ELECTRONIC ARTS INC.
Form 10-Q
November 08, 2011
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# UNITED STATES

# SECURITIES AND EXCHANGE COMMISSION

**WASHINGTON, D.C. 20549**

# FORM 10-Q

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

For the Quarterly Period Ended September 30, 2011

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. 000-17948

# ELECTRONIC ARTS INC.

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

| **Delaware** | **94-2838567** |
|---|---|
| ***(State or other jurisdiction of incorporation or organization)*** | ***(I.R.S. Employer Identification No.)*** |
| **209 Redwood Shores Parkway Redwood City, California** | **94065** |
| ***(Address of principal executive offices)*** | ***(Zip Code)*** |

**(650) 628-1500**

***(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 þ 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 þ 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 þ | Accelerated filer ¨ |
| Non-accelerated filer ¨<br>(Do not check if a smaller reporting company) | 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 þ

As of November 3, 2011, there were 331,425,465 shares of the Registrant s Common Stock, par value $0.01 per share, outstanding.

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**ELECTRONIC ARTS INC.**

**FORM 10-Q**

**FOR THE PERIOD ENDED SEPTEMBER 30, 2011**

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**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) | September 30, 2011 | March 31, 2011 (a) |
|---|---|---|
| **ASSETS** | | |
| Current assets: | | |
| Cash and cash equivalents | $ 930 | $ 1,579 |
| Short-term investments | 355 | 497 |
| Marketable equity securities | 214 | 161 |
| Receivables, net of allowances of $166 and $304, respectively | 562 | 335 |
| Inventories | 90 | 77 |
| Deferred income taxes, net | 97 | 56 |
| Other current assets | 320 | 327 |
| Total current assets | 2,568 | 3,032 |
| Property and equipment, net | 532 | 513 |
| Goodwill | 1,700 | 1,110 |
| Acquisition-related intangibles, net | 416 | 144 |
| Deferred income taxes, net | 45 | 49 |
| Other assets | 174 | 80 |
| **TOTAL ASSETS** | $ 5,435 | $ 4,928 |
| **LIABILITIES AND STOCKHOLDERS EQUITY** | | |
| Current liabilities: | | |
| Accounts payable | $ 213 | $ 228 |
| Accrued and other current liabilities | 792 | 768 |
| Deferred net revenue (packaged goods and digital content) | 849 | 1,005 |
| Total current liabilities | 1,854 | 2,001 |
| 0.75% convertible senior notes due 2016, net | 529 | |
| Income tax obligations | 187 | 192 |
| Deferred income taxes, net | 84 | 37 |
| Other liabilities | 241 | 134 |
| Total liabilities | 2,895 | 2,364 |
| Commitments and contingencies (See Note 13) | | |
| Stockholders equity: | | |
| Preferred stock, $0.01 par value. 10 shares authorized | | |
| Common stock, $0.01 par value. 1,000 shares authorized; 332 and 333 shares issued and outstanding, respectively | 3 | 3 |
| Paid-in capital | 2,551 | 2,495 |
| Accumulated deficit | (272) | (153) |
| Accumulated other comprehensive income | 258 | 219 |

| | | | | |
|---|---|---|---|---|
| Total stockholders equity | | 2,540 | | 2,564 |
| **TOTAL LIABILITIES AND STOCKHOLDERS EQUITY** | $ | 5,435 | $ | 4,928 |

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

(a) Derived from audited consolidated financial statements.

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**ELECTRONIC ARTS INC. AND SUBSIDIARIES**

**CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS**

| (Unaudited)<br>(In millions, except per share data) | Three Months Ended September 30, 2011 | Three Months Ended September 30, 2010 | Six Months Ended September 30, 2011 | Six Months Ended September 30, 2010 |
|---|---|---|---|---|
| Net revenue | $ 715 | $ 631 | $ 1,714 | $ 1,446 |
| Cost of goods sold | 432 | 363 | 672 | 585 |
| Gross profit | 283 | 268 | 1,042 | 861 |
| Operating expenses: | | | | |
| Marketing and sales | 222 | 173 | 362 | 300 |
| General and administrative | 88 | 77 | 162 | 151 |
| Research and development | 318 | 277 | 603 | 552 |
| Amortization of intangibles | 13 | 15 | 26 | 30 |
| Acquisition-related contingent consideration | 17 | (28) | 19 | (26) |
| Restructuring and other charges | (1) | 6 | 17 | 8 |
| Total operating expenses | 657 | 520 | 1,189 | 1,015 |
| Operating loss | (374) | (252) | (147) | (154) |
| Gain on strategic investments, net | | 28 | | 23 |
| Interest and other income (expense), net | (6) | 6 | (3) | 6 |
| Loss before benefit from income taxes | (380) | (218) | (150) | (125) |
| Benefit from income taxes | (40) | (17) | (31) | (20) |
| Net loss | $ (340) | $ (201) | $ (119) | $ (105) |
| Net loss per share: | | | | |
| Basic and Diluted | $ (1.03) | $ (0.61) | $ (0.36) | $ (0.32) |
| Number of shares used in computation: | | | | |
| Basic and Diluted | 331 | 329 | 331 | 328 |

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

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**ELECTRONIC ARTS INC. AND SUBSIDIARIES**

**CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS**

| (Unaudited)<br>(In millions) | Six Months Ended September 30, 2011 | 2010 |
|---|---|---|
| **OPERATING ACTIVITIES** | | |
| Net loss | $ (119) | $ (105) |
| Adjustments to reconcile net loss to net cash used in operating activities: | | |
| Depreciation, amortization and accretion, net | 94 | 94 |
| Stock-based compensation | 81 | 90 |
| Acquisition-related contingent consideration | 19 | (26) |
| Non-cash restructuring charges | | (1) |
| Net gains on investments and sale of property and equipment | (12) | (24) |
| Change in assets and liabilities: | | |
| Receivables, net | (215) | (237) |
| Inventories | (11) | (55) |
| Other assets | (63) | 14 |
| Accounts payable | (57) | 106 |
| Accrued and other liabilities | 2 | (142) |
| Deferred income taxes, net | (48) | 27 |
| Deferred net revenue (packaged goods and digital content) | (156) | (23) |
| Net cash used in operating activities | (485) | (282) |
| **INVESTING ACTIVITIES** | | |
| Capital expenditures | (84) | (23) |
| Proceeds from sale of property and equipment | 26 | |
| Proceeds from sale of marketable equity securities | | 132 |
| Proceeds from maturities and sales of short-term investments | 319 | 197 |
| Purchase of short-term investments | (179) | (262) |
| Acquisition of subsidiaries, net of cash acquired | (657) | |
| Net cash provided by (used in) investing activities | (575) | 44 |
| **FINANCING ACTIVITIES** | | |
| Proceeds from issuance of common stock | 35 | 17 |
| Proceeds from borrowings on convertible senior notes, net of issuance costs | 617 | |
| Proceeds from issuance of warrants | 65 | |
| Purchase of convertible note hedge | (107) | |
| Excess tax benefit from stock-based compensation | 3 | |
| Repurchase and retirement of common stock | (189) | |
| Net cash provided by financing activities | 424 | 17 |
| Effect of foreign exchange on cash and cash equivalents | (13) | 4 |
| Decrease in cash and cash equivalents | (649) | (217) |
| Beginning cash and cash equivalents | 1,579 | 1,273 |
| Ending cash and cash equivalents | $ 930 | $ 1,056 |

**Supplemental cash flow information:**

| | | | | |
|---|---|---|---|---|
| Cash paid (refunded) during the period for income taxes, net | $ | (9) | $ | 7 |
| **Non-cash investing activities:** | | | | |
| Change in unrealized gains on available-for-sale securities, net of taxes | $ | 55 | $ | 24 |
| Equity issued in connection with acquisition | $ | 87 | $ | |

