

TAKE TWO INTERACTIVE SOFTWARE INC
Form 10-Q
February 08, 2018

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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 December 31, 2017

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 number 001-34003

TAKE-TWO INTERACTIVE SOFTWARE, INC.

(Exact Name of Registrant as Specified in Its Charter)

Delaware 51-0350842

(State or Other Jurisdiction of (I.R.S. Employer

Incorporation or Organization) Identification No.)

110 West 44th Street 10036

New York, New York (Zip Code)

(Address of principal executive offices)

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

Indicate by check mark whether the Registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. Yes 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. (Check one):

Large accelerated filer Accelerated filer Non-accelerated filer
(Do not check if a smaller reporting company) Smaller reporting company Emerging growth company

If an emerging growth company, indicate by check mark if the registrant has elected not to use the extended transition period for complying with any new or revised financial accounting standards provided pursuant to Section 13(a) of the Exchange Act.

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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 January 31, 2018, there were 114,398,287 shares of the Registrant's Common Stock outstanding, net of treasury stock.

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(All other items in this report are inapplicable)

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PART I. FINANCIAL INFORMATION

Item 1. Financial Statements (Unaudited)

TAKE-TWO INTERACTIVE SOFTWARE, INC.

CONDENSED CONSOLIDATED BALANCE SHEETS

(in thousands, except per share amounts)

| | December 31, 2017 | March 31, 2017 |
|---|----------------------|-------------------|
| | (Unaudited) | |
| ASSETS | | |
| Current assets: | | |
| Cash and cash equivalents | \$ 774,455 | \$943,396 |
| Short-term investments | 547,329 | 448,932 |
| Restricted cash | 374,806 | 337,818 |
| Accounts receivable, net of allowances of \$67,685 and \$66,483 at December 31, 2017 and March 31, 2017, respectively | 425,931 | 219,558 |
| Inventory | 30,857 | 16,323 |
| Software development costs and licenses | 39,369 | 41,721 |
| Deferred cost of goods sold | 164,112 | 127,901 |
| Prepaid expenses and other | 90,865 | 59,593 |
| Total current assets | 2,447,724 | 2,195,242 |
| Fixed assets, net | 96,570 | 67,300 |
| Software development costs and licenses, net of current portion | 586,866 | 381,910 |
| Goodwill | 389,728 | 359,115 |
| Other intangibles, net | 108,112 | 110,262 |
| Other assets | 53,610 | 35,325 |
| Total assets | \$ 3,682,610 | \$ 3,149,154 |
| LIABILITIES AND STOCKHOLDERS' EQUITY | | |
| Current liabilities: | | |
| Accounts payable | \$ 45,998 | \$31,892 |
| Accrued expenses and other current liabilities | 907,345 | 750,875 |
| Deferred revenue | 1,118,774 | 903,125 |
| Total current liabilities | 2,072,117 | 1,685,892 |
| Long-term debt | 13,838 | 251,929 |
| Non-current deferred revenue | 44,501 | 10,406 |
| Other long-term liabilities | 151,334 | 197,199 |
| Total liabilities | \$ 2,281,790 | \$ 2,145,426 |
| Commitments and Contingencies (See Note 12) | | |
| Stockholders' equity: | | |
| Preferred stock, \$.01 par value, 5,000 shares authorized; no shares issued and outstanding at December 31, 2017 and March 31, 2017 | — | — |
| Common stock, \$.01 par value, 200,000 shares authorized; 132,581 and 119,813 shares issued and 114,325 and 102,621 outstanding at December 31, 2017 and March 31, 2017, respectively | 1,326 | 1,198 |
| Additional paid-in capital | 1,861,424 | 1,452,754 |
| Treasury stock, at cost; 18,256 common shares at December 31, 2017 and 17,192 at March 31, 2017 | (413,524 |) (303,388) |
| Accumulated deficit | (17,311 |) (99,694) |
| Accumulated other comprehensive loss | (31,095 |) (47,142) |

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| | | |
|--|-------------|-------------|
| Total stockholders' equity | 1,400,820 | 1,003,728 |
| Total liabilities and stockholders' equity | \$3,682,610 | \$3,149,154 |

See accompanying Notes.

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TAKE-TWO INTERACTIVE SOFTWARE, INC.
 CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS (Unaudited)
 (in thousands, except per share amounts)

| | Three Months Ended | | Nine Months Ended | |
|------------------------------------|--------------------|-------------|-------------------|-------------|
| | December 31, | | December 31, | |
| | 2017 | 2016 | 2017 | 2016 |
| Net revenue | \$480,840 | \$476,473 | \$1,342,618 | \$1,208,192 |
| Cost of goods sold | 267,983 | 311,074 | 709,100 | 708,059 |
| Gross profit | 212,857 | 165,399 | 633,518 | 500,133 |
| Selling and marketing | 79,513 | 95,820 | 208,641 | 247,141 |
| General and administrative | 65,951 | 52,939 | 187,378 | 149,367 |
| Research and development | 49,977 | 37,589 | 142,245 | 101,494 |
| Depreciation and amortization | 7,864 | 7,460 | 34,490 | 22,329 |
| Business reorganization | 700 | — | 13,012 | — |
| Total operating expenses | 204,005 | 193,808 | 585,766 | 520,331 |
| Income (loss) from operations | 8,852 | (28,409) | 47,752 | (20,198) |
| Interest and other, net | 3,374 | (3,715) | (2,403) | (15,298) |
| Gain on long-term investments, net | — | — | — | 1,350 |
| Income (loss) before income taxes | 12,226 | (32,124) | 45,349 | (34,146) |
| Benefit from income taxes | (12,914) | (2,282) | (37,331) | (2,169) |
| Net income (loss) | \$25,140 | \$(29,842) | \$82,680 | \$(31,977) |
| Earnings (loss) per share: | | | | |
| Basic earnings (loss) per share | \$0.22 | \$(0.33) | \$0.76 | \$(0.37) |
| Diluted earnings (loss) per share | \$0.21 | \$(0.33) | \$0.74 | \$(0.37) |
| See accompanying Notes. | | | | |

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TAKE-TWO INTERACTIVE SOFTWARE, INC.
 CONDENSED CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME (LOSS) (Unaudited)
 (in thousands)

| | Three Months Ended December 31, | | Nine Months Ended December 31, | |
|--|---------------------------------------|------------|-----------------------------------|------------|
| | 2017 | 2016 | 2017 | 2016 |
| Net income (loss) | \$25,140 | \$(29,842) | \$82,680 | \$(31,977) |
| Other comprehensive (loss) income: | | | | |
| Foreign currency translation adjustment | (385) | (5,040) | 23,391 | (10,067) |
| Cash flow hedges: | | | | |
| Change in fair value of effective cash flow hedge | (1,423) | — | (6,639) | — |
| Available-for-sale securities: | | | | |
| Unrealized loss, net on available-for-sale securities, net of taxes | (816) | (264) | (705) | (221) |
| Reclassification to earnings for realized losses, net on available for sale securities, net of taxes | — | — | — | 9 |
| Change in fair value of available for sale securities | (816) | (264) | (705) | (212) |
| Other comprehensive (loss) income | (2,624) | (5,304) | 16,047 | (10,279) |
| Comprehensive income (loss) | \$22,516 | \$(35,146) | \$98,727 | \$(42,256) |

See accompanying Notes.

