit carryforward | - | 331 |
| Other | 23 | (111) |
| Total gross current deferred income tax assets | <u>3,874</u> | <u>2,007</u> |
| Less valuation allowance | <u>(3,874)</u> | <u>(2,007)</u> |
| Net current deferred income tax assets | <u>₩ -</u> | <u>₩ -</u> |
| Non-current deferred income tax assets (liabilities) | | |
| Deferred income | ₩ 137 | ₩ 186 |
| Available-for-sale securities | (339) | 961 |
| Accrued severance benefits | 497 | 579 |
| Property and equipment | 19 | 125 |
| Research and development costs | 8,997 | 8,925 |
| Income tax loss carryforward | 14,695 | 12,934 |
| Other | 563 | 131 |
| Total gross non-current deferred income tax assets | <u>24,569</u> | <u>23,841</u> |
| Less valuation allowance | <u>(24,569)</u> | <u>(23,841)</u> |
| Net non-current deferred income tax assets | <u>₩ -</u> | <u>₩ -</u> |

Deferred income tax assets are recognized only to the extent that realization of the related tax benefit is more likely than not. Realization of the future tax benefits related to the deferred tax assets is dependent on many factors, including the Company's ability to generate taxable income within the period during which the temporary differences reverse, the outlook for the Korean economic environment, and the overall future industry outlook. Management periodically considers these factors in reaching its conclusion.

As of December 31, 2008 and 2009, the Company recognized full valuation allowances for the net deferred tax assets as the management determined that it would not be able to realize these assets based on Webzen and its subsidiaries' historical and projected net and taxable income.

As of December 31, 2009, Webzen and its subsidiaries had available net operating loss carryforwards of ₩58,867 million to offset future taxable income which expire in varying amounts from 2010 to 2014, except ₩9,209 million from subsidiary in the United States which expire in from 2025 to 2029.

The tax effects of temporary differences which are directly related to shareholders' equity amounted to ₩12 million and ₩174 million as of December 31, 2008 and 2009, respectively.

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The statutory income tax rate applicable to the Company is 27.5% and 24.2% for the years ended December 31, 2008 and 2009, respectively. In accordance with the revised Corporate Income Tax Law, statutory tax rate applicable to the Company is 24.2% until 2011 and 22% thereafter.

A reconciliation of income tax expenses at the Korean statutory income tax rate to actual income tax expenses are as follows:

| <i>(In millions of Korean Won)</i> | <u>2007</u> | <u>2008</u> | <u>2009</u> |
|---|----------------|--------------|----------------|
| Income tax (benefit) at Korean statutory tax rate | ₩ (6,396) | ₩ (1,932) | ₩ 1,056 |
| Nondeductible items | (1,744) | 606 | 844 |
| Change in statutory tax rate | - | 1,284 | 840 |
| Change in valuation allowances | 10,223 | 51 | (2,595) |
| Foreign tax credit | 369 | 726 | 881 |
| Others | 127 | 67 | 29 |
| Total income tax expense | <u>₩ 2,579</u> | <u>₩ 802</u> | <u>₩ 1,055</u> |

The Company assessed uncertain tax positions and measured unrecognized tax benefits for open tax years in accordance with ASC 740, Income Taxes (formerly referenced as FIN 48, "Accounting for Income Tax Uncertainties."). The Company did not have any unrecognized tax benefits at December 31, 2007 and there has been no changes during the years ended December 31, 2008 and 2009.

The Company is subject to taxation in the Republic of Korea, its major tax jurisdiction. The Company's tax year for 2007, 2008 and 2009 is subject to examination by the tax authorities.

The Company has no ongoing tax examinations by tax authorities at this time.

16. Earnings (losses) per share

The components of basic and diluted earnings (losses) per share were as follows:

| | <u>2007</u> | <u>2008</u> | <u>2009</u> |
|---|-------------------|-------------------|-------------------|
| Net income (loss) available for common stockholders (A) | ₩ (25,594) | ₩ (7,675) | ₩ 3,309 |
| Weighted average outstanding shares of common stock (B) | 12,319,347 | 11,982,216 | 11,856,948 |
| Dilutive effect of stock options | - | - | 28,898 |
| Common stock and common stock equivalents (C) | <u>12,319,347</u> | <u>11,982,216</u> | <u>11,885,846</u> |
| Earnings (Losses) per share | | | |
| Basic (A/B) | <u>₩ (2,078)</u> | <u>₩ (641)</u> | <u>₩ 279</u> |
| Diluted (A/C) | <u>₩ (2,078)</u> | <u>₩ (641)</u> | <u>₩ 278</u> |

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The Company did not include stock options in computation of diluted earnings (losses) per share in 2007 and 2008, because stock options are antidilutive.

17. Related party transactions

As NHN Games became a related party by acquiring majority of shares of the Company's common stock in October 2008, NHN Corporation, the parent company of NHN Games, and its affiliates including NHN USA Inc, also became related parties of the Company.

During the years ended December 31, 2007, 2008 and 2009, there were related party transactions with the aforementioned and related parties as follows:

| | <u>2007</u> | <u>2008</u> | <u>2009</u> |
|----------------------------------|-----------------------------|-------------|-------------|
| | (In millions of Korean Won) | | |
| Sales to related parties | ₩ - | ₩ - | ₩ 916 |
| Purchases from related parties | - | - | 1,524 |
| Amounts due from related parties | - | - | 249 |
| Amounts due to related parties | - | 518 | 1,428 |

In May 2008, before NHN Games became the Company's related party, the Company entered into a three-year license agreement with NHN USA Inc., related party of NHN Games, for the distribution of Huxley in North America and Europe. For the year ended December 31, 2008, revenue and cost of revenue related to this agreement has not been incurred.

As of December 31, 2008 and 2009, the Company provided loans to employees for housing amounting to ₩1,083 million and ₩345 million and recorded these loans as other current assets and other non-current assets. Short-term financial instruments amounting to ₩346 million and ₩226 million are subject to withdrawal restrictions in relation to bank loans of employees as of December 31, 2008 and 2009, respectively.

18. Subsequent events

In April 2010, the Company entered into a service agreement with NHN Games under which NHN Games will be responsible for providing channel to users of "Huxley" after the commercial launch of the game.

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19. NASDAQ Delisting

On June 18, 2010, the Company notified the NASDAQ Stock Market (“NASDAQ”) of its intent to voluntarily delist its American Depository Shares (“ADSs”) from the NASDAQ Global Market and on June 28, 2010, the Company filed with the Securities and Exchange Commission (the “SEC”) and NASDAQ a Form 25 relating to the delisting of ADSs. The Company expects that trading in ADSs will be suspended by NASDAQ on July 8, 2010. The Board of Directors of the Company unanimously approved the voluntary delisting of ADSs on June 18, 2010. Following delisting from NASDAQ, it is anticipated that the ADSs will be quoted in the over-the-counter market on the “Pink Sheets,” a centralized electronic quotation service for over-the-counter securities. The Company expects its ADSs will continue to trade on the Pink Sheets, so long as market makers demonstrate an interest in trading in ADSs.

20. Business combination in 2010

On April 15, 2010, the Company entered into a Merger Agreement with NHN Games which is the largest shareholder of the Company, a developer of massively-multiplayer online games (“MMOGs”) and a subsidiary of NHN Corporation, an operator of Naver, an Internet search engine and an online game portal, based in Korea. This acquisition will enhance the Company’s game service portfolio, expand its publishing business and promote efficient development of online games by sharing R&D resources and integrating the operational networks of the parties to the merger. Pursuant to the Merger Agreement NHN Games will merge with and into the Company under Korean law, pursuant to which NHN Games will cease to exist and the Company will be the sole surviving entity (the “Merger”). All the assets and liabilities of NHN Games, along with its rights and obligations, will be assumed by the Company in accordance with applicable laws. At the shareholder meetings of the company and NHN Games, held on June 4, 2010, the shareholders of both companies approved the Merger. The acquisition date of this merger will be July 12, 2010. Upon the consummation of the merger, each share of NHN Games stock will be converted into 1.57262712 common shares of the Company pursuant to an exchange ratio determined by a formula prescribed under Korean securities law.

NHN Games is expected to be the accounting acquirer in this transaction as this transaction is considered a reverse acquisition. It is due to the fact the largest shareholders of NHN Games will manage the control over the Company after the Merger. The estimated purchase price for NHN Games is expected to be ₩223 billion based on the June 30, 2010 closing market value of the Company’s common shares. However, the fair value of the consideration paid will be determined at the date of closing of the acquisition. The estimated purchase price is comprised entirely of common shares of the Company. Transaction costs are not expected to be significant.

In fiscal 2010, the Company will adopt ASC 805, *Business Combinations* (formerly referred as FASB’s SFAS No. 141 (revised 2007), *Business Combinations*). Assets and liabilities of the accounting acquire will be recorded at fair value in accordance with ACS 805.

The determination of fair value will require the Company’s management to make significant estimates and assumptions, with respect to intangible assets acquired, support obligations assumed, and pre-

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acquisition contingencies. The assumptions and estimates used in determining the fair values of these items will be substantially similar upon the Company's adoption of ASC 805 (formerly FAS 141R) as they were under ASC 805 (formerly FAS 141).

21. Supplemental cash flow information and non-cash activities

(In millions of Korean Won)

| | <u>2007</u> | <u>2008</u> | <u>2009</u> |
|--|-------------|-------------|-------------|
| Supplemental cash flow information | | | |
| Cash paid during the year for income taxes | ₩ 398 | ₩ 540 | ₩ 897 |
| Interest paid | 35 | 76 | 8 |
| Supplemental non-cash activities | | | |
| Assets acquired under a capital lease | ₩ 171 | ₩ - | ₩ - |
| Reclassification of available-for-sale securities to long-term available-for-sale securities | - | - | 763 |
| Reclassification of long-term deferred revenue to deferred revenue | 281 | 1,113 | 878 |
| Reclassification of leasehold deposits to other accounts receivable | - | - | 10,344 |

[Table of Contents](#)**Item 19. Exhibits**

- 1.1 Articles of Incorporation Amended on June 04, 2010 (English translation)
- 2.1*** Form of Common Share Certificate (English translation)
- 2.2**** Form of ADR
- 2.3*** Form of Deposit Agreement among Webzen Inc., JPMorgan Chase Bank as depositary and holders of American Depositary Receipts (including form of American Depositary Receipt)
- 2.4† First Amendment to the Deposit Agreement among Webzen Inc., JPMorgan Chase Bank as depositary and holders of American Depositary Receipts dated as of February 3, 2004
- 2.5†† Second Amendment to the Deposit Agreement among Webzen Inc., JPMorgan Chase Bank as depositary and holders of American Depositary Receipts dated as of July 16, 2004
- 2.6††† Third Amendment to the Deposit Agreement among Webzen Inc., JPMorgan Chase Bank as depositary and holders of American Depositary Receipts dated as of December 9, 2008
- 4.1** Channeling Agreement dated March 1, 2009 between Webzen Inc. and NHN Co., Ltd.
- 4.2** Service Agreement dated April 2009 between Webzen Inc. and NHN Games Co., Ltd.
- 4.3** License and Distribution Agreement dated May 21, 2009 between Webzen Inc. and NHN USA Inc.
- 4.4** Business Agency Agreement dated June 8, 2009 between Webzen Inc. and NHN Games Co., Ltd.
- 4.5** License and Distribution Agreement dated May 19, 2008 between Webzen Inc. and NHN USA Inc.
- 4.6** Power of Attorney dated September 9, 2008 executed by Nam-Ju Kim
- 4.7** Power of Attorney dated September 9, 2008 executed by Ki-Yong Cho
- 4.8** Power of Attorney dated September 9, 2008 executed by Kil-Saup Song
- 4.9** Power of Attorney dated September 9, 2008 executed by Chang Keun Kim
- 4.10 Lease Contract dated December 18, 2009 between Webzen Inc. as tenant and CJ Internet Inc. as landlord (English translation)
- 4.11 Real Estate Sales Contract dated July 31, 2009 between Webzen Inc. as seller and KINX as Purchaser (English translation)
- 4.12 Joint Venture Agreement dated August 1, 2009 between Webzen Inc. and NHN Games Co., Ltd. (English translation)
- 4.13 Internet Game Distribution and Service Agreement dated December 1, 2009 between Webzen Taiwan Inc. as the licensee and NHN Games Corp. as the licensor.
- 4.14 Publishing Agreement dated February 12, 2010 between Webzen Inc. and NHN Games Co., Ltd. (English translation)
- 4.15 Channeling Agreement dated April 16, 2010 between Webzen Inc. and NHN Corporation (English translation)
- 6.1 Calculation of Basic and Diluted Earnings Per Common Share and ADS (see “Note 14 to the Consolidated Financial Statements” of this Form 20-F)
- 8.1* List of Subsidiaries

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|----------|--|
| 11.1†††† | Code of Ethics (English Translation) |
| 12.1 | Certifications of Chief Executive Officer required by Rule 13a-14(a) |
| 12.2 | Certifications of Chief Financial Officer required by Rule 13a-14(a) |
| 13.1 | Certifications of Chief Executive Officer and Chief Financial Officers required by Rule 13a-14(b) |
| 99.1 | Letter, dated as of June 30, 2010, from Samil PricewaterhouseCoopers to the Securities Exchange Commission |

* Incorporated by reference to the exhibits to the annual report on Form 20-F/A, filed on November 20, 2009.

** Incorporated by reference to the exhibits to the annual report on Form 20-F, filed on June 29, 2009.

*** Incorporated by reference to the exhibits to the registration statement on Form F-1 (File No. 333-110321).

**** Incorporated by reference to the exhibits to Form F-6, filed on June 20, 2005.

† Incorporated by reference to the exhibits to Form F-6, filed on February 3, 2004.

†† Incorporated by reference to the exhibits to Form F-6, filed on July 16, 2004.

††† Incorporated by reference to the exhibits to Form F-6, filed on December 9, 2008.

†††† Incorporated by reference to the exhibits to the annual report on Form 20-F, filed on June 25, 2004.

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Signatures

The registrant hereby certifies that it meets all of the requirements for filing on Form 20-F and that it has duly caused and authorized the undersigned to sign this annual report on its behalf.

WEBZEN INC.

By: /s/ Hwi Joon Shin
Name: Hwi Joon Shin
Title: Chief Financial Officer

Date: June 30, 2010