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

**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 game software and content that can be played by consumers on a variety of platforms, including video game consoles (such as the Sony PLAYSTATION 3, Microsoft Xbox 360, and Nintendo Wii), personal computers, mobile phones (such as the Apple iPhone and Google Android compatible phones), tablets and electronic readers (such as the Apple iPad and Amazon Kindle), the Internet, and handheld game players (such as the Sony PlayStation Portable ( PSP ) and the Nintendo DS and 3DS). Some of our games are based on content that we license from others (*e.g.*, FIFA, Madden NFL, 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, Madden NFL, and NCAA Football), wholly-owned properties that can be successfully sequeled (*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, 2012 and 2011 contain 52 weeks each, and ends or ended, as the case may be, on March 31, 2012 and April 2, 2011, respectively. Our results of operations for the three months ended September 30, 2011 and 2010 contained 13 weeks each, and ended on October 1, 2011 and October 2, 2010, respectively. Our results of operations for the six months ended September 30, 2011 and 2010 contained 26 weeks each, and ended on October 1, 2011 and October 2, 2010, 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, 2011, as filed with the United States Securities and Exchange Commission ( SEC ) on May 24, 2011.

**(2) SIGNIFICANT ACCOUNTING POLICIES**

***Revenue Recognition***

We evaluate revenue recognition based on the criteria set forth in Financial Accounting Standards Board ( FASB ) Accounting Standards Codification ( ASC ) ASC 985-605, *Software: Revenue Recognition* and Staff Accounting Bulletin ( SAB ) No. 101, *Revenue Recognition in Financial Statements*, as revised by 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 must be present.

*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.

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*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).

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 vendor specific objective evidence ( 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.* 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.

*Multiple Element Revenue Arrangements*. In some of our multiple element arrangements, we sell tangible products with software and/or online services. These tangible products are generally either peripherals or ancillary collectors items. Prior to April 3, 2011, because either the software or other elements sold with the tangible products was essential to the functionality of the tangible product and/or we did not have VSOE for the tangible product, we did not separately account for tangible products. However, on April 3, 2011, we were required to adopt FASB Accounting Standards Update ( ASU ) 2009-13, *Revenue Recognition (Topic 605)*: *Multiple-Deliverable Revenue Arrangements* and ASU 2009-14, *Software (Topic 985)*: *Certain Revenue Arrangements that Include Software Elements*. While adoption of these standards did not have a material effect on financial statements for all periods presented, we did change our accounting for these tangible products whereby we now separately account for them and allocate a portion of the overall fee based on either their separate selling price or our best estimate of the fair value of the tangible product.

*Shipping and Handling.* We recognize amounts billed to customers for shipping and handling as revenue. Additionally, shipping and handling costs incurred by us are included in cost of goods sold.

*Online Subscription Revenue.* Online subscription revenue is derived principally from subscription revenue collected from customers for online play related to our massively multiplayer online games and Pogo-branded online games services. These

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customers generally pay on an annual basis or a month-to-month basis and prepaid subscription revenue is recognized ratably over the period for which the services are provided.

*Software Licenses.* We license software rights to manufacturers of products in related industries (for example, makers of personal computers or computer accessories) to include certain of our products with the manufacturer s product, or offer our products to consumers who have purchased the manufacturer s product. We call these combined products OEM bundles. These OEM bundles generally require the customer to pay us an upfront nonrefundable fee, which represents the guaranteed minimum royalty amount. Revenue is generally recognized upon delivery of the product master or the first copy. Per-copy royalties on sales that exceed the minimum guarantee are recognized as earned.

**(3) 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 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 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.