TAKE-TWO INTERACTIVE SOFTWARE, INC.
 CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS (Unaudited)
 (in thousands)

| | Nine Months Ended December 31, | |
|--|-----------------------------------|-------------|
| | 2017 | 2016 |
| Operating activities: | | |
| Net income (loss) | \$82,680 | \$(31,977) |
| Adjustments to reconcile net income (loss) to net cash provided by operating activities: | | |
| Amortization and impairment of software development costs and licenses | 62,235 | 130,019 |
| Depreciation | 23,233 | 22,329 |
| Amortization and impairment of intellectual property | 26,470 | 1,398 |
| Impairment of in-process research and development | 11,257 | — |
| Stock-based compensation | 96,111 | 55,421 |
| Amortization of discount on Convertible Notes | 15,424 | 17,870 |
| Gain on conversions of Convertible Notes | (4,855) | — |
| Amortization of debt issuance costs | 554 | 1,078 |
| Other, net | 3,432 | (3,604) |
| Changes in assets and liabilities: | | |
| Restricted cash | (36,988) | (17,372) |
| Accounts receivable | (206,084) | (160,095) |
| Inventory | (12,976) | (15,876) |
| Software development costs and licenses | (186,373) | (194,422) |
| Prepaid expenses and other assets | (39,133) | (31,460) |
| Deferred revenue | 238,590 | 302,728 |
| Deferred cost of goods sold | (33,578) | (66,502) |
| Accounts payable, accrued expenses and other liabilities | 164,086 | 230,067 |
| Net cash provided by operating activities | 204,085 | 239,602 |
| Investing activities: | | |
| Change in bank time deposits | 10,000 | 66,841 |
| Proceeds from available-for-sale securities | 172,925 | 101,357 |
| Purchases of available-for-sale securities | (282,596) | (104,357) |
| Purchases of fixed assets | (47,478) | (14,369) |
| Asset acquisition | (25,965) | — |
| Proceeds from sale of long-term investment | — | 1,350 |
| Purchase of long-term investments | — | (1,885) |
| Business acquisition | (9,401) | (750) |
| Net cash (used in) provided by investing activities | (182,515) | 48,187 |
| Financing activities: | | |
| Excess tax benefit from stock-based compensation | — | 1,499 |
| Tax payment related to net share settlements on restricted stock awards | (94,930) | (36,734) |
| Repurchase of Common Stock | (110,136) | — |
| Net cash used in financing activities | (205,066) | (35,235) |
| Effects of foreign currency exchange rates on cash and cash equivalents | 14,555 | (11,866) |
| Net change in cash and cash equivalents | (168,941) | 240,688 |
| Cash and cash equivalents, beginning of year | 943,396 | 798,742 |
| Cash and cash equivalents, end of period | \$774,455 | \$1,039,430 |

See accompanying Notes.

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TAKE-TWO INTERACTIVE SOFTWARE, INC.

Notes to Condensed Consolidated Financial Statements (Unaudited)

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

1. BASIS OF PRESENTATION AND SIGNIFICANT ACCOUNTING POLICIES

Take-Two Interactive Software, Inc. (the "Company," "we," "us," or similar pronouns) was incorporated in the state of Delaware in 1993. We are a leading developer, publisher and marketer of interactive entertainment for consumers around the globe. We develop and publish products principally through our two wholly-owned labels Rockstar Games and 2K, as well as our new Private Division label and Social Point, a leading developer of mobile games. Our products are designed for console systems and personal computers, including smart phones and tablets, and are delivered through physical retail, digital download, online platforms and cloud streaming services.

Basis of Presentation

The accompanying Condensed Consolidated Financial Statements are unaudited and include the accounts of the Company and its wholly-owned subsidiaries and, in the opinion of management, reflect all normal and recurring adjustments necessary for the fair presentation of our financial position, results of operations and cash flows. Interim results may not be indicative of the results that may be expected for the full fiscal year. All inter-company accounts and transactions have been eliminated in consolidation. The preparation of these Condensed Consolidated Financial Statements in accordance with accounting principles generally accepted in the United States requires management to make estimates and assumptions that affect the amounts reported in these Condensed Consolidated Financial Statements and accompanying notes. As permitted under generally accepted accounting principles in the United States, interim accounting for certain expenses, including income taxes, are based on full year assumptions when appropriate. Actual results could differ materially from those estimates.

Certain information and footnote disclosures normally included in financial statements prepared in accordance with accounting principles generally accepted in the United States have been omitted pursuant to the rules and regulations of the Securities and Exchange Commission, although we believe that the disclosures are adequate to make the information presented not misleading. These Condensed Consolidated Financial Statements and accompanying notes should be read in conjunction with our annual consolidated financial statements and the notes thereto, included in our Annual Report on Form 10-K for the fiscal year ended March 31, 2017.

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

Revenue Recognition

As part of our on-going assessment of estimated service periods, in June 2017, we extended Grand Theft Auto V's estimated service period from 41 through 50 months, or through December 2018. We expect this change in estimated service period to have a material impact on our Consolidated Financial Statements for fiscal 2018. The impact of this change is shown in the table below.

| | Three Months Ended December 31, 2017 | Nine Months Ended December 31, 2017 |
|---------------------------------------|---|--|
| Change in net revenue | \$(78,761) | \$(183,206) |
| Change in income from operations | (72,633) | (168,997) |
| Change in net income | (57,150) | (145,303) |
| Change in earnings per share, basic | \$(0.50) | \$(1.33) |
| Change in earnings per share, diluted | \$(0.49) | \$(1.30) |

Impairment of In-process Research & Development ("IPR&D")

During our second fiscal quarter, as a result of our decision not to proceed with further development of certain IPR&D from the Social Point, S.L. ("Social Point") acquisition, we recognized an impairment charge of \$11,257 in Depreciation and amortization expense in our Condensed Consolidated Statements of Operations.

