

ELECTRONIC ARTS INC.
Form 10-Q
August 09, 2010
[Table of Contents](#)

UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
WASHINGTON, D.C. 20549
FORM 10-Q

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

For the Quarterly Period Ended June 30, 2010

OR

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

For the Transition Period from _____ to _____

Commission File No. 0-17948

ELECTRONIC ARTS INC.

(Exact name of registrant as specified in its charter)

Delaware
(State or other jurisdiction of

incorporation or organization)

94-2838567
(I.R.S. Employer

Identification No.)

209 Redwood Shores Parkway

94065

Edgar Filing: ELECTRONIC ARTS INC. - Form 10-Q

Redwood City, California
(Address of principal executive offices)

(650) 628-1500

(Zip Code)

(Registrant's telephone number, including area code)

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

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

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, 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.

Large accelerated filer ☒ Accelerated filer ☐ Non-accelerated filer ☐ Smaller reporting company ☐
(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 ☐ NO ☒

As of August 5, 2010, there were 330,295,574 shares of the Registrant's Common Stock, par value \$0.01 per share, outstanding.

Table of Contents

ELECTRONIC ARTS INC.

FORM 10-Q

FOR THE PERIOD ENDED JUNE 30, 2010

Table of Contents

	Page
<u>Part I - FINANCIAL INFORMATION</u>	
Item 1. <u>Condensed Consolidated Financial Statements (Unaudited)</u>	
<u>Condensed Consolidated Balance Sheets as of June 30, 2010 and March 31, 2010</u>	3
<u>Condensed Consolidated Statements of Operations for the Three Months Ended June 30, 2010 and 2009</u>	4
<u>Condensed Consolidated Statements of Cash Flows for the Three Months Ended June 30, 2010 and 2009</u>	5
<u>Notes to Condensed Consolidated Financial Statements (Unaudited)</u>	6
<u>Report of Independent Registered Public Accounting Firm</u>	25
Item 2. <u>Management's Discussion and Analysis of Financial Condition and Results of Operations</u>	26
Item 3. <u>Quantitative and Qualitative Disclosures About Market Risk</u>	45
Item 4. <u>Controls and Procedures</u>	48
<u>Part II - OTHER INFORMATION</u>	
Item 1. <u>Legal Proceedings</u>	49
Item 1A. <u>Risk Factors</u>	49
Item 5. <u>Other Information</u>	58
Item 6. <u>Exhibits</u>	59
<u>Signature</u>	60
<u>Exhibit Index</u>	61

Table of Contents**PART I FINANCIAL INFORMATION****Item 1. Condensed Consolidated Financial Statements (Unaudited)**
ELECTRONIC ARTS INC. AND SUBSIDIARIES**CONDENSED CONSOLIDATED BALANCE SHEETS****(Unaudited)**

(In millions, except par value data)	June 30, 2010	March 31, 2010 (a)
ASSETS		
Current assets:		
Cash and cash equivalents	\$ 1,057	\$ 1,273
Short-term investments	480	432
Marketable equity securities	193	291
Receivables, net of allowances of \$180 and \$217, respectively	103	206
Inventories	82	100
Deferred income taxes, net	43	44
Other current assets	270	239
Total current assets	2,228	2,585
Property and equipment, net	516	537
Goodwill	1,090	1,093
Acquisition-related intangibles, net	185	204
Deferred income taxes, net	49	52
Other assets	177	175
TOTAL ASSETS	\$ 4,245	\$ 4,646
LIABILITIES AND STOCKHOLDERS' EQUITY		
Current liabilities:		
Accounts payable	\$ 55	\$ 91
Accrued and other current liabilities	620	717
Deferred net revenue (packaged goods and digital content)	490	766
Total current liabilities	1,165	1,574
Income tax obligations	229	242
Deferred income taxes, net	2	2
Other liabilities	97	99
Total liabilities	1,493	1,917
Commitments and contingencies (See Note 10)		
Stockholders' equity:		
Preferred stock, \$0.01 par value. 10 shares authorized		
Common stock, \$0.01 par value. 1,000 shares authorized; 330 and 330 shares issued and outstanding, respectively	3	3
Paid-in capital	2,417	2,375
Retained earnings	219	123
Accumulated other comprehensive income	113	228

Edgar Filing: ELECTRONIC ARTS INC. - Form 10-Q

Total stockholders' equity	2,752	2,729
TOTAL LIABILITIES AND STOCKHOLDERS' EQUITY	\$ 4,245	\$ 4,646

See accompanying Notes to Condensed Consolidated Financial Statements (unaudited).

(a) Derived from audited consolidated financial statements.

Table of Contents**ELECTRONIC ARTS INC. AND SUBSIDIARIES****CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS**

(Unaudited)		Three Months Ended	
		June 30,	
(In millions, except per share data)		2010	2009
Net revenue		\$ 815	\$ 644
Cost of goods sold		222	321
Gross profit		593	323
Operating expenses:			
Marketing and sales		127	164
General and administrative		74	66
Research and development		275	312
Amortization of intangibles		15	12
Acquisition-related contingent consideration		2	
Restructuring charges		2	14
Total operating expenses		495	568
Operating income (loss)		98	(245)
Losses on strategic investments		(5)	(16)
Interest and other income, net			3
Income (loss) before benefit from income taxes		93	(258)
Benefit from income taxes		(3)	(24)
Net income (loss)		\$ 96	\$ (234)
Net income (loss) per share:			
Basic		\$ 0.29	\$ (0.72)
Diluted		\$ 0.29	\$ (0.72)
Number of shares used in computation:			
Basic		328	323
Diluted		332	323

See accompanying Notes to Condensed Consolidated Financial Statements (unaudited).

Table of Contents**ELECTRONIC ARTS INC. AND SUBSIDIARIES****CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS**

(Unaudited)	Three Months Ended June 30,	
	2010	2009
(In millions)		
OPERATING ACTIVITIES		
Net income (loss)	\$ 96	\$ (234)
Adjustments to reconcile net income (loss) to net cash used in operating activities:		
Depreciation, amortization and accretion, net	48	48
Stock-based compensation	47	33
Non-cash restructuring charges		7
Net losses on investments and sale of property and equipment	5	15
Acquisition-related contingent consideration	2	
Change in assets and liabilities:		
Receivables, net	97	(252)
Inventories	16	4
Other assets	(37)	(35)
Accounts payable	(40)	8
Accrued and other liabilities	(109)	(82)
Deferred income taxes, net	3	(12)
Deferred net revenue (packaged goods and digital content)	(276)	172
Net cash used in operating activities	(148)	(328)
INVESTING ACTIVITIES		
Capital expenditures	(11)	(8)
Proceeds from sale of marketable equity securities	8	
Proceeds from maturities and sales of short-term investments	98	168
Purchase of short-term investments	(148)	(269)
Acquisition of subsidiaries, net of cash acquired		(3)
Net cash used in investing activities	(53)	(112)
FINANCING ACTIVITIES		
Proceeds from issuance of common stock	1	3
Net cash provided by financing activities	1	3
Effect of foreign exchange on cash and cash equivalents	(16)	21
Decrease in cash and cash equivalents	(216)	(416)
Beginning cash and cash equivalents	1,273	1,621
Ending cash and cash equivalents	\$ 1,057	\$ 1,205
Supplemental cash flow information:		
Cash paid (refunded) during the period for income taxes, net	\$ 6	\$ (2)
Non-cash investing activities:		
Change in unrealized gains (losses) on investments, net of taxes	\$ (89)	\$ 77

Edgar Filing: ELECTRONIC ARTS INC. - Form 10-Q

See accompanying Notes to Condensed Consolidated Financial Statements (unaudited).

Table of Contents

ELECTRONIC ARTS INC. AND SUBSIDIARIES

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

(Unaudited)

(1) DESCRIPTION OF BUSINESS AND BASIS OF PRESENTATION

We develop, market, publish and distribute video game software and content that can be played by consumers on a variety of platforms, including video game consoles (such as the PLAYSTATION® 3, Microsoft Xbox 360 and Nintendo Wii), personal computers, handheld game players (such as the PlayStation® Portable (PSP) and the Nintendo DS), mobile devices (such as cellular and smart phones including the Apple iPhone) and wireless devices such as the Apple iPad™. Some of our games are based on content that we license from others (*e.g.*, FIFA Soccer, Madden NFL Football, Harry Potter, and Hasbro's toy and game intellectual properties), and some of our games are based on our own wholly-owned intellectual property (*e.g.*, The Sims, Need for Speed, and Dead Space). Our goal is to publish titles with global mass-market appeal, which often means translating and localizing them for sale in non-English speaking countries. In addition, we also attempt to create software game franchises that allow us to publish new titles on a recurring basis that are based on the same property. Examples of this franchise approach are the annual iterations of our sports-based products (*e.g.*, FIFA Soccer, Madden NFL Football, and NCAA® Football), wholly-owned properties that can be successfully sequenced (*e.g.*, The Sims, Need for Speed and Battlefield) and titles based on long-lived literary and/or movie properties (*e.g.*, Harry Potter).

Our fiscal year is reported on a 52 or 53-week period that ends on the Saturday nearest March 31. Our results of operations for the fiscal years ending or ended, as the case may be, March 31, 2011 and 2010 contain 52 and 53 weeks, respectively, and ends or ended, as the case may be, on April 2, 2011 and April 3, 2010, respectively. Our results of operations for the three months ended June 30, 2010 and 2009 contained 13 weeks and 14 weeks, respectively, and ended on July 3, 2010 and July 4, 2009, respectively. For simplicity of disclosure, all fiscal periods are referred to as ending on a calendar month end.

The Condensed Consolidated Financial Statements are unaudited and reflect all adjustments (consisting only of normal recurring accruals unless otherwise indicated) that, in the opinion of management, are necessary for a fair presentation of the results for the interim periods presented. The preparation of these Condensed Consolidated Financial Statements requires management to make estimates and assumptions that affect the amounts reported in these Condensed Consolidated Financial Statements and accompanying notes. Actual results could differ materially from those estimates. The results of operations for the current interim periods are not necessarily indicative of results to be expected for the current year or any other period.

These Condensed Consolidated Financial Statements should be read in conjunction with the Consolidated Financial Statements and Notes thereto included in our Annual Report on Form 10-K for the fiscal year ended March 31, 2010, as filed with the United States Securities and Exchange Commission (SEC) on May 28, 2010.

(2) FAIR VALUE MEASUREMENTS

Fair value is the price that would be received from selling an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. When determining fair value, we consider the principal or most advantageous market in which we would transact, and we consider assumptions that market participants would use when pricing the asset or liability. We measure certain financial and nonfinancial assets and liabilities at fair value on a recurring and nonrecurring basis.

Fair Value Hierarchy

The three levels of inputs that may be 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 within Level 1, such as quoted prices for similar assets or liabilities, quoted prices in markets with insufficient volume or infrequent transactions (less active markets), or model-derived valuations in

Edgar Filing: ELECTRONIC ARTS INC. - Form 10-Q

which all significant inputs are observable or can be derived principally from or corroborated with observable market data for substantially the full term of the assets or liabilities.

Level 3. Unobservable inputs to the valuation methodology that are significant to the measurement of the fair value of assets or liabilities.

Table of Contents

Assets and Liabilities Measured at Fair Value on a Recurring Basis

Our money market funds, available-for-sale fixed income and marketable equity securities, deferred compensation plan assets, foreign currency derivatives and contingent consideration are measured and recorded at fair value on a recurring basis.

Our Level 1 assets are valued using quoted prices in active markets for identical instruments. Our Level 2 assets, including foreign currency derivatives, are valued using quoted prices for identical instruments in less active markets or using other observable market inputs for comparable instruments. Our Level 3 liability is valued using unobservable inputs to the valuation methodology that are significant to the measurement of the fair value of the contingent consideration.

Table of Contents

As of June 30, 2010 and March 31, 2010, our assets and liabilities that are measured and recorded at fair value on a recurring basis were as follows (in millions):

Fair Value Measurements at Reporting Date Using Quoted Prices in Active Markets for Significant Identical Financial Instruments Other Observable Inputs Significant Unobservable Inputs					
	As of June 30, 2010	(Level 1)	(Level 2)	(Level 3)	Balance Sheet Classification
Assets					
Money market funds	\$ 636	\$ 636	\$	\$	Cash equivalents
Available-for-sale securities:					
Marketable equity securities	193	193			Marketable equity securities
Corporate bonds	254		254		Short-term investments
U.S. agency securities	125		125		Short-term investments and cash equivalents
U.S. Treasury securities	101	101			Short-term investments and cash equivalents
Commercial paper	11		11		Short-term investments and cash equivalents
Deferred compensation plan assets ^(a)	11	11			Other assets
Foreign currency derivatives	4		4		Other current assets
Total assets at fair value	\$ 1,335	\$ 941	\$ 394	\$	
Liability					
Contingent consideration ^(b)	\$ 67	\$	\$	\$ 67	Accrued and other current liabilities and other liabilities
Total liability at fair value	\$ 67	\$	\$	\$ 67	

Fair Value Measurements Using Significant Unobservable Inputs (Level 3) Contingent Consideration		
Balance as of March 31, 2010		\$ 65
Change in fair value ^(c)		2
Balance as of June 30, 2010		\$ 67

	As of March 31, 2010	(Level 1)	(Level 2)	(Level 3)	Balance Sheet Classification
Assets					
Money market funds	\$ 619	\$ 619	\$	\$	Cash equivalents
Available-for-sale securities:					
Marketable equity securities	291	291			Marketable equity securities
Corporate bonds	234		234		Short-term investments and cash equivalents
U.S. agency securities	118		118		Short-term investments and cash equivalents
U.S. Treasury securities	93	93			Short-term investments and cash equivalents
Commercial paper	12		12		Short-term investments and cash equivalents
Deferred compensation plan assets ^(a)	12	12			Other assets
Foreign currency derivatives	2		2		Other current assets
Total assets at fair value	\$ 1,381	\$ 1,015	\$ 366	\$	

Edgar Filing: ELECTRONIC ARTS INC. - Form 10-Q

Liability

Contingent consideration ^(b)	\$	65	\$		\$	65	Accrued and other current liabilities and other liabilities
Total liability at fair value	\$	65	\$		\$	65	

(a) The deferred compensation plan assets consist of various mutual funds.

(b) The contingent consideration represents the estimated fair value of the additional variable cash consideration payable in connection with our acquisition of Playfish Limited ("Playfish") that is contingent upon the achievement of certain performance milestones. We estimated the fair value using expected future cash flows over the period in which the obligation is expected to be settled, and applied a discount rate that appropriately captures a market participant's view of the risk associated with the obligation.

(c) The change in fair value is reported as acquisition-related contingent consideration in our Condensed Consolidated Statements of Operations.

Table of Contents**Assets and Liabilities Measured at Fair Value on a Nonrecurring Basis**

We reviewed our financial and nonfinancial assets and liabilities for the three months ended June 30, 2010 and 2009 and concluded there were no material impairment charges during each of these periods.

(3) FINANCIAL INSTRUMENTS**Cash, Cash Equivalents and Short-Term Investments**

Cash, cash equivalents and short-term investments consisted of the following as of June 30, 2010 and March 31, 2010 (in millions):

	As of June 30, 2010			As of March 31, 2010			
	Cost or	Gross Unrealized		Cost or	Gross Unrealized		
	Amortized	Gains	Losses	Amortized	Gains	Losses	Fair Value
	Cost			Cost			Fair Value
Cash and cash equivalents:							
Cash	\$ 410	\$	\$	\$ 410	\$	\$	\$ 629
Money market funds	636			636			619
U.S. Treasury securities	5			5			10
Commercial paper	4			4			11
U.S. agency securities	2			3			3
Corporate bonds				1			1
Cash and cash equivalents	1,057			1,057	1,273		1,273
Short-term investments:							
Corporate bonds	252	2		254	2		233
U.S. agency securities	123			123			115
U.S. Treasury securities	96			83			83
Commercial paper	7			7			1
Short-term investments	478	2		480	2		432
Cash, cash equivalents and short-term investments	\$ 1,535	\$ 2	\$	\$ 1,537	\$ 2	\$	\$ 1,705

We evaluate our investments for impairment quarterly. Factors considered in the review of investments with an unrealized loss include the credit quality of the issuer, the duration that the fair value has been less than the adjusted cost basis, severity of the impairment, reason for the decline in value and potential recovery period, the financial condition and near-term prospects of the investees, our intent to sell the investments, any contractual terms impacting the prepayment or settlement process, as well as if we would be required to sell an investment due to liquidity or contractual reasons before its anticipated recovery. Based on our review, we did not consider the investments listed above to be other-than-temporarily impaired as of June 30, 2010 and March 31, 2010.

The following table summarizes the amortized cost and fair value of our short-term investments, classified by stated maturity as of June 30, 2010 and March 31, 2010 (in millions):

	As of June 30, 2010		As of March 31, 2010	
	Amortized Cost	Fair Value	Amortized Cost	Fair Value
Short-term investments				
Due in 1 year or less	\$ 211	\$ 211	\$ 165	\$ 165

Edgar Filing: ELECTRONIC ARTS INC. - Form 10-Q

Due in 1-2 years	167	168	174	176
Due in 2-3 years	100	101	91	91
Short-term investments	\$ 478	\$ 480	\$ 430	\$ 432

Table of Contents***Marketable Equity Securities***

Our investments in marketable equity securities consist of investments in common stock of publicly traded companies and are accounted for as available-for-sale securities and are recorded at fair value. Unrealized gains and losses are recorded as a component of accumulated other comprehensive income in stockholders' equity, net of tax, until either the security is sold or we determine that the decline in fair value of a security to a level below its adjusted cost basis is other-than-temporary. We evaluate our investments for impairment quarterly. If we conclude that an investment is other-than-temporarily impaired, we will recognize an impairment charge at that time in our Condensed Consolidated Statements of Operations.

Marketable equity securities consisted of the following as of June 30, 2010 and March 31, 2010 (in millions):

	Adjusted Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value
As of June 30, 2010	\$ 119	\$ 74	\$	\$ 193
As of March 31, 2010	\$ 132	\$ 159	\$	\$ 291

During the three months ended June 30, 2010 and 2009, we recognized impairment charges of \$2 million and \$16 million, respectively, on our investment in The9. Due to various factors, including but not limited to, the extent and duration during which the market prices of these securities had been below adjusted cost and our intent to hold these securities, we concluded the decline in values were other-than-temporary. The impairments for the three months ended June 30, 2010 and 2009 are included in losses on strategic investments in our Condensed Consolidated Statements of Operations.

During the three months ended June 30, 2010, we received proceeds of \$8 million and realized losses of \$3 million from selling a portion of our investment in The9. We did not sell any of our marketable equity securities during the three months ended June 30, 2009. The realized losses for the three months ended June 30, 2010 are included in losses on strategic investments in our Condensed Consolidated Statements of Operations.

In February 2005, we purchased approximately 19.9 percent of the then-outstanding ordinary shares (representing approximately 18 percent of the voting rights at the time) of Ubisoft Entertainment for \$91 million. Subsequent to June 30, 2010, we sold this investment for approximately \$121 million.

Other Investments Included in Other Assets

Our other investments, included in other assets on our Condensed Consolidated Balance Sheets, consist principally of non-voting preferred shares in two companies whose common stock is publicly traded and are accounted for under the cost method. Under this method, these investments are recorded at cost until we determine that the fair value of the investment has fallen below its adjusted cost basis and that such decline is other-than-temporary. We evaluate our investments for impairment quarterly. When we conclude that an investment is other-than-temporarily impaired, we recognize an impairment charge at that time in our Condensed Consolidated Statements of Operations.

During the three months ended June 30, 2010 and 2009, we did not recognize any impairment charges with respect to these investments.

(4) DERIVATIVE FINANCIAL INSTRUMENTS

The assets or liabilities associated with our derivative instruments and hedging activities are recorded at fair value in other current assets or accrued and other current liabilities, respectively, in our Condensed Consolidated Balance Sheets. As discussed below, the accounting for gains and losses resulting from changes in fair value depends on the use of the derivative instrument and whether it is designated and qualifies for hedge accounting.

We transact business in various foreign currencies and have significant international sales and expenses denominated in foreign currencies, subjecting us to foreign currency risk. We purchase foreign currency option contracts, generally with maturities of 15 months or less, to reduce the volatility of cash flows primarily related to forecasted revenue and expenses denominated in certain foreign currencies. In addition, we utilize foreign currency forward contracts to mitigate foreign exchange rate risk associated with foreign-currency-denominated monetary assets and liabilities, primarily intercompany receivables and payables. The foreign currency forward contracts generally have a contractual term of approximately three months or less and are transacted near month-end. At each quarter-end, the fair value of the foreign currency forward

Edgar Filing: ELECTRONIC ARTS INC. - Form 10-Q

contracts generally is not significant. We do not use foreign currency option or foreign currency forward contracts for speculative or trading purposes.

Table of Contents***Cash Flow Hedging Activities***

Our foreign currency option contracts are designated and qualify as cash flow hedges. The effectiveness of the cash flow hedge contracts, including time value, is assessed monthly using regression analysis, as well as other timing and probability criteria. To receive hedge accounting treatment, all hedging relationships are formally documented at the inception of the hedge and the hedges must be highly effective in offsetting changes to future cash flows on hedged transactions. The effective portion of gains or losses resulting from changes in fair value of these hedges is initially reported, net of tax, as a component of accumulated other comprehensive income in stockholders' equity. The gross amount of the effective portion of gains or losses resulting from changes in fair value of these hedges is subsequently reclassified into net revenue 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 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 income, net, in our Condensed Consolidated Statements of Operations. In the event that the underlying forecasted transactions do not occur, or it becomes remote that they will occur, within the defined hedge period, the gains or losses on the related cash flow hedges are reclassified from accumulated other comprehensive income to interest and other income, net, in our Condensed Consolidated Statements of Operations. During the reporting periods all forecasted transactions occurred and, therefore, there were no such gains or losses reclassified into interest and other income, net. As of June 30, 2010, we had foreign currency option contracts to purchase approximately \$13 million in foreign currency and to sell approximately \$166 million of foreign currencies. All of the foreign currency option contracts outstanding as of June 30, 2010 will mature in the next 12 months. As of March 31, 2010, we had foreign currency option contracts to purchase approximately \$18 million in foreign currency and to sell approximately \$30 million of foreign currencies. As of June 30, 2010 and March 31, 2010, these foreign currency option contracts outstanding had a total fair value of \$4 million and \$2 million, respectively, and are included in other current assets.