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***Assets and Liabilities Measured at Fair Value on a Recurring Basis***

As of September 30, 2011 and March 31, 2011, our assets and liabilities that were measured and recorded at fair value on a recurring basis were as follows (in millions):

| | | Fair Value Measurements at Reporting Date Using | | | |
|---|---|---|---|---|---|
| | As of September 30, 2011 | Quoted Prices in Active Markets for Identical Financial Instruments (Level 1) | Significant Other Observable Inputs (Level 2) | Significant Unobservable Inputs (Level 3) | Balance Sheet Classification |
| Assets | | | | | |
| Money market funds | $ 346 | $ 346 | $ | $ | Cash equivalents |
| Available-for-sale securities: | | | | | |
| Marketable equity securities | 214 | 214 | | | Marketable equity securities |
| Corporate bonds | 170 | | 170 | | Short-term investments |
| U.S. agency securities | 86 | | 86 | | Short-term investments |
| U.S. Treasury securities | 85 | 85 | | | Short-term investments and cash equivalents |
| Commercial paper | 22 | | 22 | | Short-term investments and cash equivalents |
| Deferred compensation plan assets [a] | 12 | 12 | | | Other assets |
| Foreign currency derivatives | 1 | | 1 | | Other current assets |
| Total assets at fair value | $ 936 | $ 657 | $ 279 | $ | |
| Liabilities | | | | | |
| Contingent consideration [b] | $ 166 | $ | $ | $ 166 | Accrued and other current liabilities and other liabilities |
| Total liabilities at fair value | $ 166 | $ | $ | $ 166 | |

| | Fair Value Measurements Using Significant Unobservable Inputs (Level 3) Contingent Consideration |
|---|---|
| Balance as of March 31, 2011 | $ 51 |
| Additions | 97 |
| Change in fair value [c] | 18 |
| Balance as of September 30, 2011 | $ 166 |

| | As of March 31, 2011 | (Level 1) | (Level 2) | (Level 3) | Balance Sheet Classification |
|---|---|---|---|---|---|
| Assets | | | | | |
| Money market funds | $ 774 | $ 774 | $ | $ | Cash equivalents |
| Available-for-sale securities: | | | | | |
| Corporate bonds | 253 | | 253 | | Short-term investments |
| Marketable equity securities | 161 | 161 | | | Marketable equity securities |
| U.S. Treasury securities | 129 | 129 | | | Short-term investments and cash equivalents |
| U.S. agency securities | 102 | | 102 | | Short-term investments |
| Commercial paper | 31 | | 31 | | Short-term investments and cash equivalents |

| | | | | | | | | | |
|---|---|---|---|---|---|---|---|---|---|
| Deferred compensation plan assets [a] | | 12 | | 12 | | | | | Other assets |
| Total assets at fair value | $ | 1,462 | $ | 1,076 | $ | 386 | $ | | |
| Liabilities | | | | | | | | | |
| Contingent consideration [b] | $ | 51 | $ | | $ | | $ | 51 | Accrued and other current liabilities and other liabilities |
| Total liabilities at fair value | $ | 51 | $ | | $ | | $ | 51 | |

| | Fair Value Measurements Using Significant Unobservable Inputs (Level 3) | |
|---|---|---|
| | Contingent Consideration | |
| Balance as of March 31, 2010 | $ | 65 |
| Additions | | 3 |
| Change in fair value [c] | | (17) |
| Balance as of March 31, 2011 | $ | 51 |

[a] The deferred compensation plan assets consist of various mutual funds.

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(b) The contingent consideration as of September 30, 2011 represents the estimated fair value of the additional variable cash consideration payable primarily in connection with our acquisitions of PopCap Games, Inc. ( PopCap ), Playfish Limited ( Playfish ) and Chillingo Limited ( Chillingo ) that is contingent upon the achievement of certain performance milestones. The contingent consideration as of March 31, 2011 represents the estimated fair value of the additional variable cash consideration payable primarily in connection with our acquisitions of Playfish and Chillingo 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 obligations are expected to be settled, and applied a discount rate that appropriately captures a market participant s view of the risk associated with the obligations. During the three months ended September 30, 2011, we recognized an additional $95 million of contingent consideration associated with our acquisition of PopCap. This estimated value is preliminary and may be materially adjusted upon completion of our valuation. See Note 6 for additional information related to the PopCap contingent consideration and allocation of purchase price.

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

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

There were no material impairment charges for assets and liabilities measured at fair value on a nonrecurring basis in periods subsequent to initial recognition during the three and six months ended September 30, 2011 and 2010.