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Recently Adopted Accounting Pronouncements

Accounting for Stock Compensation

In March 2016, the Financial Accounting Standards Board ("FASB") issued Accounting Standards Update ("ASU") 2016-09, Compensation—Stock Compensation. This new guidance identifies areas for simplification involving several aspects of accounting for share-based payment transactions, including income tax consequences, classification of awards as either equity or liabilities, an option to recognize gross stock compensation expense with actual forfeitures recognized as they occur, as well as certain classifications on the statement of cash flows.

We adopted this update effective April 1, 2017. Upon adoption, using the modified retrospective transition method, we recognized previously unrecognized excess tax benefits as a deferred tax asset, which was fully offset by a valuation allowance, resulting in no net impact to retained earnings. Without the valuation allowance, our deferred tax asset would have increased by \$24,594. We elected to apply the change in presentation of excess tax benefits as an operating activity in the Consolidated Statement of Cash Flows prospectively and thus no prior periods were adjusted. We also elected to account for forfeitures as they occur using the modified retrospective transition method, which resulted in a cumulative effect adjustment of \$323 to retained earnings (an increase in the accumulated deficit). The other aspects of the new guidance did not have a material effect on our Consolidated Financial Statements.

Accounting for Acquisitions or Disposals

In January 2017, the FASB issued ASU 2017-01, Clarifying the Definition of a Business, with the objective of providing additional guidance to assist entities with evaluating whether transactions should be accounted for as acquisitions (or disposals) of assets or businesses. The amendments in this update provide new guidance to determine when an integrated set of assets and activities (collectively referred to as a "set") is not a business. The new guidance requires that when substantially all of the fair value of the gross assets acquired (or disposed of) is concentrated in a single identifiable asset or a group of similar identifiable assets, the set is not a business. The new guidance is expected to reduce the number of transactions that need to be further evaluated. The new standard, as amended, will be effective prospectively for interim and annual reporting periods beginning on January 1, 2018 (April 1, 2018 for the Company), with early adoption permitted. We adopted this update as of April 1, 2017.

Recently Issued Accounting Pronouncements

Accounting for Goodwill

In January 2017, the FASB issued ASU 2017-04, Intangibles - Goodwill and Other (Topic 350). This ASU eliminates Step 2 from the goodwill impairment test. Under the new guidance, an entity should perform its annual or interim goodwill impairment test by comparing the fair value of a reporting unit with its carrying amount and recognize an impairment charge for the amount by which the carrying amount exceeds the reporting unit's fair value. Additionally, this ASU eliminates the requirements for any reporting unit with a zero or negative carrying amount to perform a qualitative assessment and, if it fails that qualitative test, to perform Step 2 of the goodwill impairment test. The amendments in this ASU are effective for fiscal years beginning after December 15, 2019 (April 1, 2020 for the Company), including interim periods within those fiscal years, and is applied on a prospective basis. Early adoption is permitted for interim or annual goodwill impairment tests performed on testing dates after January 1, 2017. While we are currently evaluating the impact of the adoption of this ASU, we do not believe that the adoption of this guidance will have a material impact on our Consolidated Financial Statements.

Accounting for Restricted Cash

In November 2016, the FASB issued ASU 2016-18, Statement of Cash Flows (Topic 230): Restricted Cash. This ASU amends the presentation of restricted cash within the statement of cash flows. The new guidance requires that changes in restricted cash and cash equivalents be included with cash and cash equivalents when reconciling the beginning-of-period and end-of-period total amounts on the statement of cash flows. This standard will be effective for fiscal years beginning after December 15, 2017 (April 1, 2018 for the Company), including interim periods within those fiscal years. Early adoption is permitted. We are currently evaluating the impact of the adoption of this ASU.

Accounting for Leases

In February 2016, the FASB issued ASU 2016-02, Leases. This new guidance requires lessees to recognize a right-of-use asset and a lease liability for virtually all leases (other than leases that meet the definition of a short-term lease). The liability will be equal to the present value of lease payments. The asset will be based on the liability,

subject to adjustment, such as for initial direct costs. For income statement purposes, the FASB retained a dual model, requiring leases to be classified as either operating or finance. Operating leases will result in straight-line expense (similar to current operating leases) while finance leases will result in a front-loaded expense pattern (similar to current capital leases). Classification will be based on criteria that are largely similar to those applied in current lease accounting. This update is effective for annual periods, and interim periods within

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those years, beginning after December 15, 2018 (April 1, 2019 for the Company). This new guidance must be adopted using a modified retrospective approach whereby lessees and lessors are required to recognize and measure leases at the beginning of the earliest period presented using a modified retrospective approach. Early adoption is permitted. We are currently evaluating the impact of adopting this update on our Consolidated Financial Statements, which will consist primarily of a balance sheet gross up of our operating leases, mostly for office space.

Revenue from Contracts with Customers

In May 2014, the FASB issued ASU 2014-09, Revenue from Contracts with Customers (Topic 606). Under the new standard, revenue is recognized when a customer obtains control of promised goods or services and is recognized in an amount that reflects the consideration that the entity expects to receive in exchange for those goods or services. In addition, the standard requires disclosure of the nature, amount, timing, and uncertainty of revenue and cash flows arising from contracts with customers. The FASB recently issued several amendments to the standard, including clarifications on disclosure of prior-period performance obligations and remaining performance obligations.

The guidance permits two methods of adoption: retrospectively to each prior reporting period presented (full retrospective method), or retrospectively with the cumulative effect of initially applying the guidance recognized at the date of initial application (the cumulative catch-up transition method).

The new standard is effective for annual reporting periods, and interim periods within those annual periods, beginning after December 15, 2017 (April 1, 2018 for the Company), with early adoption permitted for annual reporting periods beginning after December 15, 2016 (April 1, 2017 for the Company). We will adopt the new standard effective April 1, 2018 using the cumulative catch-up transition method.

We anticipate this standard will have a material impact on our Consolidated Financial Statements. While we are continuing to assess all potential impacts of the standard, we currently believe the most significant impact relates to our accounting for on-line enabled games that benefit from meaningful post-contract customer support ("PCS") such as unspecified content updates for which we do not have vendor-specific objective evidence of fair value ("VSOE").

Under the current accounting standards, for titles that do not have VSOE, we recognize the entire sales price ratably over the title's estimated service period. The VSOE requirement will be eliminated under the new standard. Accordingly, we may be required to recognize as revenue a portion of the sales price upon delivery of the software, as compared to the current requirement of recognizing the entire sales price ratably over an estimated offering period.