The effect of foreign currency option contracts on our Condensed Consolidated Statements of Operations for the three months ended June 30, 2010 and 2009 was immaterial.

Balance Sheet Hedging Activities

Our foreign currency forward contracts are not designated as hedging instruments, and are accounted for as derivatives whereby the fair value of the contracts is reported as other current assets or accrued and other current liabilities on our Condensed Consolidated Balance Sheets, and gains and losses resulting from changes in the fair value are reported in interest and other income, net, in our Condensed Consolidated Statements of Operations. The gains and losses on these foreign currency forward contracts generally offset the gains and losses associated with the underlying foreign-currency-denominated monetary assets and liabilities, which are also reported in interest and other income, net, in our Condensed Consolidated Statements of Operations. As of June 30, 2010, we had foreign currency forward contracts to purchase and sell approximately \$233 million in foreign currencies. Of this amount, \$79 million represented contracts to sell foreign currencies in exchange for U.S. dollars, \$148 million to purchase foreign currencies in exchange for U.S. dollars and \$6 million to sell foreign currency in exchange for British pounds sterling. As of March 31, 2010, we had foreign currency forward contracts to purchase and sell approximately \$431 million in foreign currencies. Of this amount, \$293 million represented contracts to sell foreign currencies in exchange for U.S. dollars, \$127 million to purchase foreign currency in exchange for U.S. dollars and \$11 million to sell foreign currency in exchange for British pounds sterling. The fair value of our foreign currency forward contracts was immaterial as of June 30, 2010 and March 31, 2010.

The effect of foreign currency forward contracts not designated as hedging instruments on our Condensed Consolidated Statements of Operations for the three months ended June 30, 2010 and 2009 was immaterial.

Table of Contents**(5) GOODWILL AND ACQUISITION-RELATED INTANGIBLES, NET**

The changes in the carrying amount of goodwill are as follows (in millions):

	Label Segment	Other Segments	Total
As of March 31, 2010			
Goodwill	\$ 672	\$ 789	\$ 1,461
Accumulated Impairment		(368)	(368)
	672	421	1,093
Effects of Foreign Currency Translation	(2)	(1)	(3)
As of June 30, 2010			
Goodwill	670	788	1,458
Accumulated Impairment		(368)	(368)
	\$ 670	\$ 420	\$ 1,090

Acquisition-related intangibles consisted of the following (in millions):

	As of June 30, 2010			As of March 31, 2010		
	Gross Carrying Amount	Accumulated Amortization	Acquisition-Related Intangibles, Net	Gross Carrying Amount	Accumulated Amortization	Acquisition-Related Intangibles, Net
Developed and Core Technology	\$ 257	\$ (161)	\$ 96	\$ 258	\$ (155)	\$ 103
Trade Names and Trademarks	89	(61)	28	89	(57)	32
Carrier Contracts and Related	85	(58)	27	85	(56)	29
Registered User Base and Other Intangibles	79	(45)	34	79	(39)	40
Total	\$ 510	\$ (325)	\$ 185	\$ 511	\$ (307)	\$ 204

Amortization of intangibles for the three months ended June 30, 2010 and 2009 was \$18 million (of which \$3 million was recognized in cost of goods sold) and \$15 million (of which \$3 million was recognized in cost of goods sold), respectively. Finite-lived intangible assets are amortized using the straight-line method over the lesser of their estimated useful lives or the terms of the related agreement, typically from two to fourteen years. As of June 30, 2010 and March 31, 2010, the weighted-average remaining useful life for finite-lived intangible assets was approximately 5.1 years for each period.

As of June 30, 2010, future amortization of finite-lived intangibles that will be recorded in cost of goods sold and operating expenses is estimated as follows (in millions):

Fiscal Year Ending March 31,	
2011 (remaining nine months)	\$ 49
2012	48
2013	25
2014	17
2015	14
Thereafter	32

Total	\$ 185
-------	--------

Table of Contents**(6) RESTRUCTURING CHARGES**

Restructuring information as of June 30, 2010 was as follows (in millions):

	Fiscal 2010 Restructuring			Fiscal 2009 Restructuring			Fiscal 2008 Reorganization Restructurings			
	Workforce	Facilities-related	Other	Workforce	Facilities-related	Facilities-related	Other	Facilities-related	Total	
Balances as of March 31, 2009	\$	\$	\$	\$	\$	\$	\$	\$	\$	\$
Charges to operations	62	22	32	1	13	3	7	7	23	140
Charges settled in cash	(29)	(2)	(1)	(9)	(11)		(10)		(62)	(62)
Charges settled in non-cash	(25)	(9)	(24)		(4)	(3)			(65)	(65)
Accrual reclassification								(7)	(7)	(7)
Balances as of March 31, 2010	8	11	7		3				29	29
Charges to operations		1	1						2	2
Charges settled in cash	(7)	(2)	(1)						(10)	(10)
Balances as of June 30, 2010	\$ 1	\$ 10	\$ 7	\$	\$ 3	\$	\$	\$	\$ 21	\$ 21

Fiscal 2010 Restructuring

In fiscal year 2010, we announced details of a restructuring plan to narrow our product portfolio to provide greater focus on titles with higher margin opportunities. Under this plan, we reduced our workforce by approximately 1,100 employees and have (1) consolidated or closed various facilities, (2) eliminated certain titles, and (3) incurred IT and other costs to assist in reorganizing certain activities. The majority of these actions were completed by March 31, 2010.

Since the inception of the fiscal 2010 restructuring plan through June 30, 2010, we have incurred charges of \$118 million, consisting of (1) \$62 million in employee-related expenses, (2) \$33 million related to intangible asset impairment costs, abandoned rights to intellectual property, and other costs to assist in the reorganization of our business support functions, and (3) \$23 million related to the closure of certain of our facilities. The \$18 million restructuring accrual as of June 30, 2010 related to the fiscal 2010 restructuring is expected to be settled by September 2013. During the remainder of fiscal year 2011, we anticipate incurring between \$10 million and \$15 million of restructuring charges related to the fiscal 2010 restructuring.

Overall, including charges incurred through June 30, 2010, we expect to incur total cash and non-cash charges between \$135 million and \$140 million by March 31, 2012. These charges consist primarily of (1) employee-related costs (approximately \$65 million), (2) intangible asset impairment costs, abandoned rights to intellectual property costs, and other costs to assist in the reorganization of our business support functions (approximately \$50 million), and (3) facilities exit costs (approximately \$25 million).

Fiscal 2009 Restructuring

In fiscal year 2009, we announced details of a cost reduction plan as a result of our performance combined with the economic environment. This plan included a narrowing of our product portfolio, a reduction in our worldwide workforce of approximately 11 percent, or 1,100 employees, the closure of 10 facilities, and reductions in other variable costs and capital expenditures.

Since the inception of the fiscal 2009 restructuring plan through June 30, 2010, we have incurred charges of \$55 million, consisting of (1) \$33 million in employee-related expenses, (2) \$20 million related to the closure of certain of our facilities, and (3) \$2 million related to asset impairments. We do not expect to incur any additional restructuring charges under this plan. The restructuring accrual of \$3 million as of June 30, 2010 related to the fiscal 2009 restructuring is expected to be settled by September 2016.

Fiscal 2008 Reorganization

In June 2007, we announced a plan to reorganize our business into several new divisions including, at the time four new Labels: EA SPORTS, EA Games, EA Casual Entertainment and The Sims in order to streamline decision-making, improve global focus, and speed new ideas to market. In October 2007, our Board of Directors approved a plan of reorganization (fiscal 2008 reorganization plan) in connection with the

Edgar Filing: ELECTRONIC ARTS INC. - Form 10-Q

reorganization of our business into four new Labels. During fiscal year 2009, we consolidated and reorganized two of our Labels. As a result, we now have three Labels, EA SPORTS, EA Games and EA Play, as well as a new organization, EA Interactive, which reports into our Global Publishing Organization. Each Label, as well as EA Interactive, operates with dedicated studio and product marketing teams focused on consumer-driven priorities.

Table of Contents

Since the inception of the fiscal 2008 reorganization plan through June 30, 2010, we have incurred charges of \$141 million, consisting of (1) \$12 million in employee-related expenses, (2) \$83 million related to the closure of our Chertsey, England and Chicago, Illinois facilities, which included asset impairment and lease termination costs, and (3) \$46 million related to other costs including other contract terminations, as well as IT and consulting costs to assist in the reorganization of our business support functions. We do not expect to incur any additional charges under this plan.

Other Restructurings

We also engaged in various other restructurings based on management decisions. The \$7 million restructuring accrual as of March 31, 2009 was reclassified during the three months ended June 30, 2009, from accrued and other current liabilities to other liabilities on our Condensed Consolidated Balance Sheet.

(7) ROYALTIES AND LICENSES

Our royalty expenses consist of payments to (1) content licensors, (2) independent software developers, and (3) co-publishing and distribution affiliates. License royalties consist of payments made to celebrities, professional sports organizations, movie studios and other organizations for our use of their trademarks, copyrights, personal publicity rights, content and/or other intellectual property. Royalty payments to independent software developers are payments for the development of intellectual property related to our games. Co-publishing and distribution royalties are payments made to third parties for the delivery of products.

Royalty-based obligations with content licensors and distribution affiliates are either paid in advance and capitalized as prepaid royalties or are accrued as incurred and subsequently paid. These royalty-based obligations are generally expensed to cost of goods sold generally at the greater of the contractual rate or an effective royalty rate based on the total projected net revenue. Prepayments made to thinly capitalized independent software developers and co-publishing affiliates are generally made in connection with the development of a particular product and, therefore, we are generally subject to development risk prior to the release of the product. Accordingly, payments that are due prior to completion of a product are generally expensed to research and development over the development period as the services are incurred. Payments due after completion of the product (primarily royalty-based in nature) are generally expensed as cost of goods sold.

Our contracts with some licensors include minimum guaranteed royalty payments, which are initially recorded as an asset and as a liability at the contractual amount when no performance remains with the licensor. When performance remains with the licensor, we record guarantee payments as an asset when actually paid and as a liability when incurred, rather than recording the asset and liability upon execution of the contract. Royalty liabilities are classified as current liabilities to the extent such royalty payments are contractually due within the next twelve months. As of June 30, 2010 and March 31, 2010, approximately \$7 million and \$13 million, respectively, of minimum guaranteed royalty obligations had been recognized and are included in the royalty-related assets and liabilities tables below.

Each quarter, we also evaluate the expected future realization of our royalty-based assets, as well as any unrecognized minimum commitments not yet paid to determine amounts we deem unlikely to be realized through product sales. Any impairments or losses determined before the launch of a product are charged to research and development expense. Impairments or losses determined post-launch are charged to cost of goods sold. We evaluate long-lived royalty-based assets for impairment using undiscounted cash flows when impairment indicators exist. Unrecognized minimum royalty-based commitments are accounted for as executory contracts and, therefore, any losses on these commitments are recognized when the underlying intellectual property is abandoned (*i.e.*, cease use) or the contractual rights to use the intellectual property are terminated. During the three months ended June 30, 2010 and 2009, we recognized losses of \$10 million and impairment charges of \$1 million, respectively.

The current and long-term portions of prepaid royalties and minimum guaranteed royalty-related assets, included in other current assets and other assets, consisted of (in millions):

	As of June 30, 2010	As of March 31, 2010
Other current assets	\$ 99	\$ 66
Other assets	42	36
Royalty-related assets	\$ 141	\$ 102

Table of Contents

At any given time, depending on the timing of our payments to our co-publishing and/or distribution affiliates, content licensors and/or independent software developers, we recognize unpaid royalty amounts owed to these parties as accrued liabilities. As of June 30, 2010 and March 31, 2010, the current portion of accrued royalties, included in accrued and other current liabilities was \$151 million and \$144 million, respectively. There were no long-term accrued royalty liabilities as of June 30, 2010 and March 31, 2010.

In addition, as of June 30, 2010, we were committed to pay approximately \$1,327 million to content licensors, independent software developers and co-publishing and/or distribution affiliates, but performance remained with the counterparty (*i.e.*, delivery of the product or content or other factors) and such commitments were therefore not recorded in our Condensed Consolidated Financial Statements.

(8) BALANCE SHEET DETAILS***Inventories***

Inventories as of June 30, 2010 and March 31, 2010 consisted of (in millions):

	As of June 30, 2010	As of March 31, 2010
Raw materials and work in process	\$ 6	\$ 8
In-transit inventory	1	2
Finished goods	75	90
Inventories	\$ 82	\$ 100

Property and Equipment, Net

Property and equipment, net, as of June 30, 2010 and March 31, 2010 consisted of (in millions):

	As of June 30, 2010	As of March 31, 2010
Computer equipment and software	\$ 475	\$ 480
Buildings	340	347
Leasehold improvements	98	99
Office equipment, furniture and fixtures	66	71
Land	64	65
Warehouse equipment and other	10	10
Construction in progress	10	13
	1,063	1,085
Less accumulated depreciation	(547)	(548)
Property and equipment, net	\$ 516	\$ 537

Depreciation expense associated with property and equipment amounted to \$28 million and \$32 million for the three months ended June 30, 2010 and 2009, respectively.

Acquisition-Related Restricted Cash Included in Other Current Assets and Other Assets

Edgar Filing: ELECTRONIC ARTS INC. - Form 10-Q

In connection with our acquisition of Playfish in fiscal year 2010, we deposited \$100 million into an escrow account to pay the former shareholders of Playfish in the event certain performance milestones through December 31, 2011 are achieved. Through the three months ended June 30, 2010, no distributions were made from the restricted cash amount. As this deposit is restricted in nature, as of June 30, 2010 and March 31, 2010, the estimated long-term portion of \$61 million in each period is included in other assets and the estimated short-term portion of \$39 million in each period is included in other current assets on our Condensed Consolidated Balance Sheets.

Table of Contents***Accrued and Other Current Liabilities***

Accrued and other current liabilities as of June 30, 2010 and March 31, 2010 consisted of (in millions):

	As of June 30, 2010	As of March 31, 2010
Other accrued expenses	\$ 244	\$ 293
Accrued royalties	151	144
Accrued compensation and benefits	122	177
Deferred net revenue (other)	103	103
Accrued and other current liabilities	\$ 620	\$ 717

Deferred net revenue (other) includes the deferral of subscription revenue, deferrals related to our Switzerland distribution business, advertising revenue, licensing arrangements, and other revenue for which revenue recognition criteria has not been met.

Deferred Net Revenue (Packaged Goods and Digital Content)

Deferred net revenue (packaged goods and digital content) was \$490 million as of June 30, 2010 and \$766 million as of March 31, 2010. Deferred net revenue (packaged goods and digital content) includes the unrecognized revenue from (1) bundled sales of certain online-enabled packaged goods and digital content for which either we do not have vendor-specific objective evidence of fair value (VSOE) for the online service that we provide in connection with the sale of the software or we have an obligation to provide future incremental unspecified digital content, (2) certain packaged goods sales of massively-multiplayer online role-playing games, and (3) sales of certain incremental content associated with our core subscription services that can only be played online, which are types of micro-transactions. We recognize revenue from sales of online-enabled packaged goods and digital content for which (1) we do not have VSOE for the online service that we provided in connection with the sale and (2) we have an obligation to deliver incremental unspecified digital content in the future without an additional fee on a straight-line basis generally over an estimated six month period beginning in the month after shipment. However, we expense the cost of goods sold related to these transactions during the period in which the product is delivered (rather than on a deferred basis).

(9) INCOME TAXES

We estimate our annual effective tax rate at the end of each quarterly period, and we record the tax effect of certain discrete items, which are unusual or occur infrequently, in the interim period in which they occur, including changes in judgment about deferred tax valuation allowances. In addition, jurisdictions with a projected loss for the year or a year-to-date loss where no tax benefit can be recognized are excluded from the estimated annual effective tax rate. The impact of such an exclusion could result in a higher or lower effective tax rate during a particular quarter depending on the mix and timing of actual earnings versus annual projections.

We recognize deferred tax assets and liabilities for both the expected impact of differences between the financial statement amount and the tax basis of assets and liabilities and for the expected future tax benefit to be derived from tax losses and tax credit carry forwards. We record a valuation allowance against deferred tax assets when it is considered more likely than not that all or a portion of our deferred tax assets will not be realized. In making this determination, we are required to give significant weight to evidence that can be objectively verified. It is generally difficult to conclude that a valuation allowance is not needed when there is significant negative evidence, such as cumulative losses in recent years. Forecasts of future taxable income are considered to be less objective than past results, particularly in light of the economic environment. Therefore, cumulative losses weigh heavily in the overall assessment. Based on the assumptions and requirements noted above, we have recorded a valuation allowance against most of our U.S. deferred tax assets. In addition, we expect to provide a valuation allowance on future U.S. tax benefits until we can sustain a level of profitability or until other significant positive evidence arises that suggest that these benefits are more likely than not to be realized.

The tax benefit reported for the three months ended June 30, 2010 is based on our projected annual effective tax rate for fiscal year 2011, and also includes certain discrete tax benefits recorded during the period. Our effective tax rates for the three months ended June 30, 2010 and 2009 were a tax benefit of 3.4 percent and 9.0 percent, respectively. The effective tax rate for the three months ended June 30, 2010 differs from the statutory rate of 35.0 percent primarily due to U.S. losses for which no benefit is

Table of Contents

recognized and non-U.S. losses with a reduced or zero tax benefit, partially offset by tax benefits related to the expiration of statutes of limitations and resolution of examinations by taxing authorities. The effective tax rate for the three months ended June 30, 2010 differs from the same period in fiscal year 2010 primarily due to greater tax benefits recorded in fiscal year 2010 related to the expiration of statutes of limitations and reductions in the valuation allowance on U.S. deferred tax assets.

On May 27, 2009, the Ninth Circuit Court of Appeals (the Court) overturned a 2005 Tax Court decision (2009 Decision) in *Xilinx Inc. v. Commissioner* (Xilinx). The Court's 2009 Decision (which was subsequently withdrawn on January 13, 2010) changed the tax treatment of share-based compensation expenses for the purpose of determining intangible development costs under an entity's research and development cost sharing arrangement. As a result of this decision, we recorded additional reserves for unrecognized tax benefits of approximately \$59 million during the three months ended June 30, 2009. These reserves related primarily to windfall tax benefits recognized for stock-based compensation, and were therefore recorded as reductions in paid-in capital. A portion of the additional reserves for unrecognized tax benefits recorded as a result of the 2009 decision were included as a source of taxable income in determining the valuation allowance we recorded at June 30, 2009. As a result, we recorded a tax benefit of approximately \$11 million in the three months ended June 30, 2009 for the corresponding reduction in the valuation allowance.

During the three months ended June 30, 2009, we recorded approximately \$21 million of previously unrecognized tax benefits and reduced our accrual for interest and penalties by approximately \$12 million due to the expiration of statutes of limitation in the United Kingdom.

During the three months ended June 30, 2010, we recorded a net decrease of \$9 million in gross unrecognized tax benefits. The total gross unrecognized tax benefits as of June 30, 2010 is \$269 million, of which approximately \$35 million would be offset by prior cash deposits to tax authorities for issues pending resolution. A portion of our unrecognized tax benefits will affect our effective tax rate if they are recognized upon favorable resolution of the uncertain tax positions. As of June 30, 2010, if recognized, approximately \$120 million of the unrecognized tax benefits would affect our effective tax rate and approximately \$133 million would result in adjustments to deferred tax assets with corresponding adjustments to the valuation allowance.

During the three months ended June 30, 2010, we recorded a net decrease in tax of \$2 million for accrued interest and penalties related to tax positions taken on our tax returns. As of June 30, 2010 the combined amount of accrued interest and penalties related to uncertain tax positions included in income tax obligations on our Condensed Consolidated Balance Sheet was approximately \$37 million.

The IRS has completed its examination of our federal income tax returns through fiscal year 2005. As of June 30, 2010, the IRS had proposed, and we had agreed to, certain adjustments to our tax returns for fiscal years 2000 through 2005. The effects of these adjustments have been considered in estimating our future obligations for unrecognized tax benefits and are not expected to have a material impact on our financial position or results of operations. As of June 30, 2010, we had not agreed to certain other proposed adjustments for fiscal years 2000 through 2005, and those issues were pending resolution with the IRS. Furthermore, the IRS has commenced an examination of our fiscal year 2006, 2007 and 2008 tax returns. We are also currently under income tax examination in Canada for fiscal years 2004 and 2005, and in France for fiscal years 2006 through 2008. We remain subject to income tax examination for several other jurisdictions including Canada for fiscal years after 2001, in France for fiscal years after 2008, in Germany for fiscal years after 2007, in the United Kingdom for fiscal years after 2008, and in Switzerland for fiscal years after 2007.

The timing of the resolution of income tax examinations is highly uncertain, and the amounts ultimately paid, if any, upon resolution of the issues raised by the taxing authorities may differ materially from the amounts accrued for each year. Although potential resolution of uncertain tax positions involve multiple tax periods and jurisdictions, it is reasonably possible that a reduction of up to \$70 million of the reserves for unrecognized tax benefits may occur within the next 12 months, some of which, depending on the nature of the settlement or expiration of statutes of limitations, may affect our income tax provision (benefit) and therefore benefit the resulting effective tax rate. The actual amount could vary significantly depending on the ultimate timing and nature of any settlements.

Table of Contents**(10) COMMITMENTS AND CONTINGENCIES*****Lease Commitments***

As of June 30, 2010, we leased certain of our current facilities, furniture and equipment under non-cancelable operating lease agreements. We were required to pay property taxes, insurance and normal maintenance costs for certain of these facilities and any increases over the base year of these expenses on the remainder of our facilities.

Development, Celebrity, League and Content Licenses: Payments and Commitments

The products we produce in our studios are designed and created by our employee designers, artists, software programmers and by non-employee software developers (independent artists or third-party developers). We typically advance development funds to the independent artists and third-party developers during development of our games, usually in installment payments made upon the completion of specified development milestones. Contractually, these payments are generally considered advances against subsequent royalties on the sales of the products. These terms are set forth in written agreements entered into with the independent artists and third-party developers.

In addition, we have certain celebrity, league and content license contracts that contain minimum guarantee payments and marketing commitments that may not be dependent on any deliverables. Celebrities and organizations with whom we have contracts include: FIFA, FIFPRO Foundation, FAPL (Football Association Premier League Limited), and DFL Deutsche Fußball Liga GmbH (German Soccer League) (professional soccer); National Basketball Association (professional basketball); PGA TOUR and Tiger Woods (professional golf); National Hockey League and NHL Players Association (professional hockey); Warner Bros. (Harry Potter); National Football League Properties, PLAYERS Inc., and Red Bear Inc. (professional football); Collegiate Licensing Company (collegiate football and basketball); ESPN (content in EA SPORTS games); Hasbro, Inc. (most of Hasbro's toy and game intellectual properties); and the Estate of Robert Ludlum (Robert Ludlum novels and films). These developer and content license commitments represent the sum of (1) the cash payments due under non-royalty-bearing licenses and services agreements and (2) the minimum guaranteed payments and advances against royalties due under royalty-bearing licenses and services agreements, the majority of which are conditional upon performance by the counterparty. These minimum guarantee payments and any related marketing commitments are included in the table below.

The following table summarizes our minimum contractual obligations as of June 30, 2010 (in millions):

Fiscal Year Ending March 31,	Contractual Obligations				Total
	Leases (a)	Developer/ Licensor Commitments (b)	Marketing	Other Purchase Obligations	
2011 (remaining nine months)	\$ 37	\$ 189	\$ 74	\$ 2	\$ 302
2012	39	280	51		370
2013	32	196	53		281
2014	23	29	41		93
2015	18	28	15		61
Thereafter	21	612	92		725
Total	\$ 170	\$ 1,334	\$ 326	\$ 2	\$ 1,832

(a) Lease commitments have not been reduced by minimum sub-lease rentals for unutilized office space resulting from our reorganization activities of approximately \$13 million due in the future under non-cancelable sub-leases.

(b) Developer/licensor commitments include \$7 million of commitments that have been recorded in current and long-term liabilities and a corresponding amount in current and long-term assets in our Condensed Consolidated Balance Sheet as of June 30, 2010 because payment is not contingent upon performance by the developer or licensor.

Edgar Filing: ELECTRONIC ARTS INC. - Form 10-Q

The amounts represented in the table above reflect our minimum cash obligations for the respective fiscal years, but do not necessarily represent the periods in which they will be expensed in our Condensed Consolidated Financial Statements.

In addition to what is included in the table above as of June 30, 2010, we had a liability for unrecognized tax benefits and an accrual for the payment of related interest totaling \$264 million, of which approximately \$35 million is offset by prior cash deposits to tax authorities for issues pending resolution. For the remaining liability, we are unable to make a reasonably reliable estimate of when cash settlement with a taxing authority will occur.

Table of Contents

In addition to what is included in the table above as of June 30, 2010, in connection with our acquisition of Playfish in fiscal year 2010, we may be required to pay additional variable cash consideration that is contingent upon the achievement of certain performance milestones through December 31, 2011. The additional consideration is limited to a maximum of \$100 million.

Legal Proceedings

We are subject to claims and litigation arising in the ordinary course of business. We do not believe that any liability from any reasonably foreseeable disposition of such claims and litigation, individually or in the aggregate, would have a material adverse effect on our Condensed Consolidated Financial Statements.

(11) STOCK-BASED COMPENSATION***Valuation Assumptions***

We are required to estimate the fair value of share-based payment awards on the date of grant. We recognize compensation costs for stock-based payment transactions to employees based on their grant-date fair value on a straight-line approach over the service period for which such awards are expected to vest. The fair value of restricted stock units and restricted stock is determined based on the quoted market price of our common stock on the date of grant. The fair value of stock options and stock purchase rights granted pursuant to our equity incentive plans and our 2000 Employee Stock Purchase Plan (ESPP), respectively, is determined using the Black-Scholes valuation model. The fair value of our stock options is based on the multiple-award valuation method. The determination of fair value is affected by our stock price, as well as assumptions regarding subjective and complex variables such as expected employee exercise behavior and our expected stock price volatility over the expected term of the award. Generally, our assumptions are based on historical information and judgment is required to determine if historical trends may be indicators of future outcomes. The key assumptions for the Black-Scholes valuation calculation are:

Risk-free interest rate. The risk-free interest rate is based on U.S. Treasury yields in effect at the time of grant for the expected term of the option.

Expected volatility. We use a combination of historical stock price volatility and implied volatility computed based on the price of options publicly traded on our common stock for our expected volatility assumption.

Expected term. The expected term represents the weighted-average period the stock options are expected to remain outstanding. The expected term is determined based on historical exercise behavior, post-vesting termination patterns, options outstanding and future expected exercise behavior.

Expected dividends.

The estimated assumptions used in the Black-Scholes valuation model to value our stock option grants were as follows:

	Three Months Ended June 30,	
	2010	2009
Risk-free interest rate	1.2 - 2.4%	1.8 - 3.0%
Expected volatility	41 - 44%	43 - 48%
Weighted-average volatility	43%	46%
Expected term	4.4 years	4.1 years
Expected dividends	None	None

There were no ESPP shares valued or issued during the three months ended June 30, 2010 and 2009.

Stock-Based Compensation Expense

Edgar Filing: ELECTRONIC ARTS INC. - Form 10-Q

Employee stock-based compensation expense recognized during the three months ended June 30, 2010 and 2009 was calculated based on awards ultimately expected to vest and has been reduced for estimated forfeitures. In subsequent periods, if actual forfeitures differ from those estimates, an adjustment to stock-based compensation expense will be recognized at that time.

Table of Contents

The following table summarizes stock-based compensation expense resulting from stock options, restricted stock, restricted stock units and our ESPP included in our Condensed Consolidated Statements of Operations (in millions):

	Three Months Ended June 30,	
	2010	2009
Cost of goods sold	\$ 1	\$ 1
Marketing and sales	4	3
General and administrative	12	5
Research and development	30	24
Stock-based compensation expense, net of tax	\$ 47	\$ 33

During the three months ended June 30, 2010 and 2009, we did not recognize any provision for or benefit from income taxes related to our stock-based compensation expense.

As of June 30, 2010, our total unrecognized compensation cost related to stock options was \$63 million and is expected to be recognized over a weighted-average service period of 2.1 years. As of June 30, 2010, our total unrecognized compensation cost related to restricted stock, restricted stock units and notes payable in shares of common stock (collectively referred to as restricted stock rights) was \$355 million (inclusive of approximately \$38 million of additional remaining compensation cost associated with our Employee Stock Option Exchange Program in fiscal year 2010) and is expected to be recognized over a weighted-average service period of 1.9 years. Of the \$355 million of unrecognized compensation cost above, \$24 million relates to performance-based restricted stock units that we ceased recognizing stock-based compensation expense during fiscal year 2010 because we determined that they were neither probable nor improbable of achievement.

Stock Options

The following table summarizes our stock option activity for the three months ended June 30, 2010:

	Options (in thousands)	Weighted- Average Exercise Price	Weighted- Average Remaining Contractual Term (in years)	Aggregate Intrinsic Value (in millions)
Outstanding as of March 31, 2010	16,131	\$ 30.28		
Granted	67	17.66		
Exercised	(64)	16.49		
Forfeited, cancelled or expired	(972)	33.07		
Outstanding as of June 30, 2010	15,162	30.10	5.8	\$
Exercisable as of June 30, 2010	9,114	35.47	4.0	\$

The aggregate intrinsic value represents the total pre-tax intrinsic value based on our closing stock price as of June 30, 2010, which would have been received by the option holders had all the option holders exercised their options as of that date. The weighted-average grant date fair values of stock options granted during the three months ended June 30, 2010 and 2009 were \$6.46 and \$8.02, respectively. We issue new common stock from our authorized shares upon the exercise of stock options.

Table of Contents***Restricted Stock Rights***

The following table summarizes our restricted stock rights activity, excluding performance-based restricted stock unit activity discussed below, for the three months ended June 30, 2010:

	Restricted Stock Rights (in thousands)	Weighted- Average Grant Date Fair Value
Balance as of March 31, 2010	14,300	\$ 24.45
Granted	5,399	17.65
Vested	(973)	16.54
Forfeited or cancelled	(360)	17.07
Balance as of June 30, 2010	18,366	23.01

The weighted-average grant date fair value of restricted stock rights is based on the quoted market price of our common stock on the date of grant. The weighted-average grant date fair values of restricted stock rights granted during the three months ended June 30, 2010 and 2009 were \$17.65 and \$20.76, respectively.

Performance-Based Restricted Stock Units

The weighted-average grant date fair value of performance-based restricted stock units is based on the quoted market price of our common stock on the date of grant. There was no performance-based restricted stock unit activity during the three months ended June 30, 2010. The weighted-average grant date fair value of performance-based restricted stock units granted during the three months ended June 30, 2009 was \$21.04.

Annual Meeting of Stockholders

At our Annual Meeting of Stockholders, held on August 5, 2010, our stockholders approved amendments to our 2000 Equity Incentive Plan (the Equity Plan) to (1) increase the number of shares authorized for issuance under the Equity Plan by 5.3 million shares and (2) remove the provision that provides for automatic grants to our non-employee directors upon appointment to our Board of Directors and annually upon re-election. Our stockholders also approved an amendment to the ESPP to increase the number of shares authorized under the ESPP by 2 million shares.

(12) COMPREHENSIVE LOSS

We classify items of other comprehensive income (loss) by their nature in a financial statement and display the accumulated balance of other comprehensive income separately from retained earnings and paid-in capital in the equity section of our balance sheets. Accumulated other comprehensive income primarily includes foreign currency translation adjustments, and the net of tax amounts for unrealized gains (losses) on investments and unrealized gains (losses) on derivative instruments designated as cash flow hedges. Foreign currency translation adjustments are not adjusted for income taxes as they relate to indefinite investments in non-U.S. subsidiaries.

The change in the components of comprehensive loss, net of related immaterial taxes, for the three months ended June 30, 2010 and 2009 is summarized as follows (in millions):

	Three Months Ended June 30,	
	2010	2009
Net income (loss)	\$ 96	\$ (234)

Other comprehensive income (loss):

Edgar Filing: ELECTRONIC ARTS INC. - Form 10-Q

Change in unrealized gains (losses) on investments	(89)	77
Reclassification adjustment for losses realized on investments	5	15
Change in unrealized losses on derivative instruments	(1)	(2)
Reclassification adjustment for losses (gains) realized on derivative instruments	1	(2)
Foreign currency translation adjustments	(31)	37
Total other comprehensive income (loss)	(115)	125
Total comprehensive loss	\$ (19)	\$ (109)

Table of Contents**(13) NET INCOME (LOSS) PER SHARE**

The following table summarizes the computations of basic earnings per share (Basic EPS) and diluted earnings per share (Diluted EPS). Basic EPS is computed as net income (loss) divided by the weighted-average number of common shares outstanding for the period. Diluted EPS reflects the potential dilution that could occur from common shares issuable through stock-based compensation plans including stock options, restricted stock, restricted stock units, common stock through our ESPP, warrants and other convertible securities using the treasury stock method.

(In millions, except per share data)	Three Months Ended June 30,	
	2010	2009
Net income (loss)	\$ 96	\$ (234)
Shares used to compute net income (loss) per share:		
Weighted-average common stock outstanding - basic	328	323
Dilutive potential common shares	4	
Weighted-average common stock outstanding - diluted	332	323
Net income (loss) per share:		
Basic	\$ 0.29	\$ (0.72)
Diluted	\$ 0.29	\$ (0.72)

As a result of our net loss for the three months ended June 30, 2009, we have excluded certain equity-based instruments from the diluted loss per share calculation as their inclusion would have had an antidilutive effect. Had we reported net income for the period, an additional 1 million shares of common stock would have been included in the number of shares used to calculate diluted earnings per share for the three months ended June 30, 2009.

Options to purchase and restricted stock units and restricted stock to be released in the amount of 20 million shares and 38 million shares of common stock were excluded from the computation of diluted shares for the three months ended June 30, 2010 and 2009, respectively, as their inclusion would have had an antidilutive effect. For the three months ended June 30, 2010 and 2009, the weighted-average exercise prices of these shares were \$23.01 and \$36.89 per share, respectively.

(14) SEGMENT INFORMATION

Our reporting segments are based upon: our internal organizational structure; the manner in which our operations are managed; the criteria used by our Chief Executive Officer, our Chief Operating Decision Maker (CODM), to evaluate segment performance; the availability of separate financial information; and overall materiality considerations.

Our business is currently organized around three operating labels, EA Games, EA SPORTS and EA Play, as well as EA Interactive, which reports into our Publishing Organization. Our CODM regularly receives separate financial information for distinct businesses within the EA Interactive organization, including EA Mobile, Pogo and Playfish. Accordingly, in assessing performance and allocating resources, our CODM reviews the results of our three Labels, as well as the operating segments in EA Interactive, including EA Mobile, Pogo and Playfish. Due to their similar economic characteristics, products, and distribution methods, EA Games, EA SPORTS, and EA Play's results are aggregated into one Reportable Segment (the Label segment) as shown below. The remaining operating segments' results are not material for separate disclosure and are included in the reconciliation of Label segment profit to our consolidated operating income (loss) below. In addition to assessing performance and allocating resources based on our operating segments as described herein, to a lesser degree, our CODM also reviews results based on geographic performance.

Table of Contents

The following table summarizes the financial performance of the Label segment and a reconciliation of the Label segment's profit to our consolidated operating income (loss) for the three months ended June 30, 2010 and 2009 (in millions):

	Three Months Ended June 30,	
	2010	2009
Label segment:		
Net revenue before revenue deferral	\$ 430	\$ 739
Depreciation and amortization	(11)	(15)
Other expenses	(416)	(637)
Label segment profit	3	87
Reconciliation to consolidated operating income (loss):		
Other:		
Revenue deferral	(318)	(384)
Recognition of revenue deferral	594	212
Other net revenue	109	77
Depreciation and amortization	(35)	(32)
Other expenses	(255)	(205)
Consolidated operating income (loss)	\$ 98	\$ (245)

Label segment profit differs from our consolidated operating income (loss) primarily due to the exclusion of (1) certain corporate and other functional costs that are not allocated to the Labels, (2) the deferral of certain net revenue related to online-enabled packaged goods and digital content (see Note 8 of the Notes to Condensed Consolidated Financial Statements), and (3) the results of EA Mobile, Pogo, Playfish, and our Switzerland distribution revenue that has not been allocated to the Labels. Our CODM reviews assets on a consolidated basis and not on a segment basis.

Information about our total net revenue by platform for the three months ended June 30, 2010 and 2009 is presented below (in millions):

	Three Months Ended June 30,	
	2010	2009
Consoles		
Xbox 360	\$ 262	\$ 73
PLAYSTATION 3	209	121
Wii	40	161
PlayStation 2	11	27
Total Consoles	522	382
PC	186	124
Wireless Platforms		
Mobile	52	50
PSP	19	38
Nintendo DS	11	28
Total Wireless	82	116
Other	25	22

Total Net Revenue

\$ 815 \$ 644

Table of Contents

Information about our operations in North America, Europe and Asia as of and for the three months ended June 30, 2010 and 2009 is presented below (in millions):

	Three Months Ended June 30,	
	2010	2009
<u>Net revenue from unaffiliated customers</u>		
North America	\$ 451	\$ 343
Europe	317	258
Asia	47	43
Total	\$ 815	\$ 644

	As of June 30,	
	2010	2009
<u>Long-lived assets</u>		
North America	\$ 1,325	\$ 1,150
Europe	432	169
Asia	34	44
Total	\$ 1,791	\$ 1,363

Our direct sales to GameStop Corp. and Wal-Mart Stores, Inc. represented approximately 14 percent and 11 percent of total net revenue for the three months ended June 30, 2010, respectively, and approximately 13 percent and 12 percent of total net revenue for the three months ended June 30, 2009, respectively.

(15) COLLABORATIVE ARRANGEMENTS

FASB ASC 808 defines collaborative arrangements and establishes reporting requirements for transactions between participants in a collaborative arrangement and between participants in the arrangement and third parties. FASB ASC 808 did not have a significant impact on our Condensed Consolidated Financial Statements for the three months ended June 30, 2010 and 2009.

(16) IMPACT OF RECENTLY ISSUED ACCOUNTING STANDARDS

In October 2009, the FASB issued Accounting Standards Update (ASU) 2009-13, *Revenue Recognition (Topic 605) Multiple-Deliverable Revenue Arrangements*. This guidance modifies the fair value requirements of FASB ASC subtopic 605-25, *Revenue Recognition-Multiple Element Arrangements*, by allowing the use of the best estimate of selling price in addition to vendor specific objective evidence and third-party evidence for determining the selling price of a deliverable. This guidance establishes a selling price hierarchy for determining the selling price of a deliverable, which is based on: (a) vendor-specific objective evidence, (b) third-party evidence, or (c) estimates. In addition, the residual method of allocating arrangement consideration is no longer permitted. ASU 2009-13 is effective for fiscal years beginning on or after June 15, 2010. We do not expect the adoption of ASU 2009-13 to have a material impact on our Condensed Consolidated Financial Statements.

In October 2009, the FASB issued ASU 2009-14, *Software (Topic 985) Certain Revenue Arrangements that Include Software Elements*. This guidance modifies the scope of FASB ASC subtopic 965-605, *Software-Revenue Recognition*, to exclude from its requirements non-software components of tangible products and software components of tangible products that are sold, licensed, or leased with tangible products when the software components and non-software components of the tangible product function together to deliver the tangible product's essential functionality. ASU 2009-14 is effective for fiscal years beginning on or after June 15, 2010. We do not expect the adoption of ASU 2009-14 to have a material impact on our Condensed Consolidated Financial Statements.

Table of Contents

REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM

The Board of Directors and Shareholders

Electronic Arts Inc.:

We have reviewed the condensed consolidated balance sheet of Electronic Arts Inc. and subsidiaries (the Company) as of July 3, 2010, the related condensed consolidated statements of operations and cash flows for the three-month periods ended July 3, 2010 and July 4, 2009. These condensed consolidated financial statements are the responsibility of the Company's management.

We conducted our reviews in accordance with the standards of the Public Company Accounting Oversight Board (United States). A review of interim financial information consists principally of applying analytical procedures and making inquiries of persons responsible for financial and accounting matters. It is substantially less in scope than an audit conducted in accordance with the standards of the Public Company Accounting Oversight Board (United States), the objective of which is the expression of an opinion regarding the financial statements taken as a whole. Accordingly, we do not express such an opinion.

Based on our reviews, we are not aware of any material modifications that should be made to the condensed consolidated financial statements referred to above for them to be in conformity with U.S. generally accepted accounting principles.

We have previously audited, in accordance with standards of the Public Company Accounting Oversight Board (United States), the consolidated balance sheet of Electronic Arts Inc. and subsidiaries as of April 3, 2010, and the related consolidated statements of operations, stockholders equity and comprehensive loss, and cash flows for the year then ended (not presented herein); and in our report dated May 28, 2010, we expressed an unqualified opinion on those consolidated financial statements. In our opinion, the information set forth in the accompanying condensed consolidated balance sheet as of April 3, 2010, is fairly stated, in all material respects, in relation to the consolidated balance sheet from which it has been derived.

/s/ KPMG LLP

Mountain View, California
August 9, 2010

Table of Contents**Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations****CAUTIONARY NOTE ABOUT FORWARD-LOOKING STATEMENTS**

This Quarterly Report contains forward-looking statements within the meaning of the Private Securities Litigation Reform Act of 1995. All statements, other than statements of historical fact, made in this Quarterly Report are forward looking. Examples of forward-looking statements include statements related to industry prospects, our future economic performance including anticipated revenues and expenditures, results of operations or financial position, and other financial items, our business plans and objectives, including our intended product releases, and may include certain assumptions that underlie the forward-looking statements. We use words such as anticipate, believe, expect, intend, estimate (and the negative of any of these terms), future and similar expressions to identify forward-looking statements. These forward-looking statements are subject to business and economic risk and reflect management's current expectations, and involve subjects that are inherently uncertain and difficult to predict. Our actual results could differ materially from those in the forward-looking statements. We will not necessarily update information if any forward-looking statement later turns out to be inaccurate. Risks and uncertainties that may affect our future results include, but are not limited to, those discussed in this report under the heading Risk Factors in Part II, Item 1A, as well as in our Annual Report on Form 10-K for the fiscal year ended March 31, 2010 as filed with the Securities and Exchange Commission (SEC) on May 28, 2010 and in other documents we have filed with the SEC.

OVERVIEW

The following overview is a top-level discussion of our operating results, as well as some of the trends and drivers that affect our business. Management believes that an understanding of these trends and drivers is important in order to understand our results for the three months ended June 30, 2010, as well as our future prospects. This summary is not intended to be exhaustive, nor is it intended to be a substitute for the detailed discussion and analysis provided elsewhere in this Form 10-Q, including in the remainder of Management's Discussion and Analysis of Financial Condition and Results of Operations, Risk Factors, and the Condensed Consolidated Financial Statements and related notes. Additional information can be found in the Business section of our Annual Report on Form 10-K for the fiscal year ended March 31, 2010 as filed with the SEC on May 28, 2010 and in other documents we have filed with the SEC.

About Electronic Arts

We develop, market, publish and distribute video game software and content that can be played by consumers on a variety of platforms, including video game consoles (such as the PLAYSTATION® 3, Microsoft Xbox 360 and Nintendo Wii), personal computers, handheld game players (such as the PlayStation® Portable (PSP) and the Nintendo DS), mobile devices (such as cellular and smart phones including the Apple iPhone) and wireless devices such as the Apple iPad™. Some of our games are based on content that we license from others (e.g., FIFA Soccer, Madden NFL Football, Harry Potter, and Hasbro's toy and game intellectual properties), and some of our games are based on our own wholly-owned intellectual property (e.g., The Sims, Need for Speed, and Dead Space). Our goal is to publish titles with global mass-market appeal, which often means translating and localizing them for sale in non-English speaking countries. In addition, we also attempt to create software game franchises that allow us to publish new titles on a recurring basis that are based on the same property. Examples of this franchise approach are the annual iterations of our sports-based products (e.g., FIFA Soccer, Madden NFL Football, and NCAA® Football), wholly-owned properties that can be successfully sequenced (e.g., The Sims, Need for Speed and Battlefield) and titles based on long-lived literary and/or movie properties (e.g., Harry Potter).

Financial Results

Total net revenue for the three months ended June 30, 2010 was \$815 million, up \$171 million as compared to the three months ended June 30, 2009. At June 30, 2010, deferred net revenue associated with sales of online-enabled packaged goods and digital content decreased by \$276 million as compared to March 31, 2010, directly increasing the amount of reported net revenue during the three months ended June 30, 2010. At June 30, 2009, deferred net revenue associated with sales of online-enabled packaged goods and digital content increased by \$172 million as compared to March 31, 2009, directly reducing the amount of reported net revenue during the three months ended June 30, 2009. Without these changes in deferred net revenue, reported net revenue decreased by approximately \$277 million during the three months ended June 30, 2010 as compared to the three months ended June 30, 2009. Net revenue for the three months ended June 30, 2010, was driven by *Battlefield: Bad Company 2*, *FIFA 10*, and *Dragon Age: Origins*.

Table of Contents

Net income for the three months ended June 30, 2010 was \$96 million as compared to a net loss of \$234 million for the three months ended June 30, 2009. Diluted earnings per share for the three months ended June 30, 2010 was \$0.29 as compared to a diluted loss per share of \$0.72 for the three months ended June 30, 2009. Net income increased during the three months ended June 30, 2010 as compared to the three months ended June 30, 2009 primarily as a result of (1) an increase of \$171 million in net revenue, (2) a \$99 million decrease in cost of goods sold, (3) a \$37 million decrease in research and development costs, and (4) a \$37 million decrease in marketing and sales expenses. These amounts were partially offset by a \$21 million decrease in our benefit from income taxes.

During the three months ended June 30, 2010, we used \$148 million of cash in operating activities as compared to using \$328 million of cash for the three months ended June 30, 2009. The decrease in cash used in operating activities for the three months ended June 30, 2010 as compared to the three months ended June 30, 2009 was primarily due to (1) a decrease in our gross accounts receivable balances as a result of an earlier release schedule and a decrease of our first quarter titles, (2) a decrease in external development and contracted services as part of our cost reduction initiatives, and (3) a decrease in marketing and advertising expenses.

Trends in Our Business

Economic Environment. Overall consumer spending has declined as a result of the national and global economic downturn. Retailers globally continue to take a conservative stance in ordering game inventory. We believe that the continued decline in the packaged goods sector contributed to the lower than anticipated demand for our products during the 2009 holiday selling season. We remain cautious about our future sales in light of the economic environment and the impact it has had on our business.

Current Generation Game Consoles. Video game hardware systems have historically had a life cycle of four to six years, which causes the video game software market to be cyclical as well. The current cycle began with Microsoft's launch of the Xbox 360 in 2005, and continued in 2006 when Sony and Nintendo launched their next-generation systems, the PLAYSTATION 3 and the Wii, respectively. Unlike past cycles, we believe this current cycle may be extended, partly due to the growth of online gaming services and content, the greater graphic and processing power of the current-generation hardware and the introduction of new peripherals. However, growth in the installed base of users of the Xbox 360, the PLAYSTATION 3 and the Wii may slow down in light of the economic environment. Consequently, our industry may experience a decline.

Wireless Platforms. Advances in wireless technology have resulted in a variety of new and evolving platforms for on-the-go interactive entertainment that appeal to a broad consumer base. Our efforts in wireless interactive entertainment are focused in two areas—packaged goods games for handheld game systems and downloadable games for mobile devices. We expect sales of games for mobile devices to continue to be an important part of our business worldwide.

Catalog Sales. The video game industry is experiencing a change in retail sales patterns which is decreasing revenue from catalog sales (sales of games in the periods following the launch quarter). Currently, many console games experience sales cycles that are shorter than in the past. To mitigate this trend, we offer our consumers a direct-to-consumer service (such as head-to-head play or other multiplayer options) and/or additional content available through online services to further enhance the gaming experience and extend the time that consumers play our games after their initial purchase. We anticipate that in some cases these additional online services will also generate revenue to mitigate the effect of reduced catalog sales.

Used Games. Some retailers sell used video games, which are generally priced lower than new video games and do not result in revenue to the publisher of the games from the sale. We have observed that the market for used video games has been growing. If retailers continue to increase their sales of used video games, it could negatively affect our sales of new video games and have an adverse impact on our operating results.

Concentration of Sales Among the Most Popular Games. We see a larger portion of packaged goods games sales concentrated on the most popular titles, and that those titles are typically sequels of prior games. We have reacted to this trend by significantly reducing the number of games that we produce to provide greater focus on our most promising intellectual properties.

Digital Content Distribution and Services. Consumers are spending an ever-increasing portion of their money and time on interactive entertainment that is accessible online, or through mobile digital devices such as smart phones, or through social networks such as Facebook and MySpace. We provide a variety of online delivered products and services. Many of our games that are available as packaged good products are also available through direct online download through the Internet (from websites we maintain and others that we license). We also offer online delivered content and services that are add-ons or related

Table of Contents

to our packaged goods products such as additional game content or enhancements of multiplayer services. Further, we provide other games, content and services that are available only via electronic delivery, such as Internet-only games and game services, and games for mobile devices. Advances in mobile technology have resulted in a variety of new and evolving devices that are being used to play games by an ever-broadening base of consumers. We have responded to these advances in technology, and consumer acceptance of digital distribution, by offering subscription services, online downloads for a one-time fee, and advertising-supported free games and game sites. We expect online delivery of games and game services to be an increasing part of our business going forward.

Recent Developments

International Operations and Foreign Currency Exchange Impact. International sales (*i.e.*, revenue derived from countries other than Canada and the United States), are a fundamental part of our business. Net revenue from international sales accounted for approximately 45 percent of our total net revenue during the three months ended June 30, 2010 and approximately 47 percent of our total net revenue during the three months ended June 30, 2009. We believe that in order to succeed internationally, it is important to locally develop content that is specifically directed toward local cultures and customs. Our net revenue is impacted by foreign exchange rates during the reporting period associated with our net revenue before revenue deferral as well as the foreign exchange rates associated with the recognition of our deferred net revenue of online-enabled packaged goods and digital content that were established at the time we recorded this deferred net revenue on our Condensed Consolidated Balance Sheets. The foreign exchange rates during the reporting period may not always move in the same direction as the foreign exchange rate impact associated with the recognition of our deferred net revenue of online-enabled packaged goods and digital content. During the three months ended June 30, 2010, foreign exchange rates had an overall favorable impact on our net revenue of approximately \$26 million, or 4 percent. In addition, our international investments and our cash and cash equivalents denominated in foreign currencies are subject to fluctuations in foreign currency. If the U.S. dollar strengthens against these currencies, then foreign exchange rates may have an unfavorable impact on our results of operations and our financial condition.

CRITICAL ACCOUNTING POLICIES AND ESTIMATES

Our Condensed Consolidated Financial Statements have been prepared in accordance with accounting principles generally accepted in the United States. The preparation of these Condensed Consolidated Financial Statements requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities, contingent assets and liabilities, and revenue and expenses during the reporting periods. The policies discussed below are considered by 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 requires both management judgment and estimates of matters that are inherently uncertain and unknown. As a result, actual results may differ materially from our estimates.

Revenue Recognition, Sales Returns, Allowances and Bad Debt Reserves

We derive revenue principally from sales of interactive software games designed for play on video game consoles (such as the PLAYSTATION 3, Xbox 360 and Wii), PCs, handheld game players (such as the PSP and Nintendo DS), mobile devices (such as cellular and smart phones including the Apple iPhone) and wireless devices such as the Apple iPad. We evaluate revenue recognition based on the criteria set forth in Financial Accounting Standards Board (FASB) Accounting Standards Codification (ASC) 985-605, *Software: Revenue Recognition*, and Staff Accounting Bulletin (SAB) No. 104, *Revenue Recognition*. We evaluate and recognize revenue when all four of the following criteria are met:

Evidence of an arrangement. Evidence of an agreement with the customer that reflects the terms and conditions to deliver products that must be present in order to recognize revenue.

Delivery. Delivery is considered to occur when a product is shipped and the risk of loss and rewards of ownership have been transferred to the customer. For online game services, delivery is considered to occur as the service is provided. For digital downloads that do not have an online service component, delivery is generally considered to occur when the download is made available.

Fixed or determinable fee. If a portion of the arrangement fee is not fixed or determinable, we recognize revenue as the amount becomes fixed or determinable.

Edgar Filing: ELECTRONIC ARTS INC. - Form 10-Q

Collection is deemed probable. We conduct a credit review of each customer involved in a significant transaction to determine the creditworthiness of the customer. Collection is deemed probable if we expect the customer to be able to pay amounts under the arrangement as those amounts become due. If we determine that collection is not probable, we recognize revenue when collection becomes probable (generally upon cash collection).

Table of Contents

Determining whether and when some of these criteria have been satisfied often involves assumptions and management judgments that can have a significant impact on the timing and amount of revenue we report in each period. For example, for multiple element arrangements, we must make assumptions and judgments in order to (1) determine whether and when each element has been delivered, (2) determine whether undelivered products or services are essential to the functionality of the delivered products and services, (3) determine whether VSOE exists for each undelivered element, and (4) allocate the total price among the various elements we must deliver. Changes to any of these assumptions or management 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.

Depending on the type of product, we may offer an online service that permits consumers to play against others via the Internet and/or receive additional updates or content from us. For those games that consumers can play via the Internet, we may provide a matchmaking service that permits consumers to connect with other consumers to play against each other online. In those situations where we do not require an additional fee for this online service, we account for the sale of the software product and the online service as a bundled sale, or multiple element arrangement, in which we sell both the software product and the online service for one combined price. We defer net revenue from sales of these games for which we do not have VSOE for the online service that we provided in connection with the sale, and recognize the revenue from these games over the estimated online service period, which is generally estimated to be six months beginning in the month after shipment. In addition, for some software products we also provide updates or additional content (digital content) to be delivered via the Internet that can be used with the original software product. In many cases we separately sell digital content for an additional fee; however, some purchased digital content can only be accessed via the Internet (*i.e.*, the consumer never takes possession of the digital content). We account for online transactions in which the consumer does not take possession of the digital content as a service transaction and, accordingly, we recognize the associated revenue over the estimated service period. In other transactions, at the date we sell the software product we have an obligation to provide incremental unspecified digital content in the future without an additional fee. In these cases, we account for the sale of the software product as a multiple element arrangement and recognize the revenue on a straight-line basis over the estimated period of game play.

Determining whether a transaction constitutes an online service transaction or a digital content download of a product requires judgment and can be difficult. The accounting for these transactions is significantly different. Revenue from product downloads is generally recognized when the download is made available (assuming all other recognition criteria are met). Revenue from an online game service is recognized as the service is rendered. If the service period is not defined, we recognize the revenue over the estimated service period. Determining the estimated service period is inherently subjective and is subject to regular revision based on historical online usage. In addition, determining whether we have an implicit obligation to provide incremental unspecified future digital content without an additional fee can be difficult.

Product revenue, including sales to resellers and distributors (channel partners), is recognized when the above criteria are met. We reduce product revenue for estimated future returns, price protection, and other offerings, which may occur with our customers and channel partners. Price protection represents the right to receive a credit allowance in the event we lower our wholesale price on a particular product. The amount of the price protection is generally the difference between the old price and the new price. In certain countries, we have stock-balancing programs for our PC and video game system software products, which allow for the exchange of these software products by resellers under certain circumstances. It is our general practice to exchange software products or give credits rather than to give cash refunds.

In certain countries, from time to time, we decide to provide price protection for our software products. When evaluating the adequacy of sales returns and price protection allowances, we analyze historical returns, current sell-through of distributor and retailer inventory of our software products, current trends in retail and the video game segment, changes in customer demand and acceptance of our software products, and other related factors. In addition, we monitor the volume of sales to our channel partners and their inventories, as substantial overstocking in the distribution channel could result in high returns or higher price protection costs in subsequent periods.

In the future, actual returns and price protections may materially exceed our estimates as unsold software products in the distribution channels are exposed to rapid changes in consumer preferences, market conditions or technological obsolescence due to new platforms, product updates or competing software products. For example, the risk of product returns and/or price protection for our software products may continue to increase as the PlayStation 2 console moves through its lifecycle. While we believe we can make reliable estimates regarding these matters, these estimates are inherently subjective. Accordingly, if our

Table of Contents

estimates changed, our returns and price protection reserves would change, which would impact the total net revenue we report. For example, if actual returns and/or price protection were significantly greater than the reserves we have established, our actual results would decrease our reported total net revenue. Conversely, if actual returns and/or price protection were significantly less than our reserves, this would increase our reported total net revenue. In addition, if our estimates of returns and price protection related to online-enabled packaged goods software products change, the amount of deferred net revenue we recognize in the future would change.

Significant management judgment is required to estimate our allowance for doubtful accounts in any accounting period. We determine our allowance for doubtful accounts by evaluating customer creditworthiness in the context of current economic trends and historical experience. Depending upon the overall economic climate and the financial condition of our customers, the amount and timing of our bad debt expense and cash collection could change significantly.

Fair Value Estimates

The preparation of financial statements in conformity with accounting principles generally accepted in the United States often requires us to determine the fair value of a particular item in order to fairly present our financial statements. Without an independent market or another representative transaction, determining the fair value of a particular item requires us to make several assumptions that are inherently difficult to predict and can have a material impact on the accounting conclusion.

There are various valuation techniques used to estimate fair value. These include (1) the market approach where market transactions for identical or comparable assets or liabilities are used to determine the fair value, (2) the income approach, which uses valuation techniques to convert future amounts (for example, future cash flows or future earnings) to a single present value amount, and (3) the cost approach, which is based on the amount that would be required to replace an asset. For many of our fair value estimates, including our estimates of the fair value of acquired intangible assets and acquired in-process technology, we use the income approach. Using the income approach requires the use of financial models, which require us to make various estimates including, but not limited to (1) the potential future cash flows for the asset or liability being measured, (2) the timing of receipt or payment of those future cash flows, (3) the time value of money associated with the delayed receipt or payment of such cash flows, and (4) the inherent risk associated with the cash flows (risk premium). Making these cash flow estimates are inherently difficult and subjective, and, if any of the estimates used to determine the fair value using the income approach turns out to be inaccurate, our financial results may be negatively impacted. Furthermore, relatively small changes in many of these estimates can have a significant impact to the estimated fair value resulting from the financial models or the related accounting conclusion reached. For example, a relatively small change in the estimated fair value of an asset may change a conclusion as to whether an asset is impaired.

While we are required to make certain fair value assessments associated with the accounting for several types of transactions, the following areas are the most sensitive to these assessments:

Business Combinations. We must estimate the fair value of assets acquired, liabilities and contingencies assumed, acquired in-process technology, and contingent consideration issued in a business combination. Our assessment of the estimated fair value of each of these can have a material effect on our reported results as intangible assets and acquired in-process technology are amortized over various estimated useful lives. Furthermore, a change in the estimated fair value of an asset or liability often has a direct impact on the amount to recognize as goodwill, an asset that is not amortized. Determining the fair value of assets acquired requires an assessment of the highest and best use or the expected price to sell the asset and the related expected future cash flows. Determining the fair value of acquired in-process technology also requires an assessment of our expectations related to the use of that asset. Determining the fair value of an assumed liability requires an assessment of the expected cost to transfer the liability. Determining the fair value of contingent consideration issued requires an assessment of the expected future cash flows over the period in which the obligation is expected to be settled, and applying a discount rate that appropriately captures a market participant's view of the risk associated with the obligation. This fair value assessment is also required in periods subsequent to a business combination. Such estimates are inherently difficult and subjective and can have a material impact on our Condensed Consolidated Financial Statements.

Assessment of Impairment of Goodwill, Intangibles, and Other Long-Lived Assets. Current accounting standards require that we assess the recoverability of our finite lived acquisition-related intangible assets and other long-lived assets whenever events or changes in circumstances indicate the remaining value of the assets recorded on our Condensed Consolidated Balance Sheets is potentially impaired. In order to determine if a potential impairment has occurred, management must make various assumptions about the estimated fair value of the asset by evaluating future business prospects and estimated cash flows. For some assets, our estimated fair value is dependent upon predicting which of our products will be successful. This success is dependent upon several factors, which are beyond our control, such as which operating platforms will be successful in the marketplace. Also, our revenue and earnings are dependent on our ability to meet our product release schedules.

Table of Contents

We are required to perform a two-step approach to testing goodwill for impairment for each reporting unit annually, or whenever events or changes in circumstances indicate the fair value of a reporting unit is below its carrying amount. Our reporting units are determined by the components of our operating segments that constitute a business for which (1) discrete financial information is available and (2) segment management regularly reviews the operating results of that component. We are required to perform the impairment test at least annually by applying a fair value-based test. The first step measures for impairment by applying fair value-based tests at the reporting unit level. The second step (if necessary) measures the amount of impairment by applying fair value-based tests to the individual assets and liabilities within each reporting unit.

To determine the fair value of each reporting unit used in the first step, we use a combination of the market approach, which utilizes comparable companies' data, and/or the income approach, which utilizes discounted cash flows. Each step requires us to make judgments and involves the use of significant estimates and assumptions. These estimates and assumptions include long-term growth rates and operating margins used to calculate projected future cash flows, risk-adjusted discount rates based on our weighted average cost of capital, future economic and market conditions and determination of appropriate market comparables. These estimates and assumptions have to be made for each reporting unit evaluated for impairment. Our estimates for market growth, our market share and costs are based on historical data, various internal estimates and certain external sources, and are based on assumptions that are consistent with the plans and estimates we are using to manage the underlying business. Our business consists of developing, marketing and distributing video game software using both established and emerging intellectual properties and our forecasts for emerging intellectual properties are based upon internal estimates and external sources rather than historical information and have an inherently higher risk of accuracy. If future forecasts are revised, they may indicate or require future impairment charges. We base our fair value estimates on assumptions we believe to be reasonable but that are unpredictable and inherently uncertain. Actual future results may differ from those estimates.

Assessment of Impairment of Short-Term Investments, Marketable Equity Securities and Other Investments. We periodically review our short-term investments, marketable equity securities and other investments for impairment. Our short-term investments consist of securities with remaining maturities greater than three months at the time of purchase and our marketable equity securities consist of investments in common stock of publicly traded companies, both are accounted for as available-for-sale securities. Unrealized gains and losses on our short-term investments and marketable equity securities are recorded as a component of accumulated other comprehensive income in stockholders' equity, net of tax, until either (1) the security is sold or (2) we determine that the fair value of the security has declined below its adjusted cost basis and the decline is other-than-temporary. Realized gains and losses on our short-term investments and marketable equity securities are calculated based on the specific identification method and are reclassified from accumulated other comprehensive income to interest and other income, net, and losses on strategic investments, net, respectively. Determining whether the decline in fair value is other-than-temporary requires management judgment based on the specific facts and circumstances of each security. The ultimate value realized on these securities is subject to market price volatility until they are sold. We consider various factors in determining whether we should recognize an impairment charge, including the credit quality of the issuer, the duration that the fair value has been less than the adjusted cost basis, severity of the impairment, reason for the decline in value and potential recovery period, the financial condition and near-term prospects of the investees, and our intent to sell and ability to hold the investment for a period of time sufficient to allow for any anticipated recovery in market value, any contractual terms impacting the prepayment or settlement process, as well as, if we would be required to sell an investment due to liquidity or contractual reasons before its anticipated recovery. During the three months ended June 30, 2010 and 2009, we recognized impairment charges on our marketable equity securities of \$2 million and \$16 million, respectively. Our ongoing consideration of these factors could result in additional impairment charges in the future, which could have a material impact on our financial results.

Our other investments consist principally of non-voting preferred shares in two companies whose common stock is publicly traded and are accounted for under the cost method. Under this method, these investments are recorded at cost until we determine that the fair value of the investment has fallen below its adjusted cost basis and that such declines are other-than-temporary. We monitor these investments for impairment and make appropriate reductions in the carrying values if we determine that an impairment charge is required, based primarily on the financial condition and near-term prospects of the investees. We did not recognize any impairment charges during the three months ended June 30, 2010 and 2009 on our other investments.

Assessment of Inventory Obsolescence. We regularly review inventory quantities on-hand. We write down inventory based on excess or obsolete inventories determined primarily by future anticipated demand for our products. Inventory write-downs are measured as the difference between the cost of the inventory and market value, based upon assumptions about future demand that are inherently difficult to assess. At the point of a loss recognition, a new, lower cost basis for that inventory is established, and subsequent changes in facts and circumstances do not result in the restoration or increase in that newly established cost basis.

Table of Contents

Stock-Based Compensation

We are required to estimate the fair value of share-based payment awards on the date of grant. We recognize compensation costs for stock-based payment transactions to employees based on their grant-date fair value on a straight-line approach over the service period for which such awards are expected to vest. The fair value of restricted stock units and restricted stock is determined based on the quoted market price of our common stock on the date of grant. The fair value of stock options and stock purchase rights granted pursuant to our equity incentive plans and our 2000 Employee Stock Purchase Plan (ESPP), respectively, is determined using the Black-Scholes valuation model. The determination of fair value is affected by our stock price, as well as assumptions regarding subjective and complex variables such as expected employee exercise behavior and our expected stock price volatility over the expected term of the award. Generally, our assumptions are based on historical information and judgment is required to determine if historical trends may be indicators of future outcomes. The key assumptions for the Black-Scholes valuation calculation are:

Risk-free interest rate. The risk-free interest rate is based on U.S. Treasury yields in effect at the time of grant for the expected term of the option.

Expected volatility. We use a combination of historical stock price volatility and implied volatility computed based on the price of options publicly traded on our common stock for our expected volatility assumption.

Expected term. The expected term represents the weighted-average period the stock options are expected to remain outstanding. The expected term is determined based on historical exercise behavior, post-vesting termination patterns, options outstanding and future expected exercise behavior.

Expected dividends.

Employee stock-based compensation expense is calculated based on awards ultimately expected to vest and is reduced for estimated forfeitures. Forfeitures are revised, if necessary, in subsequent periods if actual forfeitures differ from those estimates and an adjustment to stock-based compensation expense will be recognized at that time.

Changes to our underlying stock price, our assumptions used in the Black-Scholes option valuation calculation and our forfeiture rate, as well as future equity granted or assumed through acquisitions could significantly impact the compensation expense we recognize.

Royalties and Licenses

Our royalty expenses consist of payments to (1) content licensors, (2) independent software developers, and (3) co-publishing and distribution affiliates. License royalties consist of payments made to celebrities, professional sports organizations, movie studios and other organizations for our use of their trademarks, copyrights, personal publicity rights, content and/or other intellectual property. Royalty payments to independent software developers are payments for the development of intellectual property related to our games. Co-publishing and distribution royalties are payments made to third parties for the delivery of products.

Royalty-based obligations with content licensors and distribution affiliates are either paid in advance and capitalized as prepaid royalties or are accrued as incurred and subsequently paid. These royalty-based obligations are generally expensed to cost of goods sold generally at the greater of the contractual rate or an effective royalty rate based on the total projected net revenue. Significant judgment is required to estimate the effective royalty rate for a particular contract. Because the computation of effective royalty rates requires us to project future revenue, it is inherently subjective as our future revenue projections must anticipate a number of factors, including (1) the total number of titles subject to the contract, (2) the timing of the release of these titles, (3) the number of software units we expect to sell, which can be impacted by a number of variables, including product quality, the timing of the title s release and competition, and (4) future pricing. Determining the effective royalty rate for our titles is particularly challenging due to the inherent difficulty in predicting the popularity of entertainment products. Accordingly, if our future revenue projections change, our effective royalty rates would change, which could impact the amount and timing of royalty expense we recognize.

Table of Contents

Prepayments made to thinly capitalized independent software developers and co-publishing affiliates are generally made in connection with the development of a particular product and, therefore, we are generally subject to development risk prior to the release of the product. Accordingly, payments that are due prior to completion of a product are generally expensed to research and development over the development period as the services are incurred. Payments due after completion of the product (primarily royalty-based in nature) are generally expensed as cost of goods sold.

Our contracts with some licensors include minimum guaranteed royalty payments, which are initially recorded as an asset and as a liability at the contractual amount when no performance remains with the licensor. When performance remains with the licensor, we record guarantee payments as an asset when actually paid and as a liability when incurred, rather than recording the asset and liability upon execution of the contract. These obligations are classified as current liabilities to the extent such royalty payments are contractually due within the next twelve months. As of June 30, 2010 and March 31, 2010, approximately \$7 million and \$13 million, respectively, of minimum guaranteed royalty obligations had been recognized.

Each quarter, we also evaluate the expected future realization of our royalty-based assets, as well as any unrecognized minimum commitments not yet paid to determine amounts we deem unlikely to be realized through product sales. Any impairments or losses determined before the launch of a product are charged to research and development expense. Impairments or losses determined post-launch are charged to cost of goods sold. We evaluate long-lived royalty-based assets for impairment using undiscounted cash flows when impairment indicators exist. Unrecognized minimum royalty-based commitments are accounted for as executory contracts and, therefore, any losses on these commitments are recognized when the underlying intellectual property is abandoned (*i.e.*, cease use) or the contractual rights to use the intellectual property are terminated. During the three months ended June 30, 2010 and 2009, we recognized losses of \$10 million and impairment charges of \$1 million, respectively.

Income Taxes

We recognize deferred tax assets and liabilities for both the expected impact of differences between the financial statement amount and the tax basis of assets and liabilities and for the expected future tax benefit to be derived from tax losses and tax credit carry forwards. We record a valuation allowance against deferred tax assets when it is considered more likely than not that all or a portion of our deferred tax assets will not be realized. In making this determination, we are required to give significant weight to evidence that can be objectively verified. It is generally difficult to conclude that a valuation allowance is not needed when there is significant negative evidence, such as cumulative losses in recent years. Forecasts of future taxable income are considered to be less objective than past results, particularly in light of the economic environment. Therefore, cumulative losses weigh heavily in the overall assessment.

In addition to considering forecasts of future taxable income, we are also required to evaluate and quantify other possible sources of taxable income in order to assess the realization of our deferred tax assets, namely the reversal of existing deferred tax liabilities, the carry back of losses and credits as allowed under current tax law, and the implementation of tax planning strategies. Evaluating and quantifying these amounts involves significant judgments. Each source of income must be evaluated based on all positive and negative evidence; this evaluation involves assumptions about future activity. Certain taxable temporary differences that are not expected to reverse during the carry forward periods permitted by tax law cannot be considered as a source of future taxable income that may be available to realize the benefit of deferred tax assets.

Based on the assumptions and requirements noted above, we have recorded a valuation allowance against most of our U.S. deferred tax assets. In addition, we expect to provide a valuation allowance on future U.S. tax benefits until we can sustain a level of profitability or until other significant positive evidence arises that suggest that these benefits are more likely than not to be realized.

In the ordinary course of our business, there are many transactions and calculations where the tax law and ultimate tax determination is uncertain. As part of the process of preparing our Condensed Consolidated Financial Statements, we are required to estimate our income taxes in each of the jurisdictions in which we operate prior to the completion and filing of tax returns for such periods. This process requires estimating both our geographic mix of income and our uncertain tax positions in each jurisdiction where we operate. These estimates involve complex issues and require us to make judgments about the likely application of the tax law to our situation, as well as with respect to other matters, such as anticipating the positions that we will take on tax returns prior to our actually preparing the returns and the outcomes of disputes with tax authorities. The ultimate resolution of these issues may take extended periods of time due to examinations by tax authorities and statutes of limitations. In addition, changes in our business, including acquisitions, changes in our international corporate structure, changes in the geographic location of business functions or assets, changes in the geographic mix and amount of income, as well as changes in

Table of Contents

our agreements with tax authorities, valuation allowances, applicable accounting rules, applicable tax laws and regulations, rulings and interpretations thereof, developments in tax audit and other matters, and variations in the estimated and actual level of annual pre-tax income can affect the overall effective income tax rate.

We historically have considered undistributed earnings of our foreign subsidiaries to be indefinitely reinvested outside of the United States and, accordingly, no U.S. taxes have been provided thereon. We currently intend to continue to indefinitely reinvest the undistributed earnings of our foreign subsidiaries outside of the United States.

RESULTS OF OPERATIONS

Our fiscal year is reported on a 52 or 53-week period that ends on the Saturday nearest March 31. Our results of operations for the fiscal years ending or ended, as the case may be, March 31, 2011 and 2010 contain 52 and 53 weeks, respectively, and ends or ended, as the case may be, on April 2, 2011 and April 3, 2010, respectively. Our results of operations for the three months ended June 30, 2010 and 2009 contained 13 weeks and 14 weeks, respectively, and ended on July 3, 2010 and July 4, 2009, respectively. For simplicity of disclosure, all fiscal periods are referred to as ending on a calendar month end.

Net Revenue

Net revenue consists of sales generated from (1) video games sold as packaged goods and designed for play on hardware consoles (such as the PLAYSTATION 3, Xbox 360 and Wii), PCs, and handheld game players (such as the Sony PSP and Nintendo DS), (2) video games for mobile devices (such as cellular and smart phones including the Apple iPhone), (3) video games for wireless devices such as the Apple iPad, (4) digitally downloaded games and content and online services associated with these games, (5) services in connection with some of our online-enabled games, (6) programming third-party web sites with our game content, (7) allowing other companies to manufacture and sell our products in conjunction with other products, and (8) advertisements on our online web pages and in our games.

Net Revenue before Revenue Deferral, a non-GAAP financial measure, is provided in this section of Management's Discussion and Analysis of Financial Condition and Results of Operations (MD&A). See Non-GAAP Financial Measures below for an explanation of our use of this non-GAAP measure. A reconciliation to the corresponding measure calculated in accordance with accounting principles generally accepted in the United States is provided in the discussion below.

Revenue Deferral in this Net Revenue section, includes the unrecognized revenue from (1) bundled sales of certain online-enabled packaged goods and PC digital downloads for which either we do not have VSOE for the online service that we provide in connection with the sale of the software or we have an obligation to provide future incremental unspecified digital content, (2) certain packaged goods sales of massively-multiplayer online role-playing games, and (3) sales of certain incremental digital content associated with our games, which are types of micro-transactions. Fluctuations in the Revenue Deferral are largely dependent upon the amounts of products that we sell with the online features and services previously discussed, while the recognition of Revenue Deferral for a period is also dependent upon (1) the period of time the online features and services are to be provided and (2) the timing of the sale. For example, most Revenue Deferrals incurred in the first half of a fiscal year are recognized within the same fiscal year; however, substantially all of the Revenue Deferrals incurred in the last month of a fiscal year will be recognized in the subsequent fiscal year.

From a geographical perspective, our total Net Revenue for the three months ended June 30, 2010 and 2009 was as follows (in millions):

	Three Months Ended June 30, 2010				2009			
	North America	Europe	Asia	Total	North America	Europe	Asia	Total
Net Revenue before Revenue Deferral	\$ 267	\$ 236	\$ 36	\$ 539	\$ 449	\$ 319	\$ 48	\$ 816
Revenue Deferral	(135)	(159)	(24)	(318)	(200)	(163)	(21)	(384)
Recognition of Revenue Deferral	319	240	35	594	94	102	16	212
Net Revenue	\$ 451	\$ 317	\$ 47	\$ 815	\$ 343	\$ 258	\$ 43	\$ 644

For the three months ended June 30, 2010, Net Revenue before Revenue Deferral was \$539 million, driven by 2010 FIFA WORLD CUP SOUTH AFRICA, Battlefield: Bad Company 2, and SKATE 3. Net Revenue before Revenue Deferral for the three months ended June 30, 2010

decreased \$277 million, or 34 percent, as compared to the three months ended June 30, 2009.

Table of Contents

From a franchise perspective, this decrease was primarily driven by a \$320 million decrease from The Sims, EA SPORTS Active, Fight Night, and Tiger Woods PGA Tour®. This decrease was partially offset by a \$145 million increase from the FIFA World Cup and Battlefield franchises.

Revenue Deferral for the three months ended June 30, 2010 decreased \$66 million, or 17 percent, as compared to the three months ended June 30, 2009. This decrease was due to a decrease in Net Revenue before Revenue Deferral partially offset by the deferral of catalog sales of online-enabled products with an obligation to provide future incremental unspecified digital content on a when and if available basis during the three months ended June 30, 2010 with no comparable deferral of catalog sales during the three months ended June 30, 2009. From a franchise perspective, this decrease was primarily driven by a \$223 million decrease from The Sims, Fight Night, and Tiger Woods PGA Tour. This decrease was partially offset by a \$146 million increase from the FIFA World Cup and Battlefield franchises.

The Recognition of Revenue Deferral for the three months ended June 30, 2010 increased \$382 million, or 180 percent, as compared to the three months ended June 30, 2009. This increase was primarily due to the Recognition of Revenue Deferral during the three months ended June 30, 2010 associated with the sales of online-enabled products with an obligation to provide future incremental unspecified digital content on a when and if available basis during the last half of fiscal year 2010 with less comparable recognition during the three months ended June 30, 2009. From a franchise perspective, this increase was primarily driven by a \$257 million increase from Battlefield, Dragon Age, Mass Effect , and The Sims.

For three months ended June 30, 2010, Net Revenue was \$815 million, driven by *Battlefield: Bad Company 2*, *FIFA 10*, and *Dragon Age: Origins*. Net Revenue for the three months ended June 30, 2010 increased \$171 million, or 27 percent, as compared to the three months ended June 30, 2009. From a franchise perspective, this increase was primarily driven by a \$253 million increase from Battlefield, Dragon Age, Mass Effect, and Dante 's Inferno . This increase was partially offset by a \$117 million decrease from the EA SPORTS Active and Harry Potter franchises.

North America

For the three months ended June 30, 2010, Net Revenue before Revenue Deferral in North America was \$267 million, driven by sales of *2010 FIFA WORLD CUP SOUTH AFRICA*, *SKATE 3*, and *Battlefield: Bad Company 2*. Net Revenue before Revenue Deferral for the three months ended June 30, 2010 decreased \$182 million, or 41 percent, as compared to the three months ended June 30, 2009. From a franchise perspective, this decrease was primarily driven by a \$159 million decrease from Fight Night, EA SPORTS Active, and The Sims.

Revenue Deferral for the three months ended June 30, 2010 decreased \$65 million, or 33 percent, as compared to the three months ended June 30, 2009. This decrease was due to a decrease in Net Revenue before Revenue Deferral partially offset by the deferral of catalog sales of online-enabled products with an obligation to provide future incremental unspecified digital content on a when and if available basis during the three months ended June 30, 2010 with no comparable deferral of catalog sales during the three months ended June 30, 2009. From a franchise perspective, the decrease was primarily driven by a \$123 million decrease from Fight Night, The Sims, and Tiger Woods PGA Tour. This decrease was partially offset by a \$57 million increase from the FIFA World Cup and SKATE franchises.

The Recognition of Revenue Deferral for the three months ended June 30, 2010 increased \$225 million, or 239 percent, as compared to the three months ended June 30, 2009. This increase was primarily due to the Recognition of Revenue Deferral during the three months ended June 30, 2010 associated with the sales of online-enabled products with an obligation to provide future incremental unspecified digital content on a when and if available basis during the last half of fiscal year 2010 with less comparable recognition during the three months ended June 30, 2009. From a franchise perspective, the increase was primarily driven by a \$143 million increase from Battlefield, Dragon Age, Mass Effect, and Army of Two .

For the three months ended June 30, 2010, Net Revenue in North America was \$451 million, driven by *Battlefield: Bad Company 2*, *Madden 10*, and *Dragon Age: Origins*. Net Revenue for the three months ended June 30, 2010 increased \$108 million, or 31 percent, as compared to the three months ended June 30, 2009. From a franchise perspective, this increase was primarily driven by a \$143 million increase from Battlefield, Dragon Age, Mass Effect, and Army of Two. This increase was partially offset by a \$70 million decrease from the EA SPORTS Active and Harry Potter franchises.

Table of Contents***Europe***

For the three months ended June 30, 2010, Net Revenue before Revenue Deferral in Europe was \$236 million, driven by sales of *2010 FIFA WORLD CUP SOUTH AFRICA*, *FIFA 10*, and *Battlefield: Bad Company 2*. Net Revenue before Revenue Deferral for the three months ended June 30, 2010 decreased \$83 million, or 26 percent, as compared to the three months ended June 30, 2009. From a franchise perspective, this decrease was primarily driven by a \$128 million decrease from The Sims, EA SPORTS Active, Harry Potter, and The Godfather. This decrease was partially offset by a \$78 million increase from the FIFA World Cup and Battlefield franchises. We estimate that foreign exchange rates (primarily the Euro) decreased reported Net Revenue before Revenue Deferral by approximately \$3 million, or 1 percent, for the three months ended June 30, 2010 as compared to the three months ended June 30, 2009. Excluding the effect of foreign exchange rates from Net Revenue before Revenue Deferral, we estimate that Net Revenue before Revenue Deferral decreased by approximately \$80 million, or 25 percent, for the three months ended June 30, 2010 as compared to the three months ended June 30, 2009.

Revenue Deferral for three months ended June 30, 2010 decreased by \$4 million, or 2 percent, as compared to three months ended June 30, 2009. From a franchise perspective, the decrease was primarily driven by an \$81 million decrease from The Sims and Fight Night. This decrease was partially offset by a \$78 million increase from the FIFA World Cup and Battlefield franchises.

The Recognition of Revenue Deferral for the three months ended June 30, 2010 increased \$138 million, or 135 percent, as compared to the three months ended June 30, 2009. This increase was primarily due to the Recognition of Revenue Deferral during the three months ended June 30, 2010 associated with the sales of online-enabled products with an obligation to provide future incremental unspecified digital content on a when and if available basis during the last half of fiscal year 2010 with less comparable recognition during the three months ended June 30, 2009. From a franchise perspective, the increase was primarily driven by a \$106 million increase from Battlefield, The Sims, Dragon Age, and Mass Effect.

For three months ended June 30, 2010, Net Revenue in Europe was \$317 million, driven by *Battlefield: Bad Company 2*, *FIFA 10*, and *Dragon Age: Origins*. Net Revenue for the three months ended June 30, 2010 increased \$59 million, or 23 percent, as compared to the three months ended June 30, 2009. From a franchise perspective, the increase was primarily driven by an \$86 million increase from Battlefield, Dragon Age, and The Sims. This increase was partially offset by a \$42 million decrease from the EA SPORTS Active and Harry Potter franchises. During the three months ended June 30, 2010, foreign exchange rates had an overall favorable impact on our reported Net Revenue of approximately \$15 million, or 6 percent, as compared to the three months ended June 30, 2009 primarily as a result of favorable foreign exchange rates associated with the recognition of our deferred net revenue of online-enable packaged goods and digital content. Excluding the effect of foreign exchange rates from Net Revenue, we estimate that net revenue increased by approximately \$44 million, or 17 percent, for the three months ended June 30, 2010 as compared to the three months ended June 30, 2009.

Asia

For the three months ended June 30, 2010, Net Revenue before Revenue Deferral in Asia was \$36 million, driven by *2010 FIFA WORLD CUP SOUTH AFRICA*, *Battlefield: Bad Company 2*, and *FIFA Online 2*. Net Revenue before Revenue Deferral for the three months ended June 30, 2010 decreased by \$12 million, or 25 percent, as compared to the three months ended June 30, 2009. From a franchise perspective, this decrease was primarily driven by an \$18 million decrease from The Sims, The Godfather, EA SPORTS Active, Harry Potter, and Fight Night. This decrease was partially offset by a \$14 million increase from the FIFA World Cup and Battlefield franchises. We estimate that foreign exchange rates (primarily the Australian dollar) increased reported Net Revenue before Revenue Deferral by approximately \$4 million, or 8 percent, for the three months ended June 30, 2010 as compared to the three months ended June 30, 2009. Excluding the effect of foreign exchange rates from Net Revenue before Revenue Deferral, we estimate that Net Revenue before Revenue Deferral decreased by approximately \$16 million, or 33 percent, for the three months ended June 30, 2010 as compared to the three months ended June 30, 2009.

Revenue Deferral for the three months ended June 30, 2010 increased \$3 million, or 14 percent, as compared to the three months ended June 30, 2009. From a franchise perspective, the increase was driven by a \$14 million increase from FIFA World Cup and Battlefield. This increase was partially offset by a \$10 million decrease from The Sims, Fight Night, and The Godfather franchises.

The Recognition of Revenue Deferral for the three months ended June 30, 2010 increased \$19 million, or 119 percent, as compared to the three months ended June 30, 2009. From a franchise perspective, the increase was primarily driven by a \$16 million increase from Battlefield, Dragon Age, FIFA World Cup and Mass Effect.

Table of Contents

For the three months ended June 30, 2010, Net Revenue in Asia was \$47 million, driven by *Battlefield: Bad Company 2*, *FIFA 10*, and *Dante's Inferno*. Net Revenue for the three months ended June 30, 2010 increased by \$4 million, or 9 percent, as compared to the three months ended June 30, 2009. From a franchise perspective, this increase was primarily driven by an \$11 million increase from Battlefield and Dragon Age. This increase was partially offset by a \$6 million decrease from the Need for Speed and EA SPORTS Active franchises. During the three months ended June 30, 2010, foreign exchange rates had an overall favorable impact on our reported Net Revenue of approximately \$11 million, or 26 percent, as compared to the three months ended June 30, 2009 primarily as a result of favorable foreign exchange rates associated with the recognition of our deferred net revenue of online-enabled packaged goods and digital content. Excluding the effect of foreign exchange rates from Net Revenue, we estimate that Net Revenue decreased by approximately \$7 million, or 17 percent, for the three months ended June 30, 2010 as compared to the three months ended June 30, 2009.

Non-GAAP Financial Measures

Net Revenue before Revenue Deferral is a non-GAAP financial measure that excludes the impact of Revenue Deferral and the Recognition of Revenue Deferral on Net Revenue related to packaged goods games and digital content. We defer Net Revenue from sales of certain online-enabled packaged goods and digital content for which we are not able to objectively determine the fair value (as defined by accounting principles generally accepted in the United States for software sales) of the online service that we provided in connection with the sale. We recognize the revenue from these games over the estimated online service period. We also defer Net Revenue from sales of certain online-enabled packaged goods and digital content for which we had an obligation to deliver incremental unspecified digital content in the future without an additional fee. We recognize the revenue for these games on a straight-line basis over the estimated life of the game.

We believe that excluding the impact of Revenue Deferral and the Recognition of Revenue Deferral related to packaged goods games and digital content from our operating results is important to facilitate comparisons between periods in understanding our underlying sales performance for the period.

We use this non-GAAP measure internally to evaluate our operating performance, when planning, forecasting and analyzing future periods, and when assessing the performance of our management team. While we believe that this non-GAAP financial measure is useful in evaluating our business, this information should be considered as supplemental in nature and is not meant to be considered in isolation from or as a substitute for the related financial information prepared in accordance with GAAP. In addition, this non-GAAP financial measure may not be the same as non-GAAP measures presented by other companies.

Cost of Goods Sold

Cost of goods sold for our packaged-goods business consists of (1) product costs, (2) certain royalty expenses for celebrities, professional sports and other organizations and independent software developers, (3) manufacturing royalties, net of volume discounts and other vendor reimbursements, (4) expenses for defective products, (5) write-offs of post-launch prepaid royalty costs, (6) amortization of certain intangible assets, (7) personnel-related costs, and (8) warehousing and distribution costs. We generally recognize volume discounts when they are earned from the manufacturer (typically in connection with the achievement of unit-based milestones); whereas other vendor reimbursements are generally recognized as the related revenue is recognized. Cost of goods sold for our online products consists primarily of data center and bandwidth costs associated with hosting our web sites, credit card fees and royalties for use of third-party properties. Cost of goods sold for our web site advertising business primarily consists of server costs.

Cost of goods sold for the three months ended June 30, 2010 and 2009 was as follows (in millions):

June 30, 2010	% of Net Revenue	June 30, 2009	% of Net Revenue	% Change	Change as a % of Net Revenue
\$ 222	27.2%	\$ 321	49.8%	(30.8%)	(22.6%)

During the three months ended June 30, 2010, cost of goods sold decreased by 22.6 percent as a percentage of total net revenue as compared to the three months ended June 30, 2009. This decrease as a percentage of net revenue was primarily due to a \$448 million decrease in the change in deferred net revenue related to certain online-enabled packaged goods and digital content for the three months ended June 30, 2010, as compared to the three months ended June 30, 2009. Overall, we estimate the decrease in the change in deferred net revenue related to certain online-enabled packaged goods and digital content positively impacted cost of goods sold as a percent of total net revenue by 24.5 percentage points.

Table of Contents**Marketing and Sales**

Marketing and sales expenses consist of personnel-related costs, related overhead costs and advertising, marketing and promotional expenses, net of qualified advertising cost reimbursements from third parties.

Marketing and sales expenses for the three months ended June 30, 2010 and 2009 were as follows (in millions):

June 30, 2010	% of Net Revenue	June 30, 2009	% of Net Revenue	\$ Change	% Change
\$ 127	16%	\$ 164	25%	\$ (37)	(23%)

Marketing and sales expenses decreased by \$37 million, or 23 percent, during the three months ended June 30, 2010, as compared to the three months ended June 30, 2009. The decrease was primarily due to a \$41 million decrease in marketing, advertising and promotional expenses resulting from a decrease in the number of titles released during the three months ended June 30, 2010 as compared to the three months ended June 30, 2009.

General and Administrative

General and administrative expenses consist of personnel and related expenses of executive and administrative staff, related overhead costs, fees for professional services such as legal and accounting, and allowances for doubtful accounts.

General and administrative expenses for the three months ended June 30, 2010 and 2009 were as follows (in millions):

June 30, 2010	% of Net Revenue	June 30, 2009	% of Net Revenue	\$ Change	% Change
\$ 74	9%	\$ 66	10%	\$ 8	12%

General and administrative expenses increased by \$8 million, or 12 percent, during the three months ended June 30, 2010, as compared to the three months ended June 30, 2009. This increase was primarily due to (1) an increase of \$9 million in incentive-based compensation expense and (2) an increase of \$7 million in stock-based compensation expense. These increases were partially offset by a \$6 million decrease in bad debt expense.

Research and Development

Research and development expenses consist of expenses incurred by our production studios for personnel-related costs, related overhead costs, contracted services, depreciation and any impairment of prepaid royalties for pre-launch products. Research and development expenses for our online products include expenses incurred by our studios consisting of direct development and related overhead costs in connection with the development and production of our online games. Research and development expenses also include expenses associated with the development of web site content, software licenses and maintenance, network infrastructure and management overhead.

Research and development expenses for the three months ended June 30, 2010 and 2009 were as follows (in millions):

June 30, 2010	% of Net Revenue	June 30, 2009	% of Net Revenue	\$ Change	% Change
\$ 275	34%	\$ 312	48%	\$ (37)	(12%)

Research and development expenses decreased by \$37 million, or 12 percent, during the three months ended June 30, 2010, as compared to the three months ended June 30, 2009. This decrease was primarily due to decreases in expenses resulting from our cost reduction initiatives including (1) a decrease of \$24 million in additional personnel-related costs, (2) a decrease of \$23 million in external development and contracted services, and (3) a decrease of \$12 million in facilities-related expenses. These decreases were partially offset by (1) a \$14 million

increase in incentive-based compensation expense and (2) a \$6 million increase in stock-based compensation expense.

Table of Contents**Amortization of Intangibles**

Amortization of intangibles for the three months ended June 30, 2010 and 2009 was as follows (in millions):

June 30, 2010	% of Net Revenue	June 30, 2009	% of Net Revenue	\$ Change	% Change
\$ 15	2%	\$ 12	2%	\$ 3	25%

Amortization of intangibles increased \$3 million, or 25 percent, during the three months ended June 30, 2010, as compared to the three months ended June 30, 2009, primarily due to amortization of intangibles related to our acquisition of Playfish.

Restructuring Charges

Restructuring charges for the three months ended June 30, 2010 and 2009 were as follows (in millions):

June 30, 2010	% of Net Revenue	June 30, 2009	% of Net Revenue	\$ Change	% Change
\$ 2		\$ 14	2%	\$ (12)	(86%)

In connection with our fiscal year 2010 restructuring, during the three months ended June 30, 2010, we incurred \$2 million of restructuring charges primarily related to the closure of certain of our facilities and other IT-related costs to assist in the reorganization of our business support functions.

In connection with our fiscal year 2009 restructuring and fiscal 2008 reorganization, during the three months ended June 30, 2009, we incurred \$9 million and \$5 million of restructuring charges, respectively, primarily for facilities-related expenses.

Losses on Strategic Investments

Losses on strategic investments for the three months ended June 30, 2010 and 2009 were as follows (in millions):

June 30, 2010	% of Net Revenue	June 30, 2009	% of Net Revenue	\$ Change	% Change
\$ (5)	(1%)	\$ (16)	(2%)	\$ 11	69%

During the three months ended June 30, 2010, losses on strategic investments decreased by \$11 million, or 69 percent, as compared to the three months ended June 30, 2009, primarily due to a decrease in impairment charges on our investment in The9.

Income Taxes

Benefit from income taxes for the three months ended June 30, 2010 and 2009 were as follows (in millions):

June 30, 2010	Effective Tax Rate	June 30, 2009	Effective Tax Rate	% Change
\$ (3)	(3.4%)	\$ (24)	9.0%	(88%)

The tax benefit reported for the three months ended June 30, 2010 is based on our projected annual effective tax rate for fiscal 2011, and also includes certain discrete tax benefits recorded during the period. Our effective tax rates for the three months ended June 30, 2010 and 2009 were

Edgar Filing: ELECTRONIC ARTS INC. - Form 10-Q

tax benefits of 3.4 percent and 9.0 percent, respectively. The effective tax rate for the three months ended June 30, 2010 differs from the statutory rate of 35.0 percent primarily due to U.S. losses for which no benefit is recognized and non-U.S. losses with a reduced or zero tax benefit, partially offset by tax benefits related to the expiration of statutes of limitations and resolution of examinations by taxing authorities. The effective tax rate for the three months ended June 30, 2010 differs from the same period in fiscal year 2010 primarily due to greater tax benefits recorded in fiscal 2010 related to the expiration of statutes of limitations and reductions in the valuation allowance on U.S. deferred tax assets.

Table of Contents

Our effective income tax rates for fiscal year 2011 and future periods will depend on a variety of factors, including changes in the deferred tax valuation allowance, as well as changes in our business such as acquisitions and intercompany transactions, changes in our international structure, changes in the geographic location of business functions or assets, changes in the geographic mix of income, changes in or termination of our agreements with tax authorities, applicable accounting rules, applicable tax laws and regulations, rulings and interpretations thereof, developments in tax audit and other matters, and variations in our annual pre-tax income or loss. We incur certain tax expenses that do not decline proportionately with declines in our pre-tax consolidated income or loss. As a result, in absolute dollar terms, our tax expense will have a greater influence on our effective tax rate at lower levels of pre-tax income or loss than at higher levels. In addition, at lower levels of pre-tax income or loss, our effective tax rate will be more volatile.

Certain taxable temporary differences that are not expected to reverse during the carry forward periods permitted by tax law cannot be considered as a source of future taxable income that may be available to realize the benefit of deferred tax assets.

We historically have considered undistributed earnings of our foreign subsidiaries to be indefinitely reinvested outside of the United States and, accordingly, no U.S. taxes have been provided thereon. We currently intend to continue to indefinitely reinvest the undistributed earnings of our foreign subsidiaries outside of the United States.

Impact of Recently Issued Accounting Standards

In October 2009, the FASB issued Accounting Standards Update (ASU) 2009-13, *Revenue Recognition (Topic 605) Multiple-Deliverable Revenue Arrangements*. This guidance modifies the fair value requirements of FASB ASC subtopic 605-25, *Revenue Recognition-Multiple Element Arrangements*, by allowing the use of the best estimate of selling price in addition to vendor specific objective evidence and third-party evidence for determining the selling price of a deliverable. This guidance establishes a selling price hierarchy for determining the selling price of a deliverable, which is based on: (a) vendor-specific objective evidence, (b) third-party evidence, or (c) estimates. In addition, the residual method of allocating arrangement consideration is no longer permitted. ASU 2009-13 is effective for fiscal years beginning on or after June 15, 2010. We do not expect the adoption of ASU 2009-13 to have a material impact on our Condensed Consolidated Financial Statements.

In October 2009, the FASB issued ASU 2009-14, *Software (Topic 985) Certain Revenue Arrangements that Include Software Elements*. This guidance modifies the scope of FASB ASC subtopic 965-605, *Software-Revenue Recognition*, to exclude from its requirements non-software components of tangible products and software components of tangible products that are sold, licensed, or leased with tangible products when the software components and non-software components of the tangible product function together to deliver the tangible product's essential functionality. ASU 2009-14 is effective for fiscal years beginning on or after June 15, 2010. We do not expect the adoption of ASU 2009-14 to have a material impact on our Condensed Consolidated Financial Statements.

Table of Contents**LIQUIDITY AND CAPITAL RESOURCES**

(In millions)	As of June 30, 2010	As of March 31, 2010	Increase / (Decrease)
Cash and cash equivalents	\$ 1,057	\$ 1,273	\$ (216)
Short-term investments	480	432	48
Marketable equity securities	193	291	(98)
Total	\$ 1,730	\$ 1,996	\$ (266)
Percentage of total assets	41%	43%	

(In millions)	Three Months Ended June 30, 2010	2009	Increase / (Decrease)
Cash used in operating activities	\$ (148)	\$ (328)	\$ 180
Cash used in investing activities	(53)	(112)	59
Cash provided by financing activities	1	3	(2)
Effect of foreign exchange on cash and cash equivalents	(16)	21	(37)
Net decrease in cash and cash equivalents	\$ (216)	\$ (416)	\$ 200

Changes in Cash Flow

During the three months ended June 30, 2010, we used \$148 million of cash in operating activities as compared to using \$328 million of cash for the three months ended June 30, 2009. The decrease in cash used in operating activities for the three months ended June 30, 2010 as compared to the three months ended June 30, 2009 was primarily due to (1) a decrease in our gross accounts receivable balances as a result of an earlier release schedule and a decrease of our first quarter titles, (2) a decrease in external development and contracted services as part of our cost reduction initiatives, and (3) a decrease in marketing and advertising expenses.

For the three months ended June 30, 2010, we generated \$98 million of cash proceeds from maturities and sales of short-term investments. Our primary use of cash in non-operating activities consisted of \$148 million used to purchase short-term investments.

Short-term Investments and Marketable Equity Securities

Due to our mix of fixed and variable rate securities, our short-term investment portfolio is susceptible to changes in short-term interest rates. As of June 30, 2010, our short-term investments had gross unrealized gains of \$2 million, or less than 1 percent of the total in short-term investments, and gross unrealized losses of less than \$1 million, or less than 1 percent of the total in short-term investments. From time to time, we may liquidate some or all of our short-term investments to fund operational needs or other activities, such as capital expenditures, business acquisitions or stock repurchase programs. Depending on which short-term investments we liquidate to fund these activities, we could recognize a portion, or all, of the gross unrealized gains or losses.

The fair value of our marketable equity securities decreased to \$193 million as of June 30, 2010 from \$291 million as of March 31, 2010. This decrease was primarily due to (1) an \$88 million decrease in the unrealized gains on our investments and (2) an \$11 million decrease in the cost basis of our investment in The9 resulting from the sale of a portion of this investment.

In February 2005, we purchased approximately 19.9 percent of the then-outstanding ordinary shares (representing approximately 18 percent of the voting rights at the time) of Ubisoft Entertainment ("Ubisoft") for \$91 million. Subsequent to June 30, 2010, we sold this investment for approximately \$121 million.

Receivables, Net

Our gross accounts receivable balances were \$283 million and \$423 million as of June 30, 2010 and March 31, 2010, respectively. The decrease in our accounts receivable balance was primarily due to lower sales volumes in the first quarter of fiscal year 2011 as compared to the fourth

Edgar Filing: ELECTRONIC ARTS INC. - Form 10-Q

quarter of fiscal year 2010, as well as the earlier release of our first quarter titles

Table of Contents

within the three months ended June 30, 2010 as compared to the three months ended June 30, 2009. We expect our accounts receivable balance to increase during the three months ending September 30, 2010 based on our seasonal product release schedule. Reserves for sales returns, pricing allowances and doubtful accounts decreased in absolute dollars from \$217 million as of March 31, 2010 to \$180 million as of June 30, 2010. As a percentage of trailing nine month net revenue, reserves decreased from 7 percent as of March 31, 2010, to 6 percent as of June 30, 2010. We believe these reserves are adequate based on historical experience and our current estimate of potential returns, pricing allowances and doubtful accounts.

Inventories

Inventories decreased to \$82 million as of June 30, 2010 from \$100 million as of March 31, 2010, primarily as a result of lower catalog inventory.

Other Current Assets and Other Assets

Other current assets increased to \$270 million as of June 30, 2010, from \$239 million as of March 31, 2010, while other assets increased to \$177 million as of June 30, 2010 from \$175 million as of March 31, 2010. Other current assets and other assets combined, increased by \$33 million primarily due to an increase in prepaid royalties.

Accounts Payable

Accounts payable decreased to \$55 million as of June 30, 2010, from \$91 million as of March 31, 2010, primarily due to lower marketing and advertising and inventory purchases.

Accrued and Other Current Liabilities

Our accrued and other current liabilities decreased to \$620 million as of June 30, 2010 from \$717 million as of March 31, 2010. The \$97 million decrease was primarily due to (1) a \$61 million decrease in accrued incentive-based compensation, (2) an \$11 million decrease in Value-Added Tax payables, and (3) an \$8 million decrease in accrued restructuring primarily from our fiscal 2010 restructuring.

Deferred Income Taxes, Net

Our net deferred income tax asset position decreased by \$4 million as of June 30, 2010 as compared to March 31, 2010, primarily due to foreign currency translation adjustments.

Financial Condition

We believe that cash, cash equivalents, short-term investments, marketable equity securities, cash generated from operations and available financing facilities will be sufficient to meet our operating requirements for at least the next twelve months, including working capital requirements, capital expenditures and, potentially, future acquisitions or strategic investments. We may choose at any time to raise additional capital to strengthen our financial position, facilitate expansion, and pursue strategic acquisitions and investments or to take advantage of business opportunities as they arise. There can be no assurance, however, that such additional capital will be available to us on favorable terms, if at all, or that it will not result in substantial dilution to our existing stockholders.

As of June 30, 2010, approximately \$601 million of our cash, cash equivalents, and short-term investments and \$122 million of our marketable equity securities was domiciled in foreign tax jurisdictions. While we have no plans to repatriate these funds to the United States in the short term, if we choose to do so, we would be required to accrue and pay additional taxes on any portion of the repatriation where no United States income tax had been previously provided.

We have a shelf registration statement on Form S-3 on file with the SEC. This shelf registration statement, which includes a base prospectus, allows us at any time to offer any combination of securities described in the prospectus in one or more offerings. Unless otherwise specified in a prospectus supplement accompanying the base prospectus, we would use the net proceeds from the sale of any securities offered pursuant to the shelf registration statement for general corporate purposes, including for working capital, financing capital expenditures, research and development, marketing and distribution efforts and, if opportunities arise, for acquisitions or strategic alliances. Pending such uses, we may invest the net proceeds in interest-bearing securities. In addition, we may conduct concurrent or other financings at any time.

Table of Contents

Our ability to maintain sufficient liquidity could be affected by various risks and uncertainties including, but not limited to, those related to customer demand and acceptance of our products, our ability to collect our accounts receivable as they become due, successfully achieving our product release schedules and attaining our forecasted sales objectives, the impact of acquisitions and other strategic transactions in which we may engage, the impact of competition, economic conditions in the United States and abroad, the seasonal and cyclical nature of our business and operating results, risks of product returns and the other risks described in the Risk Factors section, included in Part II, Item 1A of this report.

Contractual Obligations and Commercial Commitments

Development, Celebrity, League and Content Licenses: Payments and Commitments

The products we produce in our studios are designed and created by our employee designers, artists, software programmers and by non-employee software developers (independent artists or third-party developers). We typically advance development funds to the independent artists and third-party developers during development of our games, usually in installment payments made upon the completion of specified development milestones. Contractually, these payments are generally considered advances against subsequent royalties on the sales of the products. These terms are set forth in written agreements entered into with the independent artists and third-party developers.

In addition, we have certain celebrity, league and content license contracts that contain minimum guarantee payments and marketing commitments that may not be dependent on any deliverables. Celebrities and organizations with whom we have contracts include: FIFA, FIFPRO Foundation, FAPL (Football Association Premier League Limited), and DFL Deutsche Fußball Liga GmbH (German Soccer League) (professional soccer); National Basketball Association (professional basketball); PGA TOUR and Tiger Woods (professional golf); National Hockey League and NHL Players Association (professional hockey); Warner Bros. (Harry Potter); National Football League Properties, PLAYERS Inc., and Red Bear Inc. (professional football); Collegiate Licensing Company (collegiate football and basketball); ESPN (content in EA SPORTS games); Hasbro, Inc. (most of Hasbro's toy and game intellectual properties); and the Estate of Robert Ludlum (Robert Ludlum novels and films). These developer and content license commitments represent the sum of (1) the cash payments due under non-royalty-bearing licenses and services agreements and (2) the minimum guaranteed payments and advances against royalties due under royalty-bearing licenses and services agreements, the majority of which are conditional upon performance by the counterparty. These minimum guarantee payments and any related marketing commitments are included in the table below.

The following table summarizes our minimum contractual obligations as of June 30, 2010, and the effect we expect them to have on our liquidity and cash flow in future periods (in millions):

Fiscal Year Ending March 31,	Contractual Obligations				Total
	Leases (a)	Developer/ Licensor Commitments (b)	Marketing	Other Purchase Obligations	
2011 (remaining nine months)	\$ 37	\$ 189	\$ 74	\$ 2	\$ 302
2012	39	280	51		370
2013	32	196	53		281
2014	23	29	41		93
2015	18	28	15		61
Thereafter	21	612	92		725
Total	\$ 170	\$ 1,334	\$ 326	\$ 2	\$ 1,832

(a) See discussion on operating leases in the Off-Balance Sheet Commitments section below for additional information. Lease commitments have not been reduced by minimum sub-lease rentals for unutilized office space resulting from our reorganization activities of approximately \$13 million due in the future under non-cancelable sub-leases.

(b)

Edgar Filing: ELECTRONIC ARTS INC. - Form 10-Q

Developer/licensor commitments include \$7 million of commitments to developers or licensors that have been recorded in current and long-term liabilities and a corresponding amount in current and long-term assets in our Condensed Consolidated Balance Sheet as of June 30, 2010 because payment is not contingent upon performance by the developer or licensor.

Table of Contents

The amounts represented in the table above reflect our minimum cash obligations for the respective fiscal years, but do not necessarily represent the periods in which they will be expensed in our Condensed Consolidated Financial Statements.

In addition to what is included in the table above, as of June 30, 2010, we had a liability for unrecognized tax benefits and an accrual for the payment of related interest totaling \$264 million, of which approximately \$35 million is offset by prior cash deposits to tax authorities for issues pending resolution. For the remaining liability, we are unable to make a reasonably reliable estimate of when cash settlement with a taxing authority will occur.

In connection with our acquisition of Playfish in fiscal year 2010, we may be required to pay additional variable cash consideration that is contingent upon the achievement of certain performance milestones through December 31, 2011. The additional consideration is limited to a maximum of \$100 million.

OFF-BALANCE SHEET COMMITMENTS

Lease Commitments

As of June 30, 2010, we leased certain of our current facilities, furniture and equipment under non-cancelable operating lease agreements. We were required to pay property taxes, insurance and normal maintenance costs for certain of these facilities and any increases over the base year of these expenses on the remainder of our facilities.

Director Indemnity Agreements

We entered into indemnification agreements with each of the members of our Board of Directors at the time they joined the Board to indemnify them to the extent permitted by law against any and all liabilities, costs, expenses, amounts paid in settlement and damages incurred by the directors as a result of any lawsuit, or any judicial, administrative or investigative proceeding in which the directors are sued or charged as a result of their service as members of our Board of Directors.

Table of Contents**Item 3. Quantitative and Qualitative Disclosures About Market Risk****MARKET RISK**

We are exposed to various market risks, including changes in foreign currency exchange rates, interest rates and market prices, which have experienced significant volatility in light of the global economic downturn. Market risk is the potential loss arising from changes in market rates and market prices. We employ established policies and practices to manage these risks. Foreign currency option and forward contracts are used to hedge anticipated exposures or mitigate some existing exposures subject to foreign exchange risk as discussed below. While we do not hedge our short-term investment portfolio, we protect our short-term investment portfolio against different market risks, including interest rate risk as discussed below. Our cash and cash equivalents portfolio consists of highly liquid investments with insignificant interest rate risk and original or remaining maturities of three months or less at the time of purchase. We also do not currently hedge our market price risk relating to our marketable equity securities and we do not enter into derivatives or other financial instruments for trading or speculative purposes.

Foreign Currency Exchange Rate Risk

Cash Flow Hedging Activities. From time to time, we hedge a portion of our foreign currency risk related to forecasted foreign-currency-denominated sales and expense transactions by purchasing foreign currency option contracts that generally have maturities of 15 months or less. These transactions are designated and qualify as cash flow hedges. The derivative assets associated with our hedging activities are recorded at fair value in other current assets in our Condensed Consolidated Balance Sheets. The effective portion of gains or losses resulting from changes in fair value of these hedges is initially reported, net of tax, as a component of accumulated other comprehensive income in stockholders' equity. The gross amount of the effective portion of gains or losses resulting from changes in fair value of these hedges is subsequently reclassified into net revenue 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 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 income, net, in our Condensed Consolidated Statements of Operations. In the event that the underlying forecasted transactions do not occur, or it becomes remote that they will occur, within the defined hedge period, the gains or losses on the related cash flow hedges are reclassified from accumulated other comprehensive income to interest and other income, net, in our Condensed Consolidated Statements of Operations. During the reporting periods all forecasted transactions occurred and, therefore, there were no such gains or losses reclassified into interest and other income, net. Our hedging programs are designed to reduce, but do not entirely eliminate the impact of currency exchange rate movements in net revenue and research and development expenses. As of June 30, 2010, we had foreign currency option contracts to purchase approximately \$13 million in foreign currency and to sell approximately \$166 million of foreign currencies. All of the foreign currency option contracts outstanding as of June 30, 2010 will mature in the next 12 months. As of March 31, 2010, we had foreign currency option contracts to purchase approximately \$18 million in foreign currency and to sell approximately \$30 million of foreign currencies. As of June 30, 2010 and March 31, 2010, these foreign currency option contracts outstanding had a total fair value of \$4 million and \$2 million, respectively, and are included in other current assets.

Balance Sheet Hedging Activities. We use foreign currency forward contracts to mitigate foreign currency risk associated with foreign-currency-denominated monetary assets and liabilities, primarily intercompany receivables and payables. The foreign currency forward contracts generally have a contractual term of three months or less and are transacted near month-end. Our foreign currency forward contracts are not designated as hedging instruments, and are accounted for as derivatives whereby the fair value of the contracts is reported as other current assets or accrued and other current liabilities on our Condensed Consolidated Balance Sheets, and gains and losses resulting from changes in the fair value are reported in interest and other income, net, in our Condensed Consolidated Statements of Operations. The gains and losses on these foreign currency forward contracts generally offset the gains and losses on the underlying foreign-currency-denominated monetary assets and liabilities, which are also reported in interest and other income, net, in our Condensed Consolidated Statements of Operations. In certain cases, the amount of such gains and losses will significantly differ from the amount of gains and losses recognized on the underlying foreign-currency-denominated monetary asset or liability, in which case our results will be impacted. As of June 30, 2010, we had foreign currency forward contracts to purchase and sell approximately \$233 million in foreign currencies. Of this amount, \$79 million represented contracts to sell foreign currencies in exchange for U.S. dollars, \$148 million to purchase foreign currencies in exchange for U.S. dollars and \$6 million to sell foreign currency in exchange for British pounds sterling. As of March 31, 2010, we had foreign currency forward contracts to purchase and sell approximately \$431 million in foreign currencies. Of this amount, \$293 million represented contracts to sell foreign currencies in exchange for U.S. dollars, \$127 million to purchase foreign currency in exchange for U.S. dollars and \$11 million to sell foreign currency in exchange for British pounds sterling. The fair value of our foreign currency forward contracts was immaterial as of June 30, 2010 and March 31, 2010.

Table of Contents

We believe the counterparties to these foreign currency forward and foreign currency option contracts are creditworthy multinational commercial banks. While we believe the risk of counterparty nonperformance is not material, the disruption in the global financial markets has impacted some of the financial institutions with which we do business. A sustained decline in the financial stability of financial institutions as a result of the disruption in the financial markets could affect our ability to secure credit-worthy counterparties for our foreign currency hedging programs.

Notwithstanding our efforts to mitigate some foreign currency exchange rate risks, there can be no assurance that our hedging activities will adequately protect us against the risks associated with foreign currency fluctuations. As of June 30, 2010, a hypothetical adverse foreign currency exchange rate movement of 10 percent or 15 percent would have resulted in potential declines in the fair value of the premiums on our foreign currency option contracts used in cash flow hedging of \$3 million and \$4 million, respectively. As of June 30, 2010, a hypothetical adverse foreign currency exchange rate movement of 10 percent or 15 percent would have resulted in potential losses on our foreign currency forward contracts used in balance sheet hedging of \$21 million and \$32 million, respectively. This sensitivity analysis assumes a parallel adverse shift of all foreign currency exchange rates against the U.S. dollar; however, all foreign currency exchange rates do not always move in such manner and actual results may differ materially.

Interest Rate Risk

Our exposure to market risk for changes in interest rates relates primarily to our short-term investment portfolio. We manage our interest rate risk by maintaining an investment portfolio generally consisting of debt instruments of high credit quality and relatively short maturities. However, because short-term investments mature relatively quickly and are required to be reinvested at the then current market rates, interest income on a portfolio consisting of short-term investments is more subject to market fluctuations than a portfolio of longer term investments. Additionally, the contractual terms of the investments do not permit the issuer to call, prepay or otherwise settle the investments at prices less than the stated par value. Our investments are held for purposes other than trading. Also, we do not use derivative financial instruments in our short-term investment portfolio.

As of June 30, 2010 and March 31, 2010, our short-term investments were classified as available-for-sale securities and, consequently, were recorded at fair market value with unrealized gains or losses resulting from changes in fair value reported as a separate component of accumulated other comprehensive income, net of any tax effects, in stockholders' equity. Our portfolio of short-term investments consisted of the following investment categories, summarized by fair value as of June 30, 2010 and March 31, 2010 (in millions):

	As of June 30, 2010	As of March 31, 2010
Corporate bonds	\$ 254	\$ 233
U.S. agency securities	123	115
U.S. Treasury securities	96	83
Commercial paper	7	1
Total short-term investments	\$ 480	\$ 432

Notwithstanding our efforts to manage interest rate risks, there can be no assurance that we will be adequately protected against risks associated with interest rate fluctuations. At any time, a sharp change in interest rates could have a significant impact on the fair value of our investment portfolio. The following table presents the hypothetical changes in fair value in our short-term investment portfolio as of June 30, 2010, arising from potential changes in interest rates. The modeling technique estimates the change in fair value from immediate hypothetical parallel shifts in the yield curve of plus or minus 50 basis points (BPS), 100 BPS, and 150 BPS.

Table of Contents

(In millions)	Valuation of Securities Given an Interest Rate Decrease of X Basis Points			Fair Value as of June 30, 2010	Valuation of Securities Given an Interest Rate Increase of X Basis Points		
	(150 BPS)	(100 BPS)	(50 BPS)		50 BPS	100 BPS	150 BPS
Corporate bonds	\$ 258	\$ 257	\$ 255	\$ 254	\$ 252	\$ 251	\$ 249
U.S. agency securities	125	125	124	123	123	122	122
U.S. Treasury securities	99	98	97	96	95	95	94
Commercial paper	7	7	7	7	7	7	7
Total short-term investments	\$ 489	\$ 487	\$ 483	\$ 480	\$ 477	\$ 475	\$ 472

Market Price Risk

The fair value of our marketable equity securities in publicly traded companies is subject to market price volatility and foreign currency risk for investments denominated in foreign currencies. As of June 30, 2010 and March 31, 2010, our marketable equity securities were classified as available-for-sale securities and, consequently, were recorded in our Condensed Consolidated Balance Sheets at fair market value with unrealized gains or losses resulting from changes in fair value reported as a separate component of accumulated other comprehensive income, net of any tax effects, in stockholders' equity. The fair value of our marketable equity securities as of June 30, 2010 and March 31, 2010 was \$193 million and \$291 million, respectively.

Our marketable equity securities have been, and may continue to be, adversely impacted by volatility in the public stock markets. At any time, a sharp change in market prices in our investments in marketable equity securities could have a significant impact on the fair value of our investments. The following table presents hypothetical changes in the fair value of our marketable equity securities as of June 30, 2010, arising from changes in market prices of plus or minus 25 percent, 50 percent and 75 percent.

(In millions)	Valuation of Securities Given an X Percentage Decrease in Each Stock's Market Price			Fair Value as of June 30, 2010	Valuation of Securities Given an X Percentage Increase in Each Stock's Market Price		
	(75)%	(50)%	(25)%		25%	50%	75%
Marketable equity securities	\$ 48	\$ 97	\$ 145	\$ 193	\$ 241	\$ 290	\$ 338

Table of Contents

Item 4. Controls and Procedures

Definition and limitations of disclosure controls

Our disclosure controls and procedures (as defined in Rules 13a-15(e) and 15d-15(e) under the Securities Exchange Act of 1934, as amended (the Exchange Act)) are controls and other procedures that are designed to ensure that information required to be disclosed in our reports filed under the Exchange Act, such as this report, is recorded, processed, summarized and reported within the time periods specified in the SEC's rules and forms. Disclosure controls and procedures are also designed to ensure that such information is accumulated and communicated to our management, including the Chief Executive Officer and Chief Financial Officer, as appropriate to allow timely decisions regarding required disclosure. Our management evaluates these controls and procedures on an ongoing basis.

There are inherent limitations to the effectiveness of any system of disclosure controls and procedures. These limitations include the possibility of human error, the circumvention or overriding of the controls and procedures and reasonable resource constraints. In addition, because we have designed our system of controls based on certain assumptions, which we believe are reasonable, about the likelihood of future events, our system of controls may not achieve its desired purpose under all possible future conditions. Accordingly, our disclosure controls and procedures provide reasonable assurance, but not absolute assurance, of achieving their objectives.

Evaluation of disclosure controls and procedures

Our Chief Executive Officer and our Chief Financial Officer, after evaluating the effectiveness of our disclosure controls and procedures, believe that as of the end of the period covered by this report, our disclosure controls and procedures were effective in providing the requisite reasonable assurance that material information required to be disclosed in the reports that we file or submit under the Exchange Act is recorded, processed, summarized and reported within the time periods specified in the SEC's rules and forms, and is accumulated and communicated to our management, including our Chief Executive Officer and Chief Financial Officer, as appropriate to allow timely decisions regarding the required disclosure.

Changes in internal control over financial reporting

There has been no change in our internal control over financial reporting identified in connection with our evaluation that occurred during the three months ended June 30, 2010 that has materially affected or is reasonably likely to materially affect our internal control over financial reporting.

Table of Contents

PART II OTHER INFORMATION

Item 1. Legal Proceedings

We are subject to claims and litigation arising in the ordinary course of business. We do not believe that any liability from any reasonably foreseeable disposition of such claims and litigation, individually or in the aggregate, would have a material adverse effect on our Condensed Consolidated Financial Statements.

Item 1A: Risk Factors

Our business is subject to many risks and uncertainties, which may affect our future financial performance. If any of the events or circumstances described below occurs, our business and financial performance could be harmed, our actual results could differ materially from our expectations and the market value of our stock could decline. The risks and uncertainties discussed below are not the only ones we face. There may be additional risks and uncertainties not currently known to us or that we currently do not believe are material that may harm our business and financial performance.

Our business is highly dependent on the success and availability of video game hardware systems manufactured by third parties, as well as our ability to develop commercially successful products for these systems.

We derive most of our revenue from the sale of products for play on video game hardware systems (which we also refer to as "platforms") manufactured by third parties, such as Sony's PLAYSTATION 3, Microsoft's Xbox 360 and Nintendo's Wii. The success of our business is driven in large part by the commercial success and adequate supply of these video game hardware systems, our ability to accurately predict which systems will be successful in the marketplace, and our ability to develop commercially successful products for these systems. We must make product development decisions and commit significant resources well in advance of anticipated product ship dates. A platform for which we are developing products may not succeed or may have a shorter life cycle than anticipated. If consumer demand for the systems for which we are developing products is lower than our expectations, our revenue will suffer, we may be unable to fully recover the investments we have made in developing our products, and our financial performance will be harmed. Alternatively, a system for which we have not devoted significant resources could be more successful than we had initially anticipated, causing us to miss out on meaningful revenue opportunities.

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

Our business is highly seasonal, with the highest levels of consumer demand and a significant percentage of our sales occurring in the December quarter. In addition, we seek to release many of our products in conjunction with specific events, such as the release of a related movie or the beginning of a sports season or major sporting event. If we miss these key selling periods for any reason, including product delays or delayed introduction of a new platform for which we have developed products, our sales will suffer disproportionately. Likewise, if a key event to which our product release schedule is tied were to be delayed or cancelled, our sales would also suffer disproportionately. Our ability to meet product development schedules is affected by a number of factors, including the creative processes involved, the coordination of large and sometimes geographically dispersed development teams required by the increasing complexity of our products and the platforms for which they are developed, and the need to fine-tune our products prior to their release. We have experienced development delays for our products in the past, which caused us to push back release dates. In the future, any failure to meet anticipated production or release schedules would likely result in a delay of revenue and/or possibly a significant shortfall in our revenue, increase our development expense, harm our profitability, and cause our operating results to be materially different than anticipated.

Our business is intensely competitive and hit driven. If we do not deliver hit products and services or if consumers prefer our competitors' products or services over our own, our operating results could suffer.

Competition in our industry is intense and we expect new competitors to continue to emerge in the United States and abroad. While many new products and services are regularly introduced, only a relatively small number of hit titles accounts for a significant portion of total revenue in our industry. We find that driving hit titles often requires large marketing budgets and media spend. We may not recover the investments that we make in marketing and advertising on certain products and that could harm our profitability. Hit products or services offered by our competitors may take a larger share of consumer spending than we anticipate, which could cause revenue generated from our products and services to fall below expectations. If our competitors develop and market more successful products or services, offer competitive products or services at lower price points or based on payment models perceived as offering a better value proposition (such as pay-for-play or subscription-based models), or if we do not continue to develop consistently high-quality and well-received products and services, our revenue, margins, and profitability will

decline.

Table of Contents

Our adoption of new business models could fail to produce our desired financial returns.

We are actively seeking to monetize the game properties that we publish through a variety of new platforms and business models, including online distribution, micro-transactions, and subscription services. Forecasting our revenues and profitability for these new business models is inherently uncertain and volatile. Our actual revenues and profits for these businesses may be significantly greater or less than our forecasts. Additionally, these new business models could fail for one or more of our titles, resulting in the loss of our investment in the development and infrastructure needed to support these new business models, and the opportunity cost of diverting management and financial resources away from more successful businesses.

If our marketing and advertising efforts fail to resonate with our customers, our business and operating results could be adversely affected.

Our products are marketed worldwide through a diverse spectrum of advertising and promotional programs such as television and online advertising, print advertising, retail merchandising, website development and event sponsorship. Our ability to sell our products and services is dependent in part upon the success of these programs. If the marketing for our products and services fail to resonate with our customers, particularly during the critical holiday season or during other key selling periods, or if advertising rates or other media placement costs increase, these factors could have a material adverse impact on our business and operating results.

Uncertainty and adverse changes in the economy could have a material adverse impact on our business and operating results.

As a result of the national and global economic downturn, overall consumer spending has declined and retailers globally have taken a more conservative stance in ordering game inventory. The decrease in discretionary consumer spending contributed to the decline in the demand for our products during the 2009 holiday selling season. Continued economic distress, which may result in a further decrease in demand for our products, particularly during key product launch windows, could have a material adverse impact on our operating results and financial condition. Uncertainty and adverse changes in the economy could also increase the risk of material losses on our investments, increase costs associated with developing and publishing our products, increase the cost and decrease the availability of sources of financing, and increase our exposure to material losses from bad debts, any of which could have a material adverse impact on our financial condition and operating results. If we experience further deterioration in our market capitalization or our financial performance, we could be required to recognize significant impairment charges in future periods.

Our business is subject to currency fluctuations.

International sales are a fundamental part of our business. For the three months ended June 30, 2010, international net revenue comprised 45 percent of our total net revenue. We expect international sales to continue to account for a significant portion of our total net revenue. Such sales may be subject to unexpected regulatory requirements, tariffs and other barriers. Additionally, foreign sales are primarily made in local currencies, which may fluctuate against the U.S. dollar. In addition, our foreign investments and our cash and cash equivalents denominated in foreign currencies are subject to currency fluctuations. We use foreign currency forward contracts to mitigate some foreign currency risk associated with foreign currency denominated monetary assets and liabilities (primarily certain intercompany receivables and payables) to a limited extent and foreign currency option contracts to hedge foreign currency forecasted transactions (primarily related to a portion of the revenue and expenses denominated in foreign currency generated by our operational subsidiaries). However, these activities are limited in the protection they provide us from foreign currency fluctuations and can themselves result in losses. The disruption in the global financial markets has also impacted many of the financial institutions with which we do business. A sustained decline in the financial stability of financial institutions as a result of the disruption in the financial markets could negatively impact our treasury operations, including our ability to secure credit-worthy counterparties for our foreign currency hedging programs. Accordingly, our results of operations, including our reported net revenue, operating expenses and net income, and financial condition can be adversely affected by unfavorable foreign currency fluctuations, especially the Euro, British pound sterling and Canadian dollar.

Table of Contents

Volatility in the capital markets may adversely impact the value of our investments and could cause us to recognize significant impairment charges in our operating results.

Our portfolio of short-term investments and marketable equity securities is subject to volatility in the capital markets and to national and international economic conditions. In particular, our international investments can be subject to fluctuations in foreign currency and our short-term investments are susceptible to changes in short-term interest rates. These investments are also impacted by declines in value attributable to the credit-worthiness of the issuer. From time to time, we may liquidate some or all of our short-term investments or marketable equity securities to fund operational needs or other activities, such as capital expenditures, strategic investments or business acquisitions, or for other purposes. If we were to liquidate these short-term investments at a time when they were worth less than what we had originally purchased them for, or if the obligor were unable to pay the full amount at maturity, we could incur a significant loss. Similarly, we hold marketable equity securities, which have been and may continue to be adversely impacted by price and trading volume volatility in the public stock markets. We could be required to recognize impairment charges on the securities held by us and/or we may realize losses on the sale of these securities, all of which could have an adverse effect on our financial condition and results of operations.

The majority of our sales are made to a relatively small number of key customers. If these customers reduce their purchases of our products or become unable to pay for them, our business could be harmed.

During the three months ended June 30, 2010, approximately 64 percent of our North American sales were made to our top ten customers. In Europe, our top ten customers accounted for approximately 40 percent of our sales in that territory during the three months ended June 30, 2010. Worldwide, we had direct sales to two customers, GameStop Corp. and Wal-Mart Stores Inc., which represented approximately 14 percent and 11 percent, respectively, of total net revenue for the three months ended June 30, 2010. As a result of the economic downturn, retailers globally continue to take a more conservative stance in ordering game inventory. Though our products are available to consumers through a variety of retailers, the concentration of our sales in one, or a few, large customers could lead to a short-term disruption in our sales if one or more of these customers significantly reduced their purchases or ceased to carry our products, and could make us more vulnerable to collection risk if one or more of these large customers became unable to pay for our products or declared bankruptcy. Additionally, our receivables from these large customers increase significantly in the December quarter as they make purchases in anticipation of the holiday selling season. Also, having such a large portion of our total net revenue concentrated in a few customers could reduce our negotiating leverage with these customers. If one or more of our key customers experience deterioration in their business, or become unable to obtain sufficient financing to maintain their operations, our business could be harmed.

Sales of used video game products could lower our sales of new video games.

Certain of our retail customers sell used video games. Used video game sales have been growing in North America, and are emerging in Europe. Used video games are generally priced lower than new video games and the margins on used games sales are generally greater for retailers than the margins on new game sales. We do not receive revenue from used video game sales. Sales of used video games may negatively impact our sales and profitability, and may continue to do so, to a greater or lesser extent, in the future.

Our industry is cyclical, driven by the periodic introduction of new video game hardware systems. As we continue to move through the current cycle, our industry growth may slow down and as a result, our operating results may be difficult to predict.

Video game hardware systems have historically had a life cycle of four to six years, which causes the video game software market to be cyclical as well. The current cycle began with Microsoft's launch of the Xbox 360 in 2005, and continued in 2006 when Sony and Nintendo launched their next-generation systems, the PLAYSTATION 3 and the Wii, respectively. Sales of software designed for these hardware systems represent the majority of our revenue, so our growth and success is highly correlated to sales of video game hardware systems. While there are indications that this current cycle may be extended longer than prior cycles in part, due to the growth of online services and content, the greater graphic and processing power of the current generation hardware, and the introduction of new peripherals, growth in the installed base of the current generation of video game systems is likely to slow down in the coming years. This slow-down in sales of video game players may cause a corresponding slow-down in the growth of sales of video game software, which could significantly affect our operating results.

Technology changes rapidly in our business and if we fail to anticipate or successfully implement new technologies in our games, the quality, timeliness and competitiveness of our products and services will suffer.

Rapid technology changes in our industry require us to anticipate, sometimes years in advance, which technologies we must implement and take advantage of in order to make our products and services competitive in the market. Therefore, we usually start our product development with a range of technical development goals that we hope to be able to achieve. We may not be

Table of Contents

able to achieve these goals, or our competition may be able to achieve them more quickly and effectively than we can. In either case, our products and services may be technologically inferior to our competitors, less appealing to consumers, or both. If we cannot achieve our technology goals within the original development schedule of our products and services, then we may delay their release until these technology goals can be achieved, which may delay or reduce revenue and increase our development expenses. Alternatively, we may increase the resources employed in research and development in an attempt to accelerate our development of new technologies, either to preserve our product or service launch schedule or to keep up with our competition, which would increase our development expenses.

The video game hardware manufacturers are among our chief competitors and frequently control the manufacturing of and/or access to our video game products. If they do not approve our products, we will be unable to ship to our customers.

Our agreements with hardware licensors (such as Sony for the PLAYSTATION 3, Microsoft for the Xbox 360, and Nintendo for the Wii) typically give significant control to the licensor over the approval and manufacturing of our products, which could, in certain circumstances, leave us unable to get our products approved, manufactured and shipped to customers. These hardware licensors are also among our chief competitors. Generally, control of the approval and manufacturing process by the hardware licensors increases both our manufacturing lead times and costs as compared to those we can achieve independently. While we believe that our relationships with our hardware licensors are currently good, the potential for these licensors to delay or refuse to approve or manufacture our products exists. Such occurrences would harm our business and our financial performance.

We also require compatibility code and the consent of Sony, Microsoft and Nintendo in order to include online capabilities in our products for their respective platforms and to digitally distribute our products through their proprietary networks. As online capabilities for video game systems become more significant, Sony, Microsoft and Nintendo could restrict the manner in which we provide online capabilities for our products. They may also restrict the number of products that we may distribute digitally on their networks. If Sony, Microsoft or Nintendo refuse to approve our products with online capabilities, restrict our digital download offerings on their proprietary networks, or significantly impact the financial terms on which these services are offered to our customers, our business could be harmed.

The video game hardware manufacturers set the royalty rates and other fees that we must pay to publish games for their platforms, and therefore have significant influence on our costs. If one or more of these manufacturers change their fee structure, our profitability will be materially impacted.

In order to publish products for a video game system such as the Xbox 360, PLAYSTATION 3 or Wii, we must take a license from Microsoft, Sony and Nintendo, respectively, which gives these companies the opportunity to set the fee structure that we must pay in order to publish games for that platform. Similarly, these companies have retained the flexibility to change their fee structures, or adopt different fee structures for online purchases of games, online gameplay and other new features for their consoles. The control that hardware manufacturers have over the fee structures for their platforms and online access could adversely impact our costs, profitability and margins. Because publishing products for video game systems is the largest portion of our business, any increase in fee structures would significantly harm our ability to generate profits.

If we are unable to maintain or acquire licenses to include intellectual property owned by others in our games, or to maintain or acquire the rights to publish or distribute games developed by others, we will sell fewer hit titles and our revenue, profitability and cash flows will decline. Competition for these licenses may make them more expensive and reduce our profitability.

Many of our products are based on or incorporate intellectual property owned by others. For example, our EA SPORTS products include rights licensed from major sports leagues and players' associations. Similarly, many of our other hit franchises, such as Harry Potter, are based on key film and literary licenses and our Hasbro products are based on a license for these key toy and game properties. In addition, some of our most successful products in fiscal years 2009 and 2010, the Rock Band and Left 4 Dead series, were products for which we have distribution rights. Competition for these licenses and rights is intense. If we are unable to maintain these licenses and rights or obtain additional licenses or rights with significant commercial value, our revenues, profitability and cash flows will decline significantly. Competition for these licenses may also drive up the advances, guarantees and royalties that we must pay to licensors and developers, which could significantly increase our costs and reduce our profitability.

Table of Contents

Our business is subject to risks generally associated with the entertainment industry, any of which could significantly harm our operating results.

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 cannot necessarily be predicted.

If we do not continue to attract and retain key personnel, we will be unable to effectively conduct our business.

The market for technical, creative, marketing and other personnel essential to the development and marketing of our products and management of our businesses is extremely competitive. Our leading position within the interactive entertainment industry makes us a prime target for recruiting of executives and key creative talent. If we cannot successfully recruit and retain the employees we need, or replace key employees following their departure, our ability to develop and manage our business will be impaired.

Acquisitions, investments and other strategic transactions could result in operating difficulties, dilution to our investors and other negative consequences.

We have engaged in, evaluated, and expect to continue to engage in and evaluate, a wide array of potential strategic transactions, including (1) acquisitions of companies, businesses, intellectual properties, and other assets, (2) minority investments in strategic partners, and (3) investments in new interactive entertainment businesses (for example, online and mobile games). Any of these strategic transactions could be material to our financial condition and results of operations. Although we regularly search for opportunities to engage in strategic transactions, we may not be successful in identifying suitable opportunities. We may not be able to consummate potential acquisitions or investments or an acquisition or investment we do consummate may not enhance our business or may decrease rather than increase our earnings. The process of acquiring and integrating a company or business, or successfully exploiting acquired intellectual property or other assets, could divert a significant amount of resources, as well as our management's time and focus and may create unforeseen operating difficulties and expenditures, particularly for a large acquisition. Additional risks and variations of the foregoing risks we face include:

The need to implement or remediate controls, procedures and policies appropriate for a public company in an acquired company that, prior to the acquisition, lacked these controls, procedures and policies,

Cultural challenges associated with integrating employees from an acquired company or business into our organization,

Retaining key employees and maintaining the key business and customer relationships of the businesses we acquire,

The need to integrate an acquired company's accounting, management information, human resource and other administrative systems to permit effective management and timely reporting,

The possibility that we will not discover important facts during due diligence that could have a material adverse impact on the value of the businesses we acquire,

Potential impairment charges incurred to write down the carrying amount of intangible assets generated as a result of an acquisition,

Litigation or other claims in connection with, or inheritance of claims or litigation risks as a result of, an acquisition, including claims from terminated employees, customers or other third parties,

Significant accounting charges resulting from the completion and integration of a sizeable acquisition and increased capital expenditures,

Significant acquisition-related accounting adjustments, particularly relating to an acquired company's deferred revenue, that may cause reported revenue and profits of the combined company to be lower than the sum of their stand-alone revenue and profits,

The possibility that the combined company would not achieve the expected benefits, including any anticipated operating and product synergies, of the acquisition as quickly as anticipated,

Table of Contents

The possibility that the costs of, or operational difficulties arising from, an acquisition would be greater than anticipated,

To the extent that we engage in strategic transactions outside of the United States, we face additional risks, including risks related to integration of operations across different cultures and languages, currency risks and the particular economic, political and regulatory risks associated with specific countries, and

The possibility that a change of control of a company we acquire triggers a termination of contractual or intellectual property rights important to the operation of its business.

Future acquisitions and investments could also involve the issuance of our equity and equity-linked securities (potentially diluting our existing stockholders), the incurrence of debt, contingent liabilities or amortization expenses, write-offs of goodwill, intangibles, or acquired in-process technology, or other increased cash and non-cash expenses, such as stock-based compensation. Any of the foregoing factors could harm our financial condition or prevent us from achieving improvements in our financial condition and operating performance that could have otherwise been achieved by us on a stand-alone basis. Our stockholders may not have the opportunity to review, vote on or evaluate future acquisitions or investments.

We may be subject to claims of infringement of third-party intellectual property rights, which could harm our business.

From time to time, third parties may assert claims against us relating to patents, copyrights, trademarks, personal publicity rights, or other intellectual property rights to technologies, products or delivery/payment methods that are important to our business. Although we believe that we make reasonable efforts to ensure that our products do not violate the intellectual property rights of others, it is possible that third parties still may claim infringement. For example, we may be subject to intellectual property infringement claims from certain individuals and companies who have acquired patent portfolios for the sole purpose of asserting such claims against other companies. In addition, many of our products are highly realistic and feature materials that are based on real world examples, which may be the subject of intellectual property infringement claims of others. From time to time, we receive communications from third parties regarding such claims. Existing or future infringement claims against us, whether valid or not, may be time consuming and expensive to defend. Such claims or litigations could require us to pay damages and other costs, stop selling the affected products, redesign those products to avoid infringement, or obtain a license, all of which could be costly and harm our business. In addition, many patents have been issued that may apply to potential new modes of delivering, playing or monetizing game software products and services, such as those that we produce or would like to offer in the future. We may discover that future opportunities to provide new and innovative modes of game play and game delivery to consumers may be precluded by existing patents that we are unable to license on reasonable terms.

From time to time we may become involved in other legal proceedings, which could adversely affect us.

We are currently, and from time to time in the future may become, subject to legal proceedings, claims, litigation and government investigations or inquiries, which could be expensive, lengthy, and disruptive to normal business operations. In addition, the outcome of any legal proceedings, claims, litigation, investigations or inquiries may be difficult to predict and could have a material adverse effect on our business, operating results, or financial condition.

Our business is subject to increasing regulation and the adoption of proposed legislation we oppose could negatively impact our business.

Legislation is continually being introduced in the United States at the local, state and federal levels for the establishment of government mandated rating requirements or restrictions on distribution of entertainment software based on content. To date, most courts that have ruled on such legislation have ruled in a manner favorable to the interactive entertainment industry. Other countries have adopted or are considering laws regulating or mandating ratings requirements on entertainment software content and certain foreign countries already allow government censorship of entertainment software products. Adoption of government ratings system or restrictions on distribution of entertainment software based on content could harm our business by limiting the products we are able to offer to our customers and compliance with new and possibly inconsistent regulations for different territories could be costly or delay the release of our products.

As we increase the online delivery of our products and services, we are subject to a number of foreign and domestic laws and regulations that affect companies conducting business on the Internet. In addition, laws and regulations relating to user privacy, data collection and retention, content, advertising and information security have been adopted or are being considered for adoption by many countries throughout the world. The costs of compliance with these laws may increase in the future as a result of changes in interpretation. Furthermore, any failure on our part to comply with these laws or the application of these laws in an unanticipated manner may harm our business.

Table of Contents

Our products are subject to the threat of piracy and unauthorized copying.

Entertainment software piracy is a persistent problem in our industry. The growth in peer-to-peer networks and other channels to download pirated copies of our products, the increasing availability of broadband access to the Internet and the proliferation of technology designed to circumvent the protection measures used with our products all have contributed to an expansion in piracy. Though we take technical steps to make the unauthorized copying of our products more difficult, as do the manufacturers of consoles on which our games are played, these efforts may not be successful in controlling the piracy of our products.

While legal protections exist to combat piracy, preventing and curbing infringement through enforcement of our intellectual property rights may be difficult, costly and time consuming, particularly in countries where laws are less protective of intellectual property rights. Further, the scope of the legal protection of copyright and prohibitions against the circumvention of technological protection measures to protect copyrighted works are often under scrutiny by courts and governing bodies. The repeal or weakening of laws intended to combat piracy, protect intellectual property and prohibit the circumvention of technological protection measures could make it more difficult for us to adequately protect against piracy. These factors could have a negative effect on our growth and profitability in the future.

If one or more of our titles were found to contain hidden, objectionable content, our business could suffer.

Throughout the history of our industry, many video games have been designed to include certain hidden content and gameplay features that are accessible through the use of in-game cheat codes or other technological means that are intended to enhance the gameplay experience. However, in several cases, hidden content or features have been found to be included in other publishers' products by an employee who was not authorized to do so or by an outside developer without the knowledge of the publisher. From time to time, some hidden content and features have contained profanity, graphic violence and sexually explicit or otherwise objectionable material. In a few cases, the Entertainment Software Ratings Board (ESRB) has reacted to discoveries of hidden content and features by reviewing the rating that was originally assigned to the product, requiring the publisher to change the game packaging and/or fining the publisher. Retailers have on occasion reacted to the discovery of such hidden content by removing these games from their shelves, refusing to sell them, and demanding that their publishers accept them as product returns. Likewise, consumers have reacted to the revelation of hidden content by refusing to purchase such games, demanding refunds for games they have already purchased, and refraining from buying other games published by the company whose game contained the objectionable material.

We have implemented preventative measures designed to reduce the possibility of hidden, objectionable content from appearing in the video games we publish. Nonetheless, these preventative measures are subject to human error, circumvention, overriding, and reasonable resource constraints. In addition, to the extent we acquire a company without similar controls in place, the possibility of hidden, objectionable content appearing in video games developed by that company but for which we are ultimately responsible could increase. If a video game we published were found to contain hidden, objectionable content, the ESRB could demand that we recall a game and change its packaging to reflect a revised rating, retailers could refuse to sell it and demand we accept the return of any unsold copies or returns from customers, and consumers could refuse to buy it or demand that we refund their money. This could have a material negative impact on our operating results and financial condition. In addition, our reputation could be harmed, which could impact sales of other video games we sell. If any of these consequences were to occur, our business and financial performance could be significantly harmed.

If we ship defective products, our operating results could suffer.

Products such as ours are extremely complex software programs, and are difficult to develop, manufacture and distribute. We have quality controls in place to detect defects in the software, media and packaging of our products before they are released. Nonetheless, these quality controls are subject to human error, overriding, and reasonable resource constraints. Therefore, these quality controls and preventative measures may not be effective in detecting defects in our products before they have been reproduced and released into the marketplace. In such an event, we could be required to recall a product, or we may find it necessary to voluntarily recall a product, and/or scrap defective inventory, which could significantly harm our business and operating results.

Table of Contents

Breaches of our security measures and unintended disclosures of our intellectual property or our customer data could adversely affect our business.

We take measures to prevent our source code and other confidential information from unauthorized access. A security breach that results in the disclosure of our source code, other confidential assets, or pre-release software could lead to piracy of our software or otherwise compromise our product plans. When we conduct business online directly with consumers, we may be the victim of fraudulent transactions, including credit card fraud, which presents a risk to our revenues and potentially disrupts service to our customers. As we increase our online businesses, we are also collecting and storing an increasing amount of customer data, some of it personally identifiable information including credit card data. It is possible that our security controls over customer data may not prevent the improper disclosure of personally identifiable information. A security breach that leads to disclosure of customer account information (including personally identifiable information) could harm our reputation and subject us to liability under laws that protect personal data, resulting in increased costs or loss of revenue. A resulting perception that our products or services do not adequately protect the privacy of personal information could result in a loss of current or potential customers for our online offerings that require the collection of customer data.

We may experience outages and disruptions of our online services if we fail to maintain adequate operational services and supporting infrastructure.

As we increase our online products and services, we expect to continue to invest in technology services, hardware and software, including data centers, network services, storage and database technologies, to support existing services and to introduce new products and services including websites, ecommerce capabilities, online game communities and online game play services. Creating the appropriate support for online business initiatives is expensive and complex, and could result in inefficiencies or operational failures, and increased vulnerability to cyber attacks, which could diminish the quality of our products, services, and user experience. Such failures could result in damage to our reputation and loss of current and potential users, subscribers, and advertisers which could harm our business.

Changes in our tax rates or exposure to additional tax liabilities could adversely affect our earnings and financial condition.

We are subject to income taxes in the United States and in various foreign jurisdictions. Significant judgment is required in determining our worldwide provision for income taxes, and, in the ordinary course of our business, there are many transactions and calculations where the ultimate tax determination is uncertain.

We are also required to estimate what our tax obligations will be in the future. Although we believe our tax estimates are reasonable, the estimation process and applicable laws are inherently uncertain, and our estimates are not binding on tax authorities. The tax laws' treatment of software and internet-based transactions is particularly uncertain and in some cases currently applicable tax laws are ill-suited to address these kinds of transactions. Apart from an adverse resolution of these uncertainties, our effective tax rate also could be adversely affected by our profit level, by changes in our business or changes in our structure resulting from the reorganization of our business and operating structure, changes in the mix of earnings in countries with differing statutory tax rates, changes in the elections we make, changes in applicable tax laws (in the United States or foreign jurisdictions), or changes in the valuation allowance for deferred tax assets, as well as other factors. In fiscal years 2009 and 2010, we recorded a valuation allowance against most of our U.S. deferred tax assets. We expect to provide a valuation allowance on future U.S. tax benefits until we can sustain a level of profitability or until other significant positive evidence arises that suggest that these benefits are more likely than not to be realized. Further, our tax determinations are regularly subject to audit by tax authorities and developments in those audits could adversely affect our income tax provision. Should our ultimate tax liability exceed our estimates, our income tax provision and net income or loss could be materially affected.

We incur certain tax expenses that do not decline proportionately with declines in our consolidated pre-tax income or loss. As a result, in absolute dollar terms, our tax expense will have a greater influence on our effective tax rate at lower levels of pre-tax income or loss than at higher levels. In addition, at lower levels of pre-tax income or loss, our effective tax rate will be more volatile.

We are also required to pay taxes other than income taxes, such as payroll, sales, use, value-added, net worth, property and goods and services taxes, in both the United States and foreign jurisdictions. We are regularly under examination by tax authorities with respect to these non-income taxes. There can be no assurance that the outcomes from these examinations, changes in our business or changes in applicable tax rules will not have an adverse effect on our earnings and financial condition.

Table of Contents

Furthermore, as we expand our international operations, adopt new products and new distribution models, implement changes to our operating structure or undertake intercompany transactions in light of changing tax laws, expiring rulings, acquisitions and our current and anticipated business and operational requirements, our tax expense could increase.

Our reported financial results could be adversely affected by changes in financial accounting standards or by the application of existing or future accounting standards to our business as it evolves.

Our reported financial results are impacted by the accounting policies promulgated by the Securities and Exchange Commission (SEC) and national accounting standards bodies and the methods, estimates, and judgments that we use in applying our accounting policies. Policies affecting software revenue recognition have and could further significantly affect the way we account for revenue related to our products and services. We recognize all of the revenue from bundled sales (i.e., packaged goods video games that include an online service component) on a deferred basis over an estimated online service period, which we generally estimate to be six months beginning in the month after shipment. As we increase our downloadable content and add new features to our online service, our estimate of the online service period may change and we could be required to recognize revenue over a longer period of time. We expect that a significant portion of our games will be online-enabled in the future and we could be required to recognize the related revenue over an extended period of time rather than at the time of sale. In addition, our adoption of Financial Accounting Standards Board (FASB) Accounting Standards Codification (ASC) 805, *Business Combinations*, has had a material impact on our Condensed Consolidated Financial Statements for material acquisitions consummated after March 28, 2009. As we enhance, expand and diversify our business and product offerings, the application of existing or future financial accounting standards, particularly those relating to the way we account for revenue and taxes, could have a significant adverse effect on our reported results although not necessarily on our cash flows.

We rely on business partners in many areas of our business and our business may be harmed if they are unable to honor their obligations to us.

We rely on various business partners, including third-party service providers, vendors, licensing partners, development partners, and licensees, among others, in many areas of our business. In many cases, these third parties are given access to sensitive and proprietary information in order to provide services and support to our teams. These third parties may misappropriate our information and engage in unauthorized use of it. The failure of these third parties to provide adequate services and technologies, or the failure of the third parties to adequately maintain or update their services and technologies, could result in a disruption to our business operations. Further, the disruption in the financial markets and the global economic downturn may adversely affect our business partners and they may not be able to continue honoring their obligations to us. Some of our business partners are highly-leveraged or small businesses that may be particularly vulnerable in the current economic environment. Alternative arrangements and services may not be available to us on commercially reasonable terms or we may experience business interruptions upon a transition to an alternative partner or vendor. If we lose one or more significant business partners, our business could be harmed.

Our stock price has been volatile and may continue to fluctuate significantly.

The market price of our common stock historically has been, and we expect will continue to be, subject to significant fluctuations. These fluctuations may be due to factors specific to us (including those discussed in the risk factors above, as well as others not currently known to us or that we currently do not believe are material), to changes in securities analysts' earnings estimates or ratings, to our results or future financial guidance falling below our expectations and analysts' and investors' expectations, to factors affecting the entertainment, computer, software, Internet, media or electronics industries, to our ability to successfully integrate any acquisitions we may make, or to national or international economic conditions. In particular, economic downturns may contribute to the public stock markets experiencing extreme price and trading volume volatility. These broad market fluctuations have and could continue to adversely affect the market price of our common stock.

Table of Contents**Item 5. Other Information**

At our Annual Meeting of Stockholders, held on August 5, 2010, our stockholders elected the following individuals to the Board of Directors for one-year terms:

	For	Against	Abstain	Broker Non-vote
Leonard S. Coleman	140,781,688	109,942,102	754,930	30,000,317
Jeffrey T. Huber	244,454,473	6,371,007	653,240	
Gary M. Kusin	243,481,393	7,343,316	654,011	
Geraldine B. Laybourne	141,136,083	109,557,588	785,049	
Gregory B. Maffei	225,654,902	25,046,410	777,408	
Vivek Paul	244,438,945	6,380,160	659,615	
Lawrence F. Probst III	241,720,458	9,105,518	652,744	
John S. Riccitiello	220,650,148	30,175,542	653,030	
Richard A. Simonson	226,640,992	24,062,300	775,428	
Linda J. Srere	142,117,610	108,691,042	670,068	

In addition, the following matters were voted on, received the number of votes indicated in the tables below, and approved by our stockholders:

1. Amendments to our 2000 Equity Incentive Plan to (a) increase the number of shares authorized for issuance under the Equity Plan by 5.3 million shares and (b) remove the provision of the Equity Plan that provides for automatic grants to our outside directors upon appointment to the Board of Directors and annually upon re-election.

For	Against	Abstain	Broker Non-vote
198,253,912	52,303,367	921,441	

2. Amendments to our 2000 Employee Stock Purchase Plan (the ESPP) to increase the number of shares authorized under the ESPP by 2 million shares.

For	Against	Abstain	Broker Non-vote
244,706,923	6,112,905	658,892	

3. Ratification of the appointment of KPMG LLP as our independent registered public accounting firm for fiscal year 2011.

For	Against	Abstain	Broker Non-vote
277,419,141	3,363,729	696,167	

Table of Contents

Item 6. Exhibits

Exhibit Number	Title
---------------------------	--------------

The following exhibits are filed as part of, or incorporated by reference into, this report:

- | | |
|------|--|
| 15.1 | Awareness Letter of KPMG LLP, Independent Registered Public Accounting Firm. |
| 31.1 | Certification of Chief Executive Officer pursuant to Rule 13a-14(a) of the Exchange Act, as adopted pursuant to Section 302 of the Sarbanes-Oxley Act of 2002. |
| 31.2 | Certification of Executive Vice President, Chief Financial Officer pursuant to Rule 13a-14(a) of the Exchange Act, as adopted pursuant to Section 302 of the Sarbanes-Oxley Act of 2002. |

Additional exhibits furnished with this report:

- | | |
|---------|---|
| 32.1 | Certification of Chief Executive Officer pursuant to Section 906 of the Sarbanes-Oxley Act of 2002. |
| 32.2 | Certification of Executive Vice President, Chief Financial Officer pursuant to Section 906 of the Sarbanes-Oxley Act of 2002. |
| 101.INS | XBRL Instance Document. (*) |
| 101.SCH | XBRL Taxonomy Extension Schema Document. (*) |
| 101.CAL | XBRL Taxonomy Extension Calculation Linkbase Document. (*) |
| 101.DEF | XBRL Taxonomy Extension Definition Linkbase Document. (*) |
| 101.LAB | XBRL Taxonomy Extension Label Linkbase Document. (*) |
| 101.PRE | XBRL Taxonomy Extension Presentation Linkbase Document. (*) |

* XBRL information is furnished and not filed or a part of a registration statement or prospectus for purposes of sections 11 or 12 of the Securities and Exchange Act of 1933, as amended, is deemed not filed for purposes of section 18 of the Securities and Exchange Act of 1934, as amended, and otherwise is not subject to liability under these sections.

Table of Contents

SIGNATURE

Pursuant to the requirements of the Securities Exchange Act of 1934, the registrant has duly caused this report to be signed on its behalf by the undersigned thereunto duly authorized.

ELECTRONIC ARTS INC.

(Registrant)

/s/ Eric F. Brown
Eric F. Brown
Executive Vice President,

Chief Financial Officer

DATED:

August 9, 2010

Table of Contents**ELECTRONIC ARTS INC.****FORM 10-Q****FOR THE PERIOD ENDED JUNE 30, 2010****EXHIBIT INDEX**

NUMBER	EXHIBIT TITLE	INCORPORATED BY REFERENCE			FILED HEREWITH
		FORM	FILE NO.	FILING DATE	
15.1	Awareness Letter of KPMG, LLP, Independent Registered Public Accounting Firm.				X
31.1	Certification of Chief Executive Officer pursuant to Rule 13a-14(a) of the Exchange Act, as adopted pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.				X
31.2	Certification of Executive Vice President, Chief Financial Officer pursuant to Rule 13a-14(a) of the Exchange Act, as adopted pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.				X
Additional exhibits furnished with this report:					
32.1	Certification of Chief Executive Officer pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.				X
32.2	Certification of Executive Vice President, Chief Financial Officer pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.				X
101.INS	XBRL Instance Document.				X
101.SCH	XBRL Taxonomy Extension Schema Document.				X
101.CAL	XBRL Taxonomy Extension Calculation Linkbase Document.				X
101.DEF	XBRL Taxonomy Extension Definition Linkbase Document.				X
101.LAB	XBRL Taxonomy Extension Label Linkbase Document.				X
101.PRE	XBRL Taxonomy Extension Presentation Linkbase Document.				X

Pursuant to Rule 406T of Regulation S-T, these interactive data files are furnished and not filed or a part of a registration statement or prospectus for purposes of Sections 11 or 12 of the Securities Act of 1933, as amended; are deemed not filed for purposes of section 18 of the Securities Exchange Act of 1934, as amended; and otherwise are not subject to liability under these sections. We are deemed to have complied with the reporting obligation relating to the submission of interactive data files in these exhibits and are not subject to liability under the anti-fraud provisions of the Securities Act of 1933 or any other liability provision as long as we make a good faith attempt to comply with the submission requirements and promptly amend the interactive data files after becoming aware that the interactive data files fail to comply with the submission requirements.