**(4) FINANCIAL INSTRUMENTS**

***Cash and Cash Equivalents***

As of September 30, 2011 and March 31, 2011, our cash and cash equivalents were $930 million and $1,579 million, respectively. Cash equivalents were valued at their carrying amounts as they approximate fair value due to the short maturities of these financial instruments.

***Short-Term Investments***

Short-term investments consisted of the following as of September 30, 2011 and March 31, 2011 (in millions):

| | As of September 30, 2011 | | | | As of March 31, 2011 | | | |
|---|---|---|---|---|---|---|---|---|
| | Cost or Amortized Cost | Gross Unrealized Gains | Gross Unrealized Losses | Fair Value | Cost or Amortized Cost | Gross Unrealized Gains | Gross Unrealized Losses | Fair Value |
| Corporate bonds | $ 169 | $ 1 | $ | $ 170 | $ 252 | $ 1 | $ | $ 253 |
| U.S. agency securities | 86 | | | 86 | 102 | | | 102 |
| U.S. Treasury securities | 82 | | | 82 | 124 | | | 124 |
| Commercial paper | 17 | | | 17 | 18 | | | 18 |
| Short-term investments | $ 354 | $ 1 | $ | $ 355 | $ 496 | $ 1 | $ | $ 497 |

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 these investments to be other-than-temporarily impaired as of September 30, 2011 and March 31, 2011.

The following table summarizes the amortized cost and fair value of our short-term investments, classified by stated maturity as of September 30, 2011 and March 31, 2011 (in millions):

| | As of September 30, 2011 | | As of March 31, 2011 | |
|---|---|---|---|---|
| | Amortized Cost | Fair Value | Amortized Cost | Fair Value |
| Short-term investments | | | | |
| Due in 1 year or less | $ 128 | $ 128 | $ 214 | $ 214 |
| Due in 1-2 years | 143 | 144 | 156 | 157 |
| Due in 2-3 years | 83 | 83 | 126 | 126 |
| Short-term investments | $ 354 | $ 355 | $ 496 | $ 497 |

***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 the fair value of a security to a level below its adjusted cost basis is other-than-temporary. We evaluate these 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 September 30, 2011 and March 31, 2011 (in millions):

| | Adjusted Cost | Gross Unrealized Gains | Gross Unrealized Losses | Fair Value |
|---|---|---|---|---|
| As of September 30, 2011 | $ 32 | $ 182 | $ | $ 214 |
| As of March 31, 2011 | $ 32 | $ 129 | $ | $ 161 |

We did not recognize any impairment charges during the three and six months ended September 30, 2011 on our marketable equity securities. We did not recognize impairment charges during the three months ended September 30, 2010 on our marketable equity securities. During the six months ended September 30, 2010, we recognized impairment charges of $2 million on our investment in The9. Due to various factors, including but not limited to, the extent and duration during which the market price of this security had been below its adjusted cost and our intent to hold this security, we concluded the decline in value was other-than-temporary. The impairment charge for the six months ended September 30, 2010 is included in gain on strategic investments, net in our Condensed Consolidated Statement of Operations.

We did not sell any of our marketable securities during the three and six months ended September 30, 2011. During the three months ended September 30, 2010, we received proceeds of $121 million from the sale of our investment in Ubisoft and realized gains of $28 million, net of costs to sell. During the three and six months ended September 30, 2010, we sold the remaining portions of our investment in The9 and received proceeds of $3 million and $11 million, respectively, and realized gains of less than $1 million and losses of $3 million, respectively. The realized gains and losses for the three and six months ended September 30, 2010 are included in gain on strategic investments, net in our Condensed Consolidated Statement of Operations.

***0.75% Convertible Senior Notes Due 2016***

The following table summarizes the carrying value and fair value of our 0.75% Convertible Senior Notes due 2016 (in millions):

| | As of September 30, 2011 | |
|---|---|---|
| | Carrying Value | Fair Value |
| 0.75% Convertible Senior Notes due 2016 | $ 529 | $ 608 |

The carrying value of the 0.75% Convertible Senior Notes due 2016 excludes the fair value of the equity conversion feature, which was classified as equity upon issuance, while the fair value is based on quoted market prices for the 0.75% Convertible Senior Notes due 2016, which includes the equity conversion feature. See Note 12 for additional information related to our 0.75% Convertible Senior Notes due 2016.

**(5) 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, on 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 contracts generally is not significant. We do not use foreign currency option or foreign currency forward contracts for speculative or trading purposes.

***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 qualify for hedge accounting treatment, all hedging relationships are formally documented at the inception of the hedges and 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 the 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 the 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 (expense), 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 (expense), 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 (expense), net. As of September 30, 2011, we had foreign currency option contracts to purchase approximately $38 million in foreign currency and to sell approximately $72 million of foreign currency. All of the foreign currency option contracts outstanding as of September 30, 2011 will mature in the next 12 months. As of March 31, 2011, we had foreign currency option contracts to purchase approximately $40 million in foreign currency and to sell approximately $10 million of foreign currency. As of September 30, 2011 and March 31, 2011, the fair value of these outstanding foreign currency option contracts was immaterial and is included in other current assets.

The effect of the gains and losses from our foreign currency option contracts in our Condensed Consolidated Statements of Operations for the three and six months ended September 30, 2011 and 2010 was immaterial, and is included in interest and other income (expense), net.

***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 (expense), net, in our Condensed Consolidated Statements of Operations. The gains and losses on these foreign currency forward contracts generally offset the gains and losses in the underlying foreign-currency-denominated monetary assets and liabilities, which are also reported in interest and other income (expense), net, in our Condensed Consolidated Statements of Operations. As of September 30, 2011, we had foreign currency forward contracts to purchase and sell approximately $405 million in foreign currencies. Of this amount, $384 million represented contracts to sell foreign currencies in exchange for U.S. dollars, $12 million to purchase foreign currency in exchange for U.S. dollars, and $9 million to sell foreign currency in exchange for British pounds sterling. As of March 31, 2011, we had foreign currency forward contracts to purchase and sell approximately $187 million in foreign currencies. Of this amount, $140 million represented contracts to sell foreign currencies in exchange for U.S. dollars, $31 million to purchase foreign currency in exchange for U.S. dollars, and $16 million to sell foreign currency in exchange for British pounds sterling. As of September 30, 2011 and March 31, 2011, the fair value of our foreign currency forward contracts was immaterial and is included in accrued and other liabilities.

The effect of foreign currency forward contracts in our Condensed Consolidated Statements of Operations for the three and six months ended September 30, 2011 and 2010, was as follows (in millions):

| | Location of Gain (Loss) Recognized in Income on Derivative | Amount of Gain (Loss) Recognized in Income on Derivative | | | |
|---|---|---|---|---|---|
| | | Three Months Ended September 30, | | Six Months Ended September 30, | |
| | | 2011 | 2010 | 2011 | 2010 |
| Foreign currency forward contracts not designated as hedging instruments | Interest and other income (expense), net | $ 16 | $ (7) | $ 14 | $ (5) |

**(6) BUSINESS COMBINATIONS**

***PopCap Games Inc. Acquisition***

In August 2011, we acquired all of the outstanding shares of PopCap for an aggregate purchase price of approximately (1) $645 million in cash and (2) $87 million in privately-placed shares of our common stock to the founders and chief executive officer of PopCap. In addition, we agreed to grant over a four year period to PopCap s employees up to $50 million in long-term equity retention arrangements in the form of restricted stock unit awards and options to acquire our common stock. These awards will be accounted for as stock-based compensation in accordance with ASC 718, *Compensation Stock Compensation*. PopCap is a leading provider of games for mobile phones, tablets, PCs, and social network sites. This acquisition strengthens our participation in casual gaming and contributes to the growth of our digital product offerings. The following table summarizes the acquisition date fair value of the consideration transferred which consisted of the following (in millions):

| | |
|---|---|
| Cash | $ 645 |
| Equity | 87 |
| Total purchase price | $ 732 |

The equity included in the consideration above consisted of privately-placed shares of our common stock, whose fair value was determined based on the quoted market price of our common stock on the date of acquisition.

In addition, we may be required to pay additional variable cash consideration that is contingent upon the achievement of certain performance milestones through December 31, 2013 and is limited to a maximum of $550 million based on achievement of certain non-GAAP earnings before interest and tax targets. The preliminary estimated fair value of the contingent consideration arrangement at the acquisition date was $95 million. We estimated the fair value of the contingent consideration using probability assessments of 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.

The preliminary allocation of the purchase price was based upon preliminary valuations for the intangible assets, deferred taxes, and contingent consideration liabilities, and will be completed during the third quarter of fiscal year 2012. The preliminary allocation of the purchase price may have material adjustments when the valuations have been completed. The following table summarizes the preliminary fair values of assets acquired and liabilities assumed as of September 30, 2011 (in millions):

| | |
|---|---|
| Current assets | $ 62 |
| Property and equipment, net | 6 |
| Goodwill | 565 |
| Finite-lived intangibles assets | 302 |
| Contingent consideration | (95) |
| Deferred income taxes, net | (55) |

| | |
|---|---|
| Other liabilities | (53) |
| Total purchase price | $ 732 |

All of the goodwill was assigned to our EA Brands Segment. None of the goodwill recognized upon acquisition is deductible for tax purposes. See Note 7 for additional information related to the changes in the carrying amount of goodwill and Note 17 for segment information.

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The results of operations of PopCap and the estimated fair market values of the assets acquired and liabilities assumed have been included in our Condensed Consolidated Financial Statements since the date of acquisition.

Finite-lives intangible assets acquired in this transaction are being amortized on a straight-line basis over their estimated lives ranging from three to nine years. The intangible assets as of the date of the acquisition include:

| | Gross Carrying Amount (in millions) | Weighted-Average Useful Life (in years) |
|---|---|---|
| Developed and core technology | $ 245 | 6 |
| Trade names and trademarks | 40 | 9 |
| In-process research and development | 15 | 5 |
| Other intangibles | 2 | 4 |
| Total finite-lived intangibles | $ 302 | 6 |

In connection with our acquisition of PopCap, we acquired in-process research and development assets valued at approximately $15 million in relation to game software that had not reached technical feasibility as of the date of acquisition. The fair value of PopCap s products under development was determined using the income approach, which discounts expected future cash flows from the acquired in-process technology to present value. The discount rates used in the present value calculations were derived from an average weighted average cost of capital of 13 percent. Should the in-process software not be successfully completed, completed at a higher cost, or the development efforts go beyond the timeframe estimated by management, we may not receive the full benefits anticipated from the acquisition. Benefits from the development efforts are expected to begin to be received in fiscal year 2012 and the development efforts are expected to be completed in fiscal year 2013.

There were six in-process research and development projects acquired as of the acquisition date each with $4 million or less of assigned fair value and $15 million of aggregate fair value. Additionally each project had less than $2 million of estimated costs to complete and $5 million aggregate cost to complete. As of the acquisition date, the weighted-average estimated percentage completion of all six projects combined was 36 percent.

Our Condensed Consolidated Financial Statements included the operating results of PopCap from the date of acquisition. Pro forma results of operations have not been presented because the effect of the acquisition was not material to our Condensed Consolidated Statements of Operations.

***Other Acquisitions***

During the six months ended September 30, 2011, we completed three acquisitions that did not have a significant impact on our Condensed Consolidated Financial Statements.

**(7) GOODWILL AND ACQUISITION-RELATED INTANGIBLES, NET**

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

| | EA Brands Segment |
|---|---|
| As of March 31, 2011 | |
| Goodwill | $ 1,478 |
| Accumulated impairment | (368) |
| Total | 1,110 |
| Goodwill acquired | 595 |

| | | |
|---|---|---|
| Effects of foreign currency translation | | (5) |
| As of September 30, 2011 | | |
| Goodwill | | 2,068 |
| Accumulated impairment | | (368) |
| Total | $ | 1,700 |

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

| | As of September 30, 2011 | | | As of March 31, 2011 | | |
|---|---|---|---|---|---|---|
| | Gross Carrying Amount | Accumulated Amortization | Acquisition-Related Intangibles, Net | Gross Carrying Amount | Accumulated Amortization | Acquisition-Related Intangibles, Net |
| Developed and core technology | $ 510 | $ (197) | $ 313 | $ 259 | $ (180) | $ 79 |
| Trade names and trademarks | 130 | (77) | 53 | 90 | (70) | 20 |
| Carrier contracts and related | 85 | (64) | 21 | 85 | (62) | 23 |
| Registered user base and other intangibles | 89 | (75) | 14 | 86 | (64) | 22 |
| In-process research and development | 15 | | 15 | | | |
| Total | $ 829 | $ (413) | $ 416 | $ 520 | $ (376) | $ 144 |

Amortization of intangibles for the three and six months ended September 30, 2011 was $21 million (of which $8 million was recognized in cost of goods sold) and $37 million (of which $11 million was recognized in cost of goods sold), respectively. Amortization of intangibles for the three and six months ended September 30, 2010 was $18 million (of which $3 million was recognized in cost of goods sold) and $36 million (of which $6 million was recognized in cost of goods sold), respectively. Acquisition-related intangible assets are amortized using the straight-line method over the lesser of their estimated useful lives or the agreement terms, typically from two to fourteen years. As of September 30, 2011 and March 31, 2011, the weighted-average remaining useful life for acquisition-related intangible assets was approximately 6.0 years and 5.1 years, respectively.

As of September 30, 2011, future amortization of acquisition-related intangibles that will be recorded in cost of goods sold and operating expenses is estimated as follows (in millions):

| Fiscal Year Ending March 31, | |
|---|---|
| 2012 (remaining six months) | $ 44 |
| 2013 | 78 |
| 2014 | 68 |
| 2015 | 63 |
| 2016 | 51 |
| Thereafter | 112 |
| Total | $ 416 |

**(8) RESTRUCTURING AND OTHER CHARGES**

Restructuring and other restructuring plan-related information as of September 30, 2011 was as follows (in millions):

| | Fiscal 2011 Restructuring | | Fiscal 2010 Restructuring | | | Fiscal 2009 Restructuring | Fiscal 2008 Reorgnaization | |
|---|---|---|---|---|---|---|---|---|
| | Workforce | Other | Workforce | Facilities-related | Other | Facilities-related | Facilities-related | Total |
| Balances as of March 31, 2010 | $ | $ | $ 8 | $ 11 | $ 7 | $ 3 | $ | $ 29 |
| Charges to operations | 13 | 135 | | | 13 | | | 161 |
| Charges settled in cash | (8) | (32) | (8) | (6) | (15) | (1) | | (70) |
| Charges settled in non-cash | (2) | (2) | | 1 | | | | (3) |
| Balances as of March 31, 2011 | 3 | 101 | | 6 | 5 | 2 | | 117 |
| Charges to operations | (1) | 17 | | 1 | 10 | | (10) | 17 |

| | | | | | | | | |
|---|---|---|---|---|---|---|---|---|
| Charges settled in cash | (2) | (19) | | (4) | (9) | | 10 | (24) |
| Balances as of September 30, 2011 | $ | $ 99 | $ | $ 3 | $ 6 | $ 2 | $ | $ 110 |

***Fiscal 2011 Restructuring***

In fiscal year 2011, we announced a plan focused on the restructuring of certain licensing and developer agreements in an effort to improve the long-term profitability of our packaged goods business. Under this plan, we amended certain licensing and developer agreements. To a much lesser extent, as part of this restructuring we had workforce reductions and facilities closures through March 31, 2011. Substantially all of these exit activities were completed by March 31, 2011.

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As part of our fiscal 2011 restructuring plan, we amended certain license agreements to terminate certain rights we previously had to use the licensors intellectual property. However, under these agreements we continue to be obligated to pay the contractual minimum royalty-based commitments set forth in the original agreem