It is possible that our evaluation of the expected impact of the new standard on certain transactions could change if there are additional interpretations of the new revenue guidance that are different from our preliminary conclusions.

2. MANAGEMENT AGREEMENT

In March 2014, we entered into an amended management services agreement, (the "2014 Management Agreement"), with ZelnickMedia Corporation ("ZelnickMedia") pursuant to which ZelnickMedia provided us with certain management, consulting and executive level services. The 2014 Management Agreement became effective April 1, 2014. The 2014 Management Agreement provided for an annual management fee of \$2,970 over the term of the agreement and a maximum annual bonus opportunity of \$4,752 over the term of the agreement, based on the Company achieving certain performance thresholds. In November 2017, we entered into a new management agreement, (the "2017 Management Agreement"), with ZelnickMedia pursuant to which ZelnickMedia continues to provide financial and management consulting services to the Company through March 31, 2024. The 2017 Management Agreement became effective January 1, 2018 and supersedes and replaces the 2014 Management Agreement, except as otherwise contemplated by the 2017 Management Agreement. As part of the 2017 Management Agreement, Strauss Zelnick, the President of ZelnickMedia, continues to serve as Executive Chairman and Chief Executive Officer, and Karl Slatoff, a partner of ZelnickMedia, continues to serve as President of the Company. The 2017 Management Agreement provides for an annual management fee of \$3,100 over the term of the agreement and a maximum annual bonus opportunity of \$7,440 over the term of the agreement, based on the Company achieving

certain performance thresholds.

In consideration for ZelnickMedia's services, we recorded consulting expense (a component of general and administrative expenses) of \$2,435 and \$2,440 during the three months ended December 31, 2017 and 2016, respectively, and \$6,296 and \$5,113 during the nine months ended December 31, 2017 and 2016, respectively. We recorded stock-based compensation expense for non-employee restricted stock units granted to ZelnickMedia, which is included in general and administrative expenses of \$10,351 and \$7,066 during the three months ended December 31, 2017 and 2016, respectively, and \$30,228 and \$17,862 during the nine months ended December 31, 2017 and 2016, respectively.

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In connection with the 2014 Management Agreement, we have granted restricted stock units as follows:

| | Nine Months Ended December 31, | |
|------------------------------|--------------------------------------|---------|
| | 2017 | 2016 |
| Time-based | 66,122 | 107,551 |
| Market-based(1) | 122,370 | 199,038 |
| Performance-based(1) | | |
| New IP | 20,396 | 33,174 |
| Major IP | 20,394 | 33,172 |
| Total—Performance-based | 40,790 | 66,346 |
| Total Restricted Stock Units | 229,282 | 372,935 |

(1) Represents the maximum number of shares eligible to vest.

Time-based restricted stock units granted in 2017 will vest on April 4, 2019, and those granted in 2016 will vest on April 2, 2018, in each case provided that the 2017 Management Agreement has not been terminated prior to such vesting date.

Market-based restricted stock units granted in 2017 are eligible to vest on April 4, 2019, and those granted in 2016 are eligible to vest on April 2, 2018, in each case provided that the 2017 Management Agreement has not been terminated prior to such vesting date. Market-based restricted stock units are eligible to vest based on the Company's Total Shareholder Return (as defined in the relevant grant agreement) relative to the Total Shareholder Return (as defined in the relevant grant agreement) of the companies that constitute the NASDAQ Composite Index as of the grant date measured over a two-year period. To earn the target number of market-based restricted stock units (which represents 50% of the number of the market-based restricted stock units set forth in the table above), the Company must perform at the 50th percentile, with the maximum number of market-based restricted stock units earned if the Company performs at the 75th percentile. Each reporting period we re-measure the fair value of the unvested shares of market-based restricted stock units granted to ZelnickMedia.

Performance-based restricted stock units granted in 2017 are eligible to vest on April 4, 2019, and those granted in 2016 are eligible to vest on April 2, 2018, in each case provided that the 2017 Management Agreement has not been terminated prior to such vesting date. Performance-based restricted stock units, of which 50% are tied to "New IP" and 50% to "Major IP" (as defined in the relevant grant agreement), are eligible to vest based on the Company's achievement of certain performance metrics (as defined in the relevant grant agreement) of individual product releases of "New IP" or "Major IP" measured over a two-year period. The target number of performance-based restricted stock units that may be earned pursuant to these grants is equal to 50% of the grant amounts set forth in the above table (the numbers in the table represent the maximum number of performance-based restricted stock units that may be earned). Each reporting period we assess the performance metric and upon achievement of certain thresholds record an expense for the unvested portion of the shares of performance-based restricted stock units. Certain performance metrics, based on unit sales, have been achieved as of December 31, 2017 for the "Major IP" performance-based restricted stock units granted in 2017 and 2016.

The unvested portion of time-based, market-based and performance-based restricted stock units held by ZelnickMedia were 602,217 and 898,526 as of December 31, 2017 and March 31, 2017, respectively. 478,839 restricted stock units previously granted to ZelnickMedia, vested and 46,752 restricted stock units were forfeited by ZelnickMedia during the nine months ended December 31, 2017.

3. FAIR VALUE MEASUREMENTS

The carrying amounts of our financial instruments, including cash and cash equivalents, restricted cash, accounts receivable, accounts payable and accrued expenses and other current liabilities, approximate fair value because of their short maturities.

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

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

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

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

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

| | December 31, 2017 | Quoted prices in active markets for identical assets (level 1) | Significant other observable inputs (level 2) | Significant unobservable inputs (level 3) | Balance Sheet Classification |
|--|-------------------|--|---|---|---|
| Money market funds | \$419,642 | \$419,642 | | \$ — | Cash and cash equivalents |
| Bank-time deposits | 53,598 | 53,598 | | — | Cash and cash equivalents |
| Commercial paper | 17,294 | | 17,294 | — | Cash and cash equivalents |
| Corporate bonds | 10,246 | | 10,246 | — | Cash and cash equivalents |
| Bank-time deposits | 166,321 | 166,321 | | — | Short-term investments |
| Corporate bonds | 362,416 | | 362,416 | — | Short-term investments |
| Commercial paper | 13,921 | | 13,921 | — | Short-term investments |
| Mutual funds | 4,671 | | 4,671 | — | Short-term investments |
| Foreign currency forward contracts | 134 | — | 134 | — | Prepaid expenses and other |
| Foreign currency forward contracts | (18) | — | (18) | — | Accrued expense and other current liabilities |
| Cross-currency swap | (8,626) | — | (8,626) | — | Accrued expense and other current liabilities |
| Private equity | 917 | — | — | 917 | Other assets |
| Contingent consideration | (136) | — | — | (136) | Other long-term liabilities |
| Total recurring fair value measurements, net | \$1,040,380 | \$639,561 | \$400,038 | \$ 781 | |

| | March 31, 2017 | Quoted prices in active markets for identical assets (level 1) | Significant other observable inputs (level 2) | Significant unobservable inputs (level 3) | Balance Sheet Classification |
|--------------------|----------------|--|---|---|------------------------------|
| Money market funds | \$646,386 | \$646,386 | \$— | \$ — | Cash and cash equivalents |
| Bank-time deposits | 46,605 | 46,605 | — | — | Cash and cash equivalents |
| Commercial paper | 38,268 | — | 38,268 | — | Cash and cash equivalents |
| Corporate bonds | 243,019 | — | 243,019 | — | Short-term investments |
| Bank-time deposits | 175,745 | 175,745 | — | — | Short-term investments |
| Commercial paper | 25,936 | — | 25,936 | — | Short-term investments |

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| | | | | | |
|--|-------------|-----------|-----------|-----------|---------------------------------------|
| Mutual funds | 4,232 | — | 4,232 | — | Short-term investments |
| Foreign currency forward contracts | 2 | — | 2 | — | Prepaid expenses and other |
| Foreign currency forward contracts | (352 |) — | (352 |) — | Accrued and other current liabilities |
| Private equity | 570 | — | — | 570 | Other assets |
| Contingent consideration | (6,465 |) — | — | (6,465 |) Other long-term liabilities |
| Total recurring fair value measurements, net | \$1,173,946 | \$868,736 | \$311,105 | \$ (5,895 |) |

In September 2017, we recognized a reduction to general and administrative expense of \$7,012 for the decrease in fair value of the contingent consideration liability associated with the Social Point acquisition, which reduced the fair value of the

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contingent consideration liability to \$136 after the impact of foreign exchange. The reduction resulted from the lower probability of Social Point achieving certain performance measures in the 12 and 24-month periods following the acquisition.

The fair value of contingent consideration was estimated using a Monte-Carlo simulation model, which included significant unobservable Level 3 inputs, such as projected financial performance over the earn-out period along with estimates for market volatility and the discount rate applicable to potential cash payouts.

We did not have any transfers between Level 1 and Level 2 fair value measurements, nor did we have any transfers into or out of Level 3 during the nine months ended December 31, 2017.

Debt

As of December 31, 2017, the estimated fair value of our 1.00% Convertible Notes due 2018 (the "1.00% Convertible Notes") was \$72,227. The fair value was determined using Level 2 inputs, observable market data, for the 1.00% Convertible Notes and their embedded option feature. See Note 9 for additional information regarding our 1.00% Convertible Notes.

4. SHORT-TERM INVESTMENTS

Our short-term investments consisted of the following:

| | December 31, 2017 | | | |
|--------------------------------|------------------------|-------|----------|------------|
| | Gross Unrealized | | | |
| | Cost or Amortized Cost | Gains | Losses | Fair Value |
| Short-term investments | | | | |
| Bank time deposits | \$ 166,321 | \$— | \$— | \$ 166,321 |
| Available-for-sale securities: | | | | |
| Corporate bonds | 363,127 | 18 | (729) | 362,416 |
| Commercial paper | 13,921 | — | — | 13,921 |
| Mutual funds | 4,665 | 15 | (9) | 4,671 |
| Total short-term investments | \$ 548,034 | \$ 33 | \$ (738) | \$ 547,329 |

| | March 31, 2017 | | | |
|--------------------------------|------------------------|--------|----------|------------|
| | Gross Unrealized | | | |
| | Cost or Amortized Cost | Gains | Losses | Fair Value |
| Short-term investments | | | | |
| Bank time deposits | \$ 175,745 | \$— | \$— | \$ 175,745 |
| Available-for-sale securities: | | | | |
| Corporate bonds | 243,140 | 98 | (219) | 243,019 |
| Commercial paper | 25,938 | 5 | (7) | 25,936 |
| Mutual funds | 4,118 | 123 | (9) | 4,232 |
| Total short-term investments | \$ 448,941 | \$ 226 | \$ (235) | \$ 448,932 |

Based on our review of investments with unrealized losses, we did not consider these investments to be other-than-temporarily impaired as of December 31, 2017 or March 31, 2017.

The following table summarizes the contracted maturities of our short-term investments at December 31, 2017:

| | December 31, 2017 | |
|------------------------------|-------------------|------------|
| | Amortized Cost | Fair Value |
| Short-term investments | | |
| Due in 1 year or less | \$371,567 | \$371,489 |
| Due in 1 - 2 years | 176,467 | 175,840 |
| Total short-term investments | \$548,034 | \$547,329 |

5. DERIVATIVE INSTRUMENTS AND HEDGING ACTIVITIES

Our risk management strategy includes the use of derivative financial instruments to reduce the volatility of earnings and cash flows associated with changes in foreign currency exchange rates. We do not enter into derivative financial contracts for speculative or trading purposes. We recognize derivative instruments as either assets or liabilities on our Condensed Consolidated Balance Sheets, and we measure those instruments at fair value. We classify cash flows from derivative transactions as cash flows from operating activities in our Condensed Consolidated Statements of Cash Flows.

Foreign currency forward contracts

The following table shows the gross notional amounts of foreign currency forward contracts:

| | December 31, March 31, | |
|--|------------------------|------------|
| | 2017 | 2017 |
| Forward contracts to sell foreign currencies | \$ 130,763 | \$ 177,549 |
| Forward contracts to purchase foreign currencies | 3,883 | 9,170 |

For the three months ended December 31, 2017 and 2016, we recorded a loss of \$620 and a gain of \$11,158, respectively, and for the nine months ended December 31, 2017 and 2016, we recorded a loss of \$15,325 and a gain of \$11,731, respectively, related to foreign currency forward contracts in Interest and other, net in our Condensed Consolidated Statements of Operations. Our foreign currency exchange forward contracts are not designated as hedging instruments under hedge accounting and are used to reduce the impact of foreign currency on certain balance sheet exposures and certain revenue and expense. These instruments are generally short term in nature, with typical maturities of less than one year, and are subject to fluctuations in foreign exchange rates.

Cross-currency swaps

We entered into a cross-currency swap agreement in August 2017 related to an intercompany loan that has been designated and accounted for as a cash flow hedge of foreign currency exchange risk. The intercompany loan is related to the acquisition of Social Point. As of December 31, 2017, the notional amount of the cross-currency swap is \$129,000. This cross-currency swap mitigates the exposure to fluctuations in the U.S. dollar-euro exchange rate related to the intercompany loan. The critical terms of the cross-currency swap agreement correspond to the intercompany loan and both mature at the same time in 2027; as such, there was no ineffectiveness during the period. Changes in the fair value of this cross-currency swap are recorded in Accumulated other comprehensive income (loss) and offset the change in value of interest and principal payment as a result of changes in foreign exchange rates. Resulting gains or losses from the cross-currency swap are reclassified from Accumulated other comprehensive income (loss) to earnings to completely offset foreign currency transaction gains and losses recognized on the intercompany loan. We recognize the difference between the U.S. dollar interest payments received from the swap counterparty and the U.S. dollar equivalent of the euro interest payments made to the swap counterparty in interest and other, net on our Condensed Consolidated Statement of Operations. There are no credit-risk related contingent features associated with these swaps.

6. INVENTORY

Inventory balances by category are as follows:

| | December 31, 2017 | March 31, 2017 |
|--------------------|----------------------|----------------------|
| Finished products | \$ 27,717 | \$15,530 |
| Parts and supplies | 3,140 | 793 |
| Inventory | \$ 30,857 | \$16,323 |

Estimated product returns included in inventory at December 31, 2017 and March 31, 2017 were \$423 and \$529, respectively.

7. SOFTWARE DEVELOPMENT COSTS AND LICENSES

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

| | December 31, 2017 | | March 31, 2017 | |
|--|-------------------|-------------|----------------|-------------|
| | Current | Non-current | Current | Non-current |
| Software development costs, internally developed | \$30,420 | \$ 477,883 | \$28,959 | \$ 310,229 |
| Software development costs, externally developed | 6,611 | 108,858 | 5,455 | 71,407 |
| Licenses | 2,338 | 125 | 7,307 | 274 |
| Software development costs and licenses | \$39,369 | \$ 586,866 | \$41,721 | \$ 381,910 |

During the three months ended December 31, 2017 and 2016, we recorded \$0 and \$7,731, respectively, and during the nine months ended December 31, 2017 and 2016, we recorded \$960 and \$19,325, respectively, of software development impairment charges (a component of cost of goods sold).

Liability Awards

In September 2017, we reclassified 5,550,000 time and performance based restricted stock units as equity awards.

These awards were granted in prior periods and historically accounted for as liability awards as they previously could be settled only in cash and based on a contractually stipulated cash settlement value. However, in September 2017, at our Annual Meeting of Stockholders, we received stockholder approval to increase the number of shares of Common Stock for which awards may be granted and therefore now have the ability and intent to settle these awards in stock. As a result, we reclassified \$74,707 from Other long-term liabilities to Additional paid-in capital within Stockholders' equity. Additionally, we recognized incremental cost of \$112,789 to reflect the difference between the share price at the time of the modification and the contractually stipulated cash settlement value. Of these incremental costs, \$84,176 was capitalized within Software development costs and licenses, net of current portion; \$23,251 was recorded within Software development costs and royalties (a component of cost of goods sold); and \$5,361 was recorded within Research and development costs.

8. ACCRUED EXPENSES AND OTHER CURRENT LIABILITIES

Accrued expenses and other current liabilities consist of the following:

| | December 31, 2017 | March 31, 2017 |
|--|----------------------|-------------------|
| Software development royalties | \$ 532,665 | \$492,133 |
| Compensation and benefits | 82,703 | 44,843 |
| Business reorganization | 71,105 | 65,935 |
| Licenses | 66,113 | 37,019 |
| Marketing and promotions | 56,189 | 21,030 |
| Deferred acquisition payments | 25,000 | 25,000 |
| Other | 73,570 | 64,915 |
| Accrued expenses and other current liabilities | \$ 907,345 | \$750,875 |

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9. DEBT

Credit Agreement

In December 2017, we entered into a Seventh Amendment to our Second Amended and Restated Credit Agreement (as amended, the "Credit Agreement"). The Credit Agreement provides for borrowings of up to \$100,000 which may be increased by up to \$100,000 pursuant to the terms of the Credit Agreement and which is secured by substantially all of our assets and the equity of our subsidiaries. The Credit Agreement expires on August 18, 2019. Revolving loans under the Credit Agreement bear interest at our election of (a) 0.25% to 0.75% above a certain base rate (4.50% at December 31, 2017) or (b) 1.25% to 1.75% above the LIBOR Rate (approximately 1.57% at December 31, 2017), with the margin rate subject to the achievement of certain average liquidity levels. We are also required to pay a monthly fee on the unused available balance, ranging from 0.25% to 0.375% based on availability. We had no outstanding borrowings at December 31, 2017 and March 31, 2017.

Availability under the Credit Agreement is unrestricted when liquidity, as defined in the Credit Agreement, is at least \$300,000. When liquidity is below \$300,000 availability under the Credit Agreement is restricted by our United States and United Kingdom based accounts receivable and inventory balances. The Credit Agreement also allows for the issuance of letters of credit in an aggregate amount of up to \$5,000.

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

| | December 31, 2017 | March 31, 2017 |
|-------------------------------|----------------------|----------------------|
| Available borrowings | \$ 98,325 | \$98,320 |
| Outstanding letters of credit | 1,664 | 1,664 |

We recorded interest expense and fees related to the Credit Agreement of \$111 and \$111, respectively for the three months ended December 31, 2017 and 2016 and \$332 and \$332 for the nine months ended December 31, 2017 and 2016, respectively. The Credit Agreement contains covenants that substantially limit us and our subsidiaries' ability to create, incur, assume or be liable for indebtedness; dispose of assets outside the ordinary course of business; acquire, merge or consolidate with or into another person or entity; create, incur or allow any lien on any of their respective properties; make investments; or pay dividends or make distributions (each subject to certain limitations); or optionally prepay any indebtedness (subject to certain exceptions, including an exception permitting the redemption of our unsecured convertible senior notes upon the meeting of certain minimum liquidity requirements). In addition, the Credit Agreement provides for certain events of default such as nonpayment of principal and interest, breaches of representations and warranties, noncompliance with covenants, acts of insolvency, default on indebtedness held by third parties and default on certain material contracts (subject to certain limitations and cure periods). The Credit Agreement also contains a requirement that we maintain an interest coverage ratio of more than one to one for the trailing twelve-month period, if certain average liquidity levels fall below \$30,000.

1.00% Convertible Notes Due 2018

On June 18, 2013, we issued \$250,000 aggregate principal amount of 1.00% Convertible Notes due 2018. The 1.00% Convertible Notes were issued at 98.5% of par value for proceeds of \$246,250. Interest on the 1.00% Convertible Notes is payable semi-annually in arrears on July 1st and January 1st of each year, commencing on January 1, 2014. The 1.00% Convertible Notes mature on July 1, 2018, unless earlier repurchased by the Company or converted. We do not have the right to redeem the 1.00% Convertible Notes prior to maturity. We also granted the underwriters a 30-day option to purchase up to an additional \$37,500 principal amount of 1.00% Convertible Notes to cover overallotments, if any. On July 17, 2013, we closed our public offering of \$37,500 principal amount of our 1.00% Convertible Notes as a result of the underwriters exercising their overallotment option in full on July 12, 2013, bringing the total proceeds to \$283,188.

The 1.00% Convertible Notes are convertible at an initial conversion rate of 46.4727 shares of our common stock per \$1 principal amount of 1.00% Convertible Notes (representing an initial conversion price of approximately \$21.52 per share of common stock for a total of approximately 13,361,000 underlying conversion shares) subject to adjustment in certain circumstances. Holders were able to convert the 1.00% Convertible Notes at their option prior to the close of

business on the business day immediately preceding January 1, 2018 only under the following circumstances:

(1) during any fiscal quarter commencing after September 30, 2013, if the last reported sale price of the common stock for at least 20 trading days (whether or not consecutive) during a period of 30 consecutive trading days ending on the last trading day of the preceding fiscal quarter is greater than or equal to 130% of the applicable conversion price on each applicable trading day; (2) during the five business day period after any 10 consecutive trading day period (the "measurement period") in which the trading price per \$1 principal amount of 1.00% Convertible Notes for each day of that measurement period was less than 98% of the product of the last reported sale price of our common stock and the applicable conversion rate on each such day; or (3) upon the occurrence of specified corporate events. On and after January 1, 2018 until the close of business on the business day immediately preceding the maturity date, holders may convert their

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1.00% Convertible Notes at any time, regardless of the foregoing circumstances. Upon conversion, the 1.00% Convertible Notes may be settled, at our election, in cash, shares of our common stock, or a combination of cash and shares of our common stock. Accordingly, as of January 1, 2018, the 1.00% Convertible Notes may be converted at the holder's option through June 30, 2018. During the three and nine months ended December 31, 2017, 1.00% Convertible Notes with an aggregate principal amount of \$40,088 and \$253,986, respectively, were settled, and an additional \$2 were tendered for conversion with January 2018 settlement dates. As a result of early conversions of the 1.00% Convertible Notes, we recorded a gain within Interest and other, net on our Consolidated Statement of Operations of \$0.7 million and \$4.9 million for the three and nine month period ended December 31, 2017.

We elected to settle in shares of our common stock. Our intent and ability, given our option, would be to settle future conversions in shares of our common stock. As such, we have continued to classify these 1.00% Convertible Notes as long-term debt.

Upon the occurrence of certain fundamental changes involving the Company, holders of the 1.00% Convertible Notes may require us to purchase all or a portion of their 1.00% Convertible Notes for cash at a price equal to 100% of the principal amount of the notes to be purchased, plus accrued and unpaid interest (including additional interest, if any) to, but excluding, the fundamental change purchase date.

The indenture governing the 1.00% Convertible Notes contains customary terms and covenants and events of default. If an event of default (as defined therein) occurs and is continuing, the Trustee by notice to the Company, or the holders of at least 25% in aggregate principal amount of the 1.00% Convertible Notes then outstanding by notice to the Company and the Trustee, may, and the Trustee at the request of such holders shall, declare 100% of the principal of and accrued and unpaid interest (including additional interest, if any) on all the 1.00% Convertible Notes to be due and payable. In the case of an event of default arising out of certain bankruptcy events, 100% of the principal of and accrued and unpaid interest (including additional interest, if any), on the 1.00% Convertible Notes will automatically become due and payable immediately.

The 1.00% Convertible Notes are senior unsecured obligations and rank senior in right of payment to our existing and future indebtedness that is expressly subordinated in right of payment to the 1.00% Convertible Notes; equal in right of payment to our existing and future indebtedness that is not so subordinated; effectively junior in right of payment to any of our secured indebtedness to the extent of the value of the assets securing such indebtedness; and structurally junior to all existing and future indebtedness incurred by our subsidiaries.

We separately account for the liability and equity components of the 1.00% Convertible Notes in a manner that reflects our nonconvertible debt borrowing rate. We estimated the fair value of the 1.00% Convertible Notes to be \$225,567 upon issuance of our 1.00% Convertible Notes, assuming a 6.15% non-convertible borrowing rate. The carrying amount of the equity component was determined to be approximately \$57,621 by deducting the fair value of the liability component from the net proceeds of the 1.00% Convertible Notes. The excess of the principal amount of the liability component over its carrying amount is amortized to interest and other, net over the term of the 1.00% Convertible Notes using the effective interest method. The equity component is not remeasured as long as it continues to meet the conditions for equity classification. In accounting for the \$2,815 of banking, legal and accounting fees related to the issuance of the 1.00% Convertible Notes, we allocated \$2,209 to the liability component and \$606 to the equity component. Debt issuance costs attributable to the liability component are being amortized to interest and other, net over the term of the 1.00% Convertible Notes, and issuance costs attributable to the equity component were netted with the equity component in additional paid-in capital.

As of December 31, 2017 and March 31, 2017, the if-converted value of our 1.00% Convertible Notes exceeded the principal amount of \$14,163 and \$268,149, respectively by \$58,064 and \$470,456, respectively.

The following table provides additional information related to our 1.00% Convertible Notes:

| | December 31, 2017 | March 31, 2017 |
|---|----------------------|-------------------|
| Additional paid-in capital | \$ 35,784 | \$ 35,784 |
| Principal amount of 1.00% Convertible Notes | \$ 14,163 | \$ 268,149 |
| Unamortized discount of the liability component | 311 | 15,751 |

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| | | |
|--|-----------|------------|
| Carrying amount of debt issuance costs | 14 | 469 |
| Net carrying amount of 1.00% Convertible Notes | \$ 13,838 | \$ 251,929 |

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The following table provides the components of interest expense related to our 1.00% Convertible Notes:

| | Three Months Ended December 31, 2017 | | Nine Months Ended December 31, 2016 | |
|--|---|---------|--|----------|
| Cash interest expense (coupon interest expense) | \$(60) | \$698 | \$519 | \$2,115 |
| Non-cash amortization of discount on 1.00% Convertible Notes | 1,509 | 3,285 | 15,424 | 10,289 |
| Amortization of debt issuance costs | 48 | 99 | 471 | 333 |
| Total interest expense related to 1.00% Convertible Notes | \$1,497 | \$4,082 | \$16,414 | \$12,737 |

10. EARNINGS (LOSS) PER SHARE ("EPS")

The following table sets forth the computation of basic and diluted earnings (loss) per share (shares in thousands):

| | Three Months Ended December 31, 2017 | | Nine Months Ended December 31, 2016 | |
|---|---|------------|---|------------|
| Computation of Basic earnings (loss) per share: | | | | |
| Net income (loss) | \$25,140 | \$(29,842) | \$82,680 | \$(31,977) |
| Less: net income allocated to participating securities | (62) | — | (211) | — |
| Net income (loss) for basic earnings (loss) per share calculation | \$25,078 | \$(29,842) | \$82,469 | \$(31,977) |
| Total weighted average shares outstanding—basic | 113,991 | 90,428 | 109,010 | 86,796 |
| Less: weighted average participating shares outstanding | (279) | — | (278) | — |
| Weighted average common shares outstanding—basic | 113,712 | 90,428 | 108,732 | 86,796 |
| Basic earnings (loss) per share | \$0.22 | \$(0.33) | \$0.76 | \$(0.37) |
| Computation of Diluted earnings (loss) per share: | | | | |
| Net income (loss) | \$25,140 | \$(29,842) | \$82,680 | \$(31,977) |
| Less: net income allocated to participating securities | (59) | — | (206) | — |
| Net income (loss) for diluted earnings (loss) per share calculation | \$25,081 | \$(29,842) | \$82,474 | \$(31,977) |
| Weighted average common shares outstanding—basic | 113,712 | 90,428 | 108,732 | 86,796 |
| Add: dilutive effect of common stock equivalents | 4,206 | — | 2,708 | — |
| Weighted average common shares outstanding—diluted | 117,918 | 90,428 | 111,440 | 86,796 |
| Less: weighted average participating shares outstanding | (279) | — | (278) | — |
| Weighted average common shares outstanding- diluted | 117,639 | 90,428 | 111,162 | \$86,796 |
| Diluted earnings (loss) per share | \$0.21 | \$(0.33) | \$0.74 | \$(0.37) |

Certain of our unvested restricted stock awards (including restricted stock units and time-based and market-based restricted stock awards) are considered participating securities since these securities have non-forfeitable rights to dividends or dividend equivalents during the contractual period of the award, and thus require the two-class method of computing EPS.

The calculation of EPS for common stock under the two-class method shown above for the three and nine months ended December 31, 2017 excludes income attributable to the participating securities from the numerator and excludes the dilutive effect of those awards from the denominator.

We incurred a net loss for the three and nine months ended December 31, 2016; therefore, the basic and diluted weighted average shares outstanding for those periods exclude the effect of the unvested share-based awards that are considered participating securities and all common stock equivalents because their effect would be antidilutive. For

the three and nine months ended

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December 31, 2016, we had 4,912,000 of unvested share-based awards that are excluded from the EPS calculation due to the net loss for those periods.

We define common stock equivalents as restricted stock awards and common stock related to the Convertible Notes (see Note 9) outstanding during the period. Common stock equivalents are measured using the treasury stock method, except for the Convertible Notes, which are assessed for their effect on diluted EPS using the more dilutive of the treasury stock method or the if-converted method. Under the provisions of the if-converted method, the Convertible Notes are assumed to be converted and included in the denominator of the EPS calculation and the interest expense, net of tax, recorded in connection with the Convertible Notes is added back to the numerator.

During the nine months ended December 31, 2017, 2,877,000 restricted stock awards vested, we granted 2,303,000 unvested restricted stock awards, and 1,575,000 unvested restricted stock awards were forfeited. The forfeiture of awards resulted in the reversal of expense of \$17,214 and amounts capitalized as software development costs of \$53,569.

11. ACCUMULATED OTHER COMPREHENSIVE LOSS

The following table provides the components of accumulated other comprehensive loss:

| | Nine Months Ended December 31, 2017 | | | | Total |
|--|--|---|---|---|------------|
| | Foreign currency translation adjustments | Unrealized gain (loss) on forward contracts | Unrealized gain (loss) on cross-currency swap | Unrealized gain (loss) on available-for-sales securities(1) | |
| Balance at March 31, 2017 | \$(47,666) | \$ 600 | \$ — | \$ (76) | \$(47,142) |
| Other comprehensive income (loss) before reclassifications | 23,391 | — | (8,626) | (705) | 14,060 |
| Amounts reclassified from accumulated other comprehensive loss | — | — | 1,987 | — | 1,987 |
| Balance at December , 2017 | \$(24,275) | \$ 600 | \$ (6,639) | \$ (781) | \$(31,095) |

| | Nine Months Ended December 31, 2016 | | | | Total |
|--|--|--|--|--|------------|
| | Foreign currency translation adjustments | Unrealized gain (loss) on derivative instruments | Unrealized gain (loss) on available-for-sales securities | | |
| Balance at March 31, 2016 | \$(38,580) | \$ 600 | \$ 84 | | \$(37,896) |
| Other comprehensive (loss) income before reclassifications | (10,067) | — | (221) | | (10,288) |
| Amounts reclassified from accumulated other comprehensive loss | — | — | 9 | | 9 |
| Balance at December 31, 2016 | \$(48,647) | \$ 600 | \$ (128) | | \$(48,175) |

12. COMMITMENTS AND CONTINGENCIES

We have entered into various agreements in the ordinary course of business that require substantial cash commitments over the next several years. Other than agreements entered into in the ordinary course of business and in addition to the agreements requiring known cash commitments as reported in Part II, Item 7 of our Annual Report on Form 10-K for the fiscal year ended March 31, 2017, we did not have any significant changes to our commitments since March 31, 2017.

Legal and Other Proceedings

We are, or may become, subject to demands and claims (including intellectual property claims) and are involved in routine litigation in the ordinary course of business, which we do not believe to be material to our business or financial statements. We have appropriately accrued amounts related to certain of these claims and legal and other proceedings.

While it is reasonably possible that a loss may be incurred in excess of the amounts accrued in our financial statements, we believe that such losses, unless otherwise disclosed, would not be material.

On April 11, 2016, we filed a declaratory judgment action in the United States District Court for the Southern District of New York seeking, among other things, a judicial declaration that Leslie Benzies, the former president of one of our subsidiaries with whom we had been in ongoing discussions regarding his separation of employment, is not entitled to any minimum allocation

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or financial parity with any other person under the applicable royalty plan. We believe we will prevail in this matter, although there can be no assurance of the outcome. On April 12, 2016, Mr. