TAKE TWO INTERACTIVE SOFTWARE INC
Form 10-Q
October 30, 2013

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UNITED STATES
SECURITIES AND EXCHANGE COMMISSION

WASHINGTON, D.C. 20549

FORM 10-Q

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

For the quarterly period ended September 30, 2013

OR

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

For the transition period from to .
Commission file number 001-34003

TAKE-TWO INTERACTIVE SOFTWARE, INC.

(Exact Name of Registrant as Specified in Its Charter)

Delaware	**51-0350842**
(State or Other Jurisdiction of Incorporation or Organization)	(I.R.S. Employer Identification No.)
622 Broadway	
New York, New York	**10012**
(Address of principal executive offices)	(Zip Code)

Registrant's Telephone Number, Including Area Code: **(646) 536-2842**

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

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

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

Large accelerated filer ý Accelerated filer o Smaller reporting company o

Non-accelerated filer o
(Do not check if a
smaller reporting company)

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

As of October 28, 2013, there were 97,101,554 shares of the Registrant's Common Stock outstanding.

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(All other items in this report are inapplicable)

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PART I. FINANCIAL INFORMATION

Item 1. Financial Statements

TAKE-TWO INTERACTIVE SOFTWARE, INC.

CONDENSED CONSOLIDATED BALANCE SHEETS

(in thousands, except per share amounts)

	September 30, 2013 (Unaudited)	March 31, 2013
ASSETS		
Current assets:		
Cash and cash equivalents	**$ 661,923**	$ 402,502
Accounts receivable, net of allowances of $78,081 and $64,081 at September 30, 2013 and March 31, 2013, respectively	**1,011,391**	189,596
Inventory	**84,033**	30,218
Software development costs and licenses	**119,534**	198,955
Deferred cost of goods sold	**302,253**	3,694
Prepaid expenses and other	**72,133**	41,187
Total current assets	**2,251,267**	866,152
Fixed assets, net	**34,271**	25,362
Software development costs and licenses, net of current portion	**113,505**	95,241
Goodwill	**228,006**	225,992
Other intangibles, net	**5,743**	8,827
Other assets	**68,522**	56,265
Total assets	**$ 2,701,314**	$ 1,277,839
LIABILITIES AND STOCKHOLDERS' EQUITY		
Current liabilities:		
Accounts payable	**$ 287,672**	$ 79,932
Accrued expenses and other current liabilities	**294,992**	228,916
Deferred revenue	**1,154,419**	26,919
Liabilities of discontinued operations	**1,123**	1,232
Total current liabilities	**1,738,206**	336,999
Long-term debt	**443,526**	335,202
Other long-term liabilities	**20,720**	17,087
Liabilities of discontinued operations, net of current portion		556
Total liabilities	**2,202,452**	689,844
Commitments and contingencies		
Stockholders' equity:		
Preferred stock, $.01 par value, 5,000 shares authorized		
	1,046	937

Common stock, $.01 par value, 200,000 shares authorized; 104,611 and 93,743 shares issued and outstanding at September 30, 2013 and March 31, 2013, respectively		
Additional paid-in capital	**922,058**	832,460
Accumulated deficit	**(426,864)**	(240,830)
Accumulated other comprehensive income (loss)	**2,622**	(4,572)
Total stockholders' equity	**498,862**	587,995
Total liabilities and stockholders' equity	**$ 2,701,314**	$ 1,277,839

See accompanying Notes.

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TAKE-TWO INTERACTIVE SOFTWARE, INC.

CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS (Unaudited)

(in thousands, except per share amounts)

	Three months ended September 30,		Six months ended September 30,	
	2013	**2012**	**2013**	**2012**
Net revenue	**$ 148,824**	$ 273,084	**$ 291,491**	$ 499,223
Cost of goods sold	**92,463**	158,487	**186,305**	345,218
Gross profit	**56,361**	114,597	**105,186**	154,005
Selling and marketing	**101,342**	65,851	**142,943**	144,858
General and administrative	**43,023**	30,809	**75,883**	74,011
Research and development	**26,520**	19,320	**47,391**	34,632
Depreciation and amortization	**3,367**	2,550	**6,424**	5,319
Total operating expenses	**174,252**	118,530	**272,641**	258,820
Loss from operations	**(117,891)**	(3,933)	**(167,455)**	(104,815)
Interest and other, net	**(10,747)**	(7,419)	**(20,069)**	(15,468)
Loss on extinguishment of debt	**(9,014)**		**(9,014)**	
Gain on convertible note hedge and warrants, net	**5,372**		**3,461**	
Loss from continuing operations before income taxes	**(132,280)**	(11,352)	**(193,077)**	(120,283)
(Benefit) provision for income taxes	**(8,185)**	1,085	**(7,098)**	2,926
Loss from continuing operations	**(124,095)**	(12,437)	**(185,979)**	(123,209)
Loss from discontinued operations, net of taxes	**(25)**	(54)	**(55)**	(120)
Net loss	**$ (124,120)**	$ (12,491)	**$ (186,034)**	$ (123,329)
Earnings (loss) per share:				
Continuing operations	**$ (1.40)**	$ (0.15)	**$ (2.12)**	$ (1.45)
Discontinued operations				
Basic earnings (loss) per share	**$ (1.40)**	$ (0.15)	**$ (2.12)**	$ (1.45)
Continuing operations	**$ (1.40)**	$ (0.15)	**$ (2.12)**	$ (1.45)
Discontinued operations				
Diluted earnings (loss) per share	**$ (1.40)**	$ (0.15)	**$ (2.12)**	$ (1.45)

See accompanying Notes.

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TAKE-TWO INTERACTIVE SOFTWARE, INC.

CONDENSED CONSOLIDATED STATEMENTS OF COMPREHENSIVE LOSS (Unaudited)

(in thousands)

	Three Months Ended September 30,		Six Months Ended September 30,	
	2013	**2012**	**2013**	**2012**
Net loss	**$ (124,120)**	$ (12,491)	**$ (186,034)**	$ (123,329)
Other comprehensive income:				
Foreign currency translation adjustment	**7,827**	11,654	**6,992**	318
Change in unrealized gains on cash flow hedges, net	**355**	272	**202**	169
Other comprehensive income	**8,182**	11,926	**7,194**	487
Comprehensive loss	**$ (115,938)**	$ (565)	**$ (178,840)**	$ (122,842)

See accompanying Notes.

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TAKE-TWO INTERACTIVE SOFTWARE, INC.

CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS (Unaudited)

(in thousands)

	Six Months Ended September 30,	
	2013	**2012**
Operating activities:		
Net loss	$ **(186,034)**	$ (123,329)
Adjustments to reconcile net loss to net cash provided by (used in) operating activities:		
Amortization and impairment of software development costs and licenses	**84,161**	142,286
Depreciation and amortization	**6,424**	5,319
Loss from discontinued operations	**55**	120
Amortization and impairment of intellectual property	**3,042**	4,944
Stock-based compensation	**21,266**	14,097
Deferred income taxes	**(6,105)**	(9)
Amortization of discount on Convertible Notes	**12,296**	9,199
Amortization of debt issuance costs	**1,070**	1,017
Loss on extinguishment of debt	**9,014**	
Gain on convertible note hedge and warrants, net	**(3,461)**	
Other, net	**1,165**	362
Changes in assets and liabilities, net of effect from purchases of businesses:		
Accounts receivable	**(821,795)**	(109,916)
Inventory	**(53,815)**	(38,091)
Software development costs and licenses	**(7,866)**	(111,317)
Prepaid expenses, other current and other non-current assets	**(35,835)**	8,236
Deferred revenue	**1,127,500**	24,420
Deferred cost of goods sold	**(298,559)**	(4,917)
Accounts payable, accrued expenses and other liabilities	**283,318**	96,075
Net cash used in discontinued operations	**(720)**	(814)
Net cash provided by (used in) operating activities	**135,121**	(82,318)
Investing activities:		
Purchase of fixed assets	**(15,452)**	(8,021)
Net cash used in investing activities	**(15,452)**	(8,021)
Financing activities:		
Proceeds from issuance of 1.00% Convertible Notes	**283,188**	
Payment for extinguishment of 4.375% Convertible Notes	**(165,999)**	
Proceeds from termination of convertible note hedge transactions	**84,429**	
Payment for termination of convertible note warrant transactions	**(55,651)**	
Payment of debt issuance costs for the issuance of 1.00% Convertible Notes	**(2,815)**	
Net cash provided by financing activities	**143,152**	
Effects of foreign currency exchange rates on cash and cash equivalents	**(3,400)**	(1,656)
Net increase (decrease) in cash and cash equivalents	**259,421**	(91,995)
Cash and cash equivalents, beginning of year	**402,502**	420,279

Cash and cash equivalents, end of period	**$ 661,923**	$ 328,284

See accompanying Notes.

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TAKE-TWO INTERACTIVE SOFTWARE, INC.

Notes to Unaudited Condensed Consolidated Financial Statements

(Dollars in thousands, except share and per share amounts)

1. BASIS OF PRESENTATION AND SIGNIFICANT ACCOUNTING POLICIES

Take-Two Interactive Software, Inc. (the "Company," "we," "us," or similar pronouns) was incorporated in the state of Delaware in 1993. We are a leading developer, publisher and marketer of interactive entertainment for consumers around the globe. The Company develops and publishes products through its two wholly-owned labels Rockstar Games and 2K. Our products are designed for console systems, handheld gaming systems and personal computers, including smart phones and tablets, and are delivered through physical retail, digital download, online platforms and cloud streaming services.

Basis of Presentation

The accompanying Unaudited Condensed Consolidated Financial Statements include the accounts of the Company and its wholly-owned subsidiaries and reflect all normal and recurring adjustments necessary for the fair presentation of our financial position, results of operations and cash flows. All material inter-company accounts and transactions have been eliminated in consolidation. The preparation of these Unaudited Condensed Consolidated Financial Statements in conformity with accounting principles generally accepted in the United States requires management to make estimates and assumptions that affect the amounts reported in these Unaudited Condensed Consolidated Financial Statements and accompanying notes. As permitted under U.S. generally accepted accounting principles, interim accounting for certain expenses, including income taxes, are based on full year assumptions when appropriate. Actual results could differ materially from those estimates.

Certain information and footnote disclosures normally included in financial statements prepared in accordance with U.S. generally accepted accounting principles have been omitted pursuant to the rules and regulations of the Securities and Exchange Commission ("SEC"), although we believe that the disclosures are adequate to make the information presented not misleading. These Unaudited Condensed Consolidated Financial Statements and accompanying notes should be read in conjunction with our annual consolidated financial statements and the notes thereto, included in our Annual Report on Form 10-K for the year ended March 31, 2013.

Certain reclassifications have been made to prior period amounts to conform to the current period presentation.

Discontinued Operations

In February 2010, we completed the sale to SYNNEX Corporation ("Synnex") of our Jack of All Games third party distribution business, which primarily distributed third party interactive entertainment software, hardware and accessories in North America. The financial information of our distribution business has been classified as discontinued operations in these Unaudited Condensed Consolidated Financial Statements for all of the periods presented. See Note 2 for additional information regarding discontinued operations. Unless otherwise noted, amounts and disclosures throughout the Notes to Unaudited Condensed Consolidated Financial Statements relate to the Company's continuing operations.

TAKE-TWO INTERACTIVE SOFTWARE, INC.

Notes to Unaudited Condensed Consolidated Financial Statements (Continued)

(Dollars in thousands, except share and per share amounts)

1. BASIS OF PRESENTATION AND SIGNIFICANT ACCOUNTING POLICIES (Continued)

Financial Instruments

The carrying amounts of our financial instruments, including cash and cash equivalents, accounts receivable, accounts payable and accrued liabilities, approximate fair value because of their short maturities. We consider all highly liquid instruments purchased with original maturities of three months or less to be cash equivalents. At September 30, 2013 and March 31, 2013 we had $26,387 and $7,489, respectively, of cash on deposit reported as a component of prepaid expenses and other in the accompanying Condensed Consolidated Balance Sheets because its use was restricted.

As of September 30, 2013, the estimated fair value of the Company's 1.75% Convertible Notes due 2016 and the Company's 1.00% Convertible Notes due 2018 was $298,475 and $318,579, respectively. See Note 8 for additional information regarding our Convertible Notes. The fair value was determined using observable market data for the Convertible Notes and its embedded option feature.

We transact business in various foreign currencies and have significant sales and purchase transactions denominated in foreign currencies, subjecting us to foreign currency exchange rate risk. From time to time, we use hedging programs in an effort to mitigate the effect of foreign currency exchange rate movements.

Cash Flow Hedging Activities

We use foreign currency forward contracts to mitigate foreign currency exchange rate risk associated with forecasted transactions involving non-functional currency denominated expenditures. These contracts, which are designated and qualify as cash flow hedges, are accounted for as derivatives whereby the fair value of the contracts is reported as either assets or liabilities on our Condensed Consolidated Balance Sheets. The effective portion of gains or losses resulting from changes in the fair value of these hedges is initially reported, net of tax, as a component of accumulated other comprehensive income (loss) in stockholders' equity. The gross amount of the effective portion of gains or losses resulting from changes in the fair value of these hedges is subsequently reclassified into cost of goods sold or research and development expenses, as appropriate, in the period when the forecasted transaction is recognized in our Condensed Consolidated Statements of Operations. In the event that the gains or losses in accumulated other comprehensive income (loss) are deemed to be ineffective, the ineffective portion of gains or losses resulting from changes in fair value, if any, is reclassified to interest and other, net, in our Condensed Consolidated Statements of Operations. In the event that the underlying forecasted transactions do not occur, or it becomes probable that they will not occur, within the defined hedge period, the gains or losses on the related cash flow hedges are reclassified from accumulated other comprehensive income (loss) to interest and other, net, in our Condensed Consolidated Statements of Operations. During the reporting periods presented, all forecasted transactions occurred, and therefore, there were no such gains or losses reclassified into interest and other, net. We do not enter into derivative financial contracts for speculative or trading purposes. At September 30, 2013 and March 31, 2013, we had $5,544 and $7,906, respectively, of forward contracts outstanding to buy foreign currencies in exchange for U.S. dollars all of which have maturities of less than one year. As of September 30, 2013 and March 31, 2013, the fair value of these outstanding forward contracts was immaterial and is included in prepaid expenses and other. The fair value of these outstanding forward contracts is estimated based on the prevailing exchange rates of the various hedged currencies as of the end of the period.

TAKE-TWO INTERACTIVE SOFTWARE, INC.

Notes to Unaudited Condensed Consolidated Financial Statements (Continued)

(Dollars in thousands, except share and per share amounts)

1. BASIS OF PRESENTATION AND SIGNIFICANT ACCOUNTING POLICIES (Continued)

Balance Sheet Hedging Activities

We use foreign currency forward contracts to mitigate foreign currency exchange rate risk associated with non-functional currency denominated cash balances and inter-company funding loans, non-functional currency denominated accounts receivable and non-functional currency denominated accounts payable. These transactions are not designated as hedging instruments and are accounted for as derivatives whereby the fair value of the contracts is reported as either assets or liabilities on our Condensed Consolidated Balance Sheets, and gains and losses resulting from changes in the fair value are reported in interest and other, net, in our Condensed Consolidated Statements of Operations. We do not enter into derivative financial contracts for speculative or trading purposes. At September 30, 2013, we had $52,576 of forward contracts outstanding to buy foreign currencies in exchange for U.S. dollars and $540,623 of forward contracts outstanding to sell foreign currencies in exchange for U.S. dollars, all of which have maturities of less than one year, and relate primarily to receivables from the release of *Grand Theft Auto V* in September 2013. At March 31, 2013, we had $55,397 of forward contracts outstanding to sell foreign currencies in exchange for U.S. dollars all of which have maturities of less than one year. For the three months ended September 30, 2013 and 2012, we recorded losses of $10,809 and $1,415, respectively, related to foreign currency forward contracts in interest and other, net on the Condensed Consolidated Statements of Operations. For the six months ended September 30, 2013 and 2012, we recorded a loss of $10,267 and a gain of $244, respectively, related to foreign currency forward contracts in interest and other, net on the Condensed Consolidated Statements of Operations. As of September 30, 2013, the fair value of these outstanding forward contracts was $1,935 and is included in prepaid expenses and other. As of March 31, 2013, the fair value of these outstanding forward contracts was immaterial and is included in accrued expenses and other current liabilities. The fair value of these outstanding forward contracts is estimated based on the prevailing exchange rates of the various hedged currencies as of the end of the period.

Revenue Recognition

Revenue Arrangements with Multiple Deliverables

We enter into multiple element revenue arrangements in which we may provide a combination of game software, additional content, maintenance or support. Assuming all other recognition criteria are met, for our software and software-related multiple element arrangements, we determine the fair value of each delivered and undelivered element using vendor-specific objective evidence ("VSOE") and allocate the total price among the various elements. Absent VSOE, revenue is deferred until the earlier of the point at which VSOE of fair value exists for any undelivered element or until all elements of the arrangement have been delivered. However, if the only undelivered element is maintenance and support, the entire arrangement fee is recognized ratably over the performance period. For arrangements which require that revenue recognition is deferred, the cost of goods sold is deferred and recognized as the related net revenue is recognized. Deferred cost of goods sold includes product costs, software development costs and royalties, internal royalties and license amortization and royalties. Changes in assumptions or judgments or changes to the elements in a software arrangement could cause a material increase or decrease in the amount of revenue that we report in a particular period. We determine VSOE for each element based on historical stand-alone sales to third parties. In

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TAKE-TWO INTERACTIVE SOFTWARE, INC.

Notes to Unaudited Condensed Consolidated Financial Statements (Continued)

(Dollars in thousands, except share and per share amounts)

1. BASIS OF PRESENTATION AND SIGNIFICANT ACCOUNTING POLICIES (Continued)

determining VSOE, we require that a substantial majority of the selling prices for a product or service fall within a reasonably narrow pricing range.

The deferred revenue and deferred cost of goods sold balances at September 30, 2013 consist primarily of unrecognized revenue and cost of goods sold from the release of *Grand Theft Auto V*, which released in September 2013, for which we do not have VSOE of fair value for the undelivered elements being delivered at a later date. *Grand Theft Auto V* includes access to *Grand Theft Auto Online* which launched in October 2013.

Recently Issued Accounting Pronouncements

Reclassification of Accumulated Other Comprehensive Income

In February 2013, new guidance was issued requiring new disclosures about reclassifications from accumulated other comprehensive income to net income. This new guidance requires an entity to provide information about the amounts reclassified out of accumulated other comprehensive income by component. In addition, an entity is required to present, either on the face of the statement where net income is presented or in the notes, significant amounts reclassified out of accumulated other comprehensive income by the respective line items of net income but only if the amount reclassified is required under U.S. GAAP to be reclassified to net income in its entirety in the same reporting period. For other amounts that are not required under U.S. GAAP to be reclassified in their entirety to net income, an entity is required to cross-reference to other disclosures required under U.S. GAAP that provide additional detail about those amounts. The new guidance is effective prospectively for annual and interim periods beginning after December 15, 2012 (April 1, 2013 for the Company). The adoption of this new guidance did not have a material impact on our Condensed Consolidated Financial Statements and the required disclosures are provided in Note 10.

Presentation of Unrecognized Tax Benefits

In July 2013, new guidance was issued requiring that entities that have an unrecognized tax benefit and a net operating loss carryforward or similar tax loss or tax credit carryforward in the same jurisdiction as the uncertain tax position present the unrecognized tax benefit as a reduction of the deferred tax asset for the loss or tax credit carryforward rather than as a liability when the uncertain tax position would reduce the loss or tax credit carryforward under the tax law. The disclosure requirements will be effective for annual periods (and interim periods within those annual periods) beginning after December 15, 2013 (June 30, 2014 for the Company), and will require prospective application. Early adoption is permitted. We are currently evaluating the impact on our Condensed Consolidated Financial Statements from the adoption of this guidance.

2. DISCONTINUED OPERATIONS

In February 2010, we completed the sale of our Jack of All Games third party distribution business, which primarily distributed third party interactive entertainment software, hardware and accessories in North America, for approximately $44,000, including $37,250 in cash, subject to purchase price adjustments, and up to an additional $6,750 subject to the achievement of certain items, which were not met. In April 2011, we settled on the purchase adjustments and as a result the purchase price

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TAKE-TWO INTERACTIVE SOFTWARE, INC.

Notes to Unaudited Condensed Consolidated Financial Statements (Continued)

(Dollars in thousands, except share and per share amounts)

2. DISCONTINUED OPERATIONS (Continued)

was lowered by $1,475. Consequently, the net purchase price after the settlement was $35,775. The sale has allowed us to focus our resources on our publishing operations. The financial information of our distribution business has been classified as discontinued operations in the Unaudited Condensed Consolidated Financial Statements for all of the periods presented. The following is a summary of the liabilities of discontinued operations primarily related to a liability for a lease assumption without economic benefit less estimates of sublease income. The lease matures on September 30, 2014.

	September 30, 2013	March 31, 2013
Liabilities of discontinued operations:		
Current:		
Accrued expenses and other current liabilities	**$ 1,123**	$ 1,232
Total current liabilities	**1,123**	1,232
Other non-current liabilities		556
Total liabilities of discontinued operations	**$ 1,123**	$ 1,788

3. MANAGEMENT AGREEMENT

In March 2007, we entered into a management services agreement (as amended, the "Management Agreement") with ZelnickMedia Corporation ("ZelnickMedia"), whereby ZelnickMedia provides us with certain management, consulting and executive level services. In May 2011, we entered into a new management agreement (the "New Management Agreement") with ZelnickMedia, which upon effectiveness, superseded and replaced the Management Agreement pursuant to which ZelnickMedia will continue to provide management, consulting and executive level services to the Company through May 2015. As part of the New Management Agreement, Strauss Zelnick, the President of ZelnickMedia, continues to serve as Executive Chairman and Chief Executive Officer and Karl Slatoff, a partner of ZelnickMedia, serves as President. The New Management Agreement provides for the annual management fee to remain at $2,500, subject to annual increases in the amount of 3% over the term of the agreement, and the maximum annual bonus was increased to $3,500 from $2,500, subject to annual increases in the amount of 3% over the term of the agreement, based on the Company achieving certain performance thresholds. In consideration for ZelnickMedia's services, we recorded consulting expense (a component of general and administrative expenses) of $2,056 and $1,095 for the three months ended September 30, 2013 and 2012, respectively, and $3,183 and $2,189 for the six months ended September 30, 2013 and 2012, respectively.

Pursuant to the Management Agreement, in August 2007, we issued stock options to ZelnickMedia to acquire 2,009,075 shares of our common stock at an exercise price of $14.74 per share, which vested over 36 months and expire 10 years from the date of grant. In June 2008, pursuant to the Management Agreement, we granted 600,000 shares of restricted stock to ZelnickMedia that vested annually over a three year period and 900,000 shares of market-based restricted stock that could have vested over a four year period through June 2012, provided that the Company's Total Shareholder Return (as defined in the relevant grant agreements) was at or higher than the 75th percentile of the NASDAQ Industrial Index measured annually on a cumulative basis. Because the price of our common stock did not

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TAKE-TWO INTERACTIVE SOFTWARE, INC.

Notes to Unaudited Condensed Consolidated Financial Statements (Continued)

(Dollars in thousands, except share and per share amounts)

3. MANAGEMENT AGREEMENT (Continued)

achieve its performance targets, the 900,000 shares of market-based restricted stock were forfeited in June 2012.

In addition, pursuant to the New Management Agreement, we granted 1,100,000 shares of restricted stock to ZelnickMedia that will vest annually through April 1, 2015 and 1,650,000 shares of market-based restricted stock that will be eligible to vest through April 1, 2015, based on the Company's Total Shareholder Return (as defined in the relevant grant agreements) relative to the Total Shareholder Return of the companies that constitute the NASDAQ Composite Index measured annually on a cumulative basis. To earn all of the shares of market-based restricted stock, the Company must perform at the 75th percentile, or top quartile, of the NASDAQ Composite Index. Each reporting period, we remeasure the fair value of the unvested portion of the shares of market-based restricted stock granted to ZelnickMedia. The unvested portion of the shares of restricted stock granted pursuant to the New Management Agreement as of September 30, 2013 and March 31, 2013 was 1,894,750 and 2,169,750 shares, respectively. For the three months ended September 30, 2013 and 2012, we recorded an expense of $5,633 and $1,524, respectively, of stock-based compensation (a component of general and administrative expenses) related to the shares of restricted stock granted pursuant to the New Management Agreement. For the six months ended September 30, 2013 and 2012, we recorded an expense of $6,120 and $741, respectively, of stock-based compensation (a component of general and administrative expenses) related to the shares of restricted stock granted pursuant to the New Management Agreement.

4. FAIR VALUE MEASUREMENTS

We follow a three-level fair value hierarchy that prioritizes the inputs used to measure fair value. This hierarchy requires entities to maximize the use of "observable inputs" and minimize the use of "unobservable inputs." The three levels of inputs used to measure fair value are as follows:

Level 1 Quoted prices in active markets for identical assets or liabilities.

Level 2 Observable inputs other than quoted prices included in Level 1, such as quoted prices for markets that are not active or other inputs that are observable or can be corroborated by observable market data.

Level 3 Unobservable inputs that are supported by little or no market activity and that are significant to the fair value of the assets or liabilities. This includes certain pricing models, discounted cash flow methodologies and similar techniques that use significant unobservable inputs.

The table below segregates all assets that are measured at fair value on a recurring basis (which is measured at least annually) into the most appropriate level within the fair value hierarchy based on the inputs used to determine the fair value at the measurement date.

	September 30, 2013	Quoted prices in active markets for identical assets (level 1)	Significant other observable inputs (level 2)	Significant unobservable inputs (level 3)	Balance Sheet Classification
Money market funds	$ 281,232	$ 281,232	$	$	Cash and cash equivalents
Bank-time deposits	$ 92,767	$ 92,767	$	$	Cash and cash equivalents

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TAKE-TWO INTERACTIVE SOFTWARE, INC.

Notes to Unaudited Condensed Consolidated Financial Statements (Continued)

(Dollars in thousands, except share and per share amounts)

5. INVENTORY

Inventory balances by category are as follows:

	September 30, 2013	March 31, 2013
Finished products	**$ 77,085**	$ 28,026
Parts and supplies	**6,948**	2,192
Inventory	**$ 84,033**	$ 30,218

Estimated product returns included in inventory at September 30, 2013 and March 31, 2013 were $1,696 and $1,505, respectively.

6. SOFTWARE DEVELOPMENT COSTS AND LICENSES

Details of our capitalized software development costs and licenses are as follows:

	September 30, 2013		March 31, 2013	
	Current	Non-current	Current	Non-current
Software development costs, internally developed	**$ 93,257**	**$ 43,378**	$ 178,297	$ 38,592
Software development costs, externally developed	**17,222**	**67,126**	10,469	53,649
Licenses	**9,055**	**3,001**	10,189	3,000
Software development costs and licenses	**$ 119,534**	**$ 113,505**	$ 198,955	$ 95,241

Software development costs and licenses as of September 30, 2013 and March 31, 2013 included $189,801 and $270,488, respectively, related to titles that have not been released. During the six months ended September 30, 2013, we recorded $29,636 of software development impairment charges (a component of cost of goods sold).

7. ACCRUED EXPENSES AND OTHER CURRENT LIABILITIES

Accrued expenses and other current liabilities consist of the following:

	September 30, 2013	March 31, 2013
Sales tax liability	**$ 78,159**	$ 3,950
Software development royalties	**59,109**	64,840
Income tax payable and deferred tax liability	**46,060**	53,261
Marketing and promotions	**34,519**	21,601
Compensation and benefits	**29,372**	33,564
Rent and deferred rent obligations	**8,774**	8,456
Professional fees	**6,024**	7,733
Licenses	**4,009**	12,268
Deferred consideration for acquisitions	**2,498**	2,498
Other	**26,468**	20,745
Accrued expenses and other current liabilities	**$ 294,992**	$ 228,916

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TAKE-TWO INTERACTIVE SOFTWARE, INC.

Notes to Unaudited Condensed Consolidated Financial Statements (Continued)

(Dollars in thousands, except share and per share amounts)

8. DEBT

Credit Agreement

In October 2011, we entered into a Second Amended and Restated Credit Agreement (the "Credit Agreement") which amended and restated our July 2007 Credit Agreement. The Credit Agreement provides for borrowings of up to $100,000 which may be increased by up to $40,000 pursuant to the terms of the Credit Agreement, and is secured by substantially all of our assets and the equity of our subsidiaries. The Credit Agreement expires on October 17, 2016. Revolving loans under the Credit Agreement bear interest at our election of (a) 1.50% to 2.00% above a certain base rate (4.75% at September 30, 2013), or (b) 2.50% to 3.00% above the LIBOR Rate (approximately 2.68% at September 30, 2013), with the margin rate subject to the achievement of certain average liquidity levels. We are also required to pay a monthly fee on the unused available balance, ranging from 0.375% to 0.50% based on availability. We had no outstanding borrowings at September 30, 2013 and March 31, 2013.

Availability under the Credit Agreement is restricted by our United States and United Kingdom based accounts receivable and inventory balances. The Credit Agreement also allows for the issuance of letters of credit in an aggregate amount of up to $25,000.

Information related to availability on our Credit Agreement is as follows:

	September 30, 2013	March 31, 2013
Available borrowings	**$ 70,736**	$ 73,565
Outstanding letters of credit	**1,664**	1,664

We recorded interest expense and fees related to the Credit Agreement of $160 for the three months ended September 30, 2013 and 2012 and $319 for the six months ended September 30, 2013 and 2012.

The Credit Agreement contains covenants that substantially limit us and our subsidiaries' ability to: create, incur, assume or be liable for indebtedness; dispose of assets outside the ordinary course of business; acquire, merge or consolidate with or into another person or entity; create, incur or allow any lien on any of their respective properties; make investments; or pay dividends or make distributions (each subject to certain limitations); or optionally prepay any indebtedness (subject to certain exceptions, including an exception permitting the redemption of the Company's unsecured convertible senior notes upon the meeting of certain minimum liquidity requirements). In addition, the Credit Agreement provides for certain events of default such as nonpayment of principal and interest, breaches of representations and warranties, noncompliance with covenants, acts of insolvency, default on indebtedness held by third parties and default on certain material contracts (subject to certain limitations and cure periods). The Credit Agreement also contains a requirement that we maintain an interest coverage ratio of more than one to one for the trailing twelve month period, if certain average liquidity levels fall below $30,000. As of September 30, 2013, we were in compliance with all covenants and requirements outlined in the Credit Agreement.

TAKE-TWO INTERACTIVE SOFTWARE, INC.

Notes to Unaudited Condensed Consolidated Financial Statements (Continued)

(Dollars in thousands, except share and per share amounts)

8. DEBT (Continued)

4.375% Convertible Notes Due 2014

In June 2009, we issued $138,000 aggregate principal amount of 4.375% Convertible Notes due 2014 (the "4.375% Convertible Notes"). The issuance of the 4.375% Convertible Notes included $18,000 related to the exercise of an over-allotment option by the underwriters. Interest on the 4.375% Convertible Notes was paid semi-annually in arrears on June 1st and December 1st of each year, and commenced on December 1, 2009. The 4.375% Convertible Notes were scheduled to mature on June 1, 2014, unless earlier redeemed or repurchased by the Company or converted. As further described below, on June 12, 2013, we issued a notice of redemption calling all of our outstanding 4.375% Convertible Notes for redemption on August 29, 2013.

The 4.375% Convertible Notes were convertible at an initial conversion rate of 93.6768 shares of our common stock per $1 principal amount of 4.375% Convertible Notes (representing an initial conversion price of approximately $10.675 per share of common stock for a total of approximately 12,927,000 underlying conversion shares) subject to adjustment in certain circumstances. Holders could have converted the 4.375% Convertible Notes at their option prior to the close of business on the business day immediately preceding December 1, 2013 only under the following circumstances: (1) during any fiscal quarter commencing after July 31, 2009, if the last reported sale price of the common stock for at least 20 trading days (whether or not consecutive) during a period of 30 consecutive trading days ending on the last trading day of the preceding fiscal quarter was greater than or equal to 130% of the applicable conversion price on each applicable trading day; (2) during the five business day period after any 10 consecutive trading day period (the "measurement period") in which the trading price per $1 principal amount of 4.375% Convertible Notes for each day of that measurement period was less than 98% of the product of the last reported sale price of our common stock and the applicable conversion rate on each such day; (3) if we called the 4.375% Convertible Notes for redemption, at any time prior to the close of business on the third scheduled trading day prior to the redemption date; or (4) upon the occurrence of specified corporate events. Upon conversion, the 4.375% Convertible Notes could have been settled, at our election, in cash, shares of our common stock, or a combination of cash and shares of the Company's common stock.

We recorded approximately $3,410 of banking, legal and accounting fees related to the issuance of the 4.375% Convertible Notes which were capitalized as debt issuance costs and were being amortized to interest and other, net over the term of the 4.375% Convertible Notes.

At any time on or after June 5, 2012, the Company could have redeemed all of the outstanding 4.375% Convertible Notes for cash, but only if the last reported sale of our common stock for 20 or more trading days in a period of 30 consecutive trading days ending on the trading day prior to the date we provided notice of redemption to holders of the 4.375% Convertible Notes exceeded 150% of the conversion price in effect on each such trading day. This condition was met on June 12, 2013. The redemption price equaled 100% of the principal amount of the 4.375% Convertible Notes to be redeemed, plus all accrued and unpaid interest (including additional interest, if any) to, but excluding, the redemption date.

On June 12, 2013, we issued a notice of redemption calling all of our outstanding 4.375% Convertible Notes, in the aggregate principal amount of $138,000, for redemption on August 29, 2013 at a redemption price of $1 per $1 principal amount, plus accrued and unpaid interest up to, but not

TAKE-TWO INTERACTIVE SOFTWARE, INC.

Notes to Unaudited Condensed Consolidated Financial Statements (Continued)

(Dollars in thousands, except share and per share amounts)

8. DEBT (Continued)

including, the redemption date. Holders who elected to convert following receipt of the notice of redemption were entitled to make-whole shares in addition to such shares they would otherwise be entitled to receive upon conversion. The notice of redemption specified that we would settle any 4.375% Convertible Notes surrendered for conversion in connection with the redemption on a combination settlement basis by paying cash up to a cash amount equal to $166,000 in the aggregate of converted notes and delivering shares of our common stock in respect of the amount, if any, by which our conversion obligation exceeded such cash amount. During the three and six months ended September 30, 2013, at the option of the holders, $137,993 of 4.375% Convertible Notes were converted for $165,992 in cash and 3,217,000 shares of our common stock. On August 29, 2013, we redeemed $7 of 4.375% Convertible Notes and we paid $7 in cash. During the three and six months ended September 30, 2013, we recorded a loss on extinguishment, net of capitalized debt issuance costs, totaling $9,014 related to these transactions.

In connection with the offering of the 4.375% Convertible Notes, we entered into convertible note hedge transactions which were expected to reduce the potential dilution to our common stock upon conversion of the 4.375% Convertible Notes. The transactions included options to purchase approximately 12,927,000 shares of common stock at $10.675 per share, expiring on June 1, 2014, for a total cost of approximately $43,600, which was charged to additional paid-in capital.

Separately, the Company entered into warrant transactions with a strike price of $14.945 per share. The warrants covered approximately 12,927,000 shares of the Company's common stock and were scheduled to expire on August 30, 2014, for total proceeds of approximately $26,300, which was credited to additional paid-in capital.

On June 12, 2013, the Company entered into Unwind Agreements with respect to the convertible note hedge transactions and Unwind Agreements with respect to the warrant transactions with each of the hedge counterparties (collectively, the "Unwind Agreements"). Pursuant to the terms of the Unwind Agreements, and in connection with the Company's issuance of a notice of redemption for all the 4.375% Convertible Notes, the Company had the right to deliver a notice to the hedge counterparties, prior to the redemption date set forth in such redemption notice, designating an early termination date for the convertible note hedge transactions and warrant transactions. The hedge counterparties owed a cash payment to the Company as a result of the early termination of the convertible note hedge transactions that was calculated based on its current fair market value. The Company owed a cash payment to the hedge counterparties, as applicable, as a result of the early termination of the warrant transactions that was calculated based on its current fair market value. As a result of the Unwind Agreements, the convertible note hedge transactions and warrant transactions were accounted for as derivatives whereby the fair values of these transactions were reported as a convertible note hedge receivable and as a convertible note warrant liability with an offsetting impact to additional paid-in capital. Gains and losses resulting from changes in the fair value were reported in gain on convertible note hedge and warrants, net, in our Condensed Consolidated Statements of Operations. In August 2013, the payment received from unwinding the associated convertible note hedge transactions resulted in proceeds to us of $84,429, offset by $55,651 we paid the warrants holders.

During the three months ended September 30, 2013, we recorded a gain of approximately $21,670 resulting from the change in the fair value of the convertible note hedge transactions and a loss of

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TAKE-TWO INTERACTIVE SOFTWARE, INC.

Notes to Unaudited Condensed Consolidated Financial Statements (Continued)

(Dollars in thousands, except share and per share amounts)

8. DEBT (Continued)

approximately $16,298 resulting from the change in the fair value of the convertible note warrant liability to gain on convertible note hedge and warrants, net, in our Condensed Consolidated Statements of Operations. During the six months ended September 30, 2013, we recorded a gain of approximately $17,259 resulting from the change in the fair value of the convertible note hedge transactions and a loss of approximately $13,798 resulting from the change in the fair value of the convertible note warrant liability to gain on convertible note hedge and warrants, net, in our Condensed Consolidated Statements of Operations.

The following table provides additional information related to our 4.375% Convertible Notes:

	March 31, 2013
Additional paid-in capital	$ 42,018
Principal amount of 4.375% Convertible Notes	$ 138,000
Unamortized discount of the liability component	12,819
Net carrying amount of 4.375% Convertible Notes	$ 125,181
Carrying amount of debt issuance costs	$ 797

The following table provides the components of interest expense related to our 4.375% Convertible Notes:

	Three Months Ended September 30,		Six Months Ended September 30,	
	2013	2012	**2013**	2012
Cash interest expense (coupon interest expense)	**$ 1,007**	$ 1,509	**$ 2,516**	$ 3,018
Non-cash amortization of discount on 4.375% Convertible Notes	**1,771**	2,347	**4,358**	4,620
Amortization of debt issuance costs	**113**	170	**284**	341
Total interest expense related to 4.375% Convertible Notes	**$ 2,891**	$ 4,026	**$ 7,158**	$ 7,979

1.75% Convertible Notes Due 2016

On November 16, 2011, we issued $250,000 aggregate principal amount of 1.75% Convertible Notes due 2016 (the "1.75% Convertible Notes"). Interest on the 1.75% Convertible Notes is payable semi-annually in arrears on June 1st and December 1st of each year, commencing on June 1, 2012. The 1.75% Convertible Notes mature on December 1, 2016, unless earlier repurchased by the Company or converted. The Company does not have the right to redeem the 1.75% Convertible Notes prior to maturity.

The 1.75% Convertible Notes are convertible at an initial conversion rate of 52.3745 shares of our common stock per $1 principal amount of 1.75% Convertible Notes (representing an initial conversion price of approximately $19.093 per share of common stock for a total of approximately 13,094,000

TAKE-TWO INTERACTIVE SOFTWARE, INC.

Notes to Unaudited Condensed Consolidated Financial Statements (Continued)

(Dollars in thousands, except share and per share amounts)

8. DEBT (Continued)

underlying conversion shares) subject to adjustment in certain circumstances. Holders may convert the 1.75% Convertible Notes at their option prior to the close of business on the business day immediately preceding June 1, 2016 only under the following circumstances: (1) during any fiscal quarter commencing after March 31, 2012, if the last reported sale price of the common stock for at least 20 trading days (whether or not consecutive) during a period of 30 consecutive trading days ending on the last trading day of the preceding fiscal quarter is greater than or equal to 130% of the applicable conversion price on each applicable trading day; (2) during the five business day period after any 10 consecutive trading day period (the "measurement period") in which the trading price per $1 principal amount of 1.75% Convertible Notes for each day of that measurement period was less than 98% of the product of the last reported sale price of our common stock and the applicable conversion rate on each such day; or (3) upon the occurrence of specified corporate events. On and after June 1, 2016 until the close of business on the business day immediately preceding the maturity date, holders may convert their 1.75% Convertible Notes at any time, regardless of the foregoing circumstances. Upon conversion, the 1.75% Convertible Notes may be settled, at our election, in cash, shares of our common stock, or a combination of cash and shares of the Company's common stock.

Upon the occurrence of certain fundamental changes involving the Company, holders of the 1.75% Convertible Notes may require us to purchase all or a portion of their 1.75% Convertible Notes for cash at a price equal to 100% of the principal amount of the notes to be purchased, plus accrued and unpaid interest (including additional interest, if any) to, but excluding, the fundamental change purchase date.

The indenture governing the 1.75% Convertible Notes contains customary terms and covenants and events of default. If an event of default (as defined therein) occurs and is continuing, the Trustee by notice to the Company, or the holders of at least 25% in aggregate principal amount of the 1.75% Convertible Notes then outstanding by notice to the Company and the Trustee, may, and the Trustee at the request of such holders shall, declare 100% of the principal of and accrued and unpaid interest (including additional interest, if any) on all the 1.75% Convertible Notes to be due and payable. In the case of an event of default arising out of certain bankruptcy events, 100% of the principal of and accrued and unpaid interest (including additional interest, if any), on the 1.75% Convertible Notes will automatically become due and payable immediately. As of September 30, 2013, we were in compliance with all covenants and requirements outlined in the indenture governing the 1.75% Convertible Notes.

The 1.75% Convertible Notes are senior unsecured obligations and rank senior in right of payment to our existing and future indebtedness that is expressly subordinated in right of payment to the 1.75% Convertible Notes; equal in right of payment to our existing and future indebtedness that is not so subordinated; effectively junior in right of payment to any of our secured indebtedness to the extent of the value of the assets securing such indebtedness; and structurally junior to all existing and future indebtedness incurred by our subsidiaries.

In accounting for the $6,875 of banking, legal and accounting fees related to the issuance of the 1.75% Convertible Notes, we allocated $5,428 to the liability component and $1,447 to the equity component. Debt issuance costs attributable to the liability component are being amortized to interest and other, net over the term of the 1.75% Convertible Notes, and issuance costs attributable to the equity component were netted with the equity component in additional paid-in capital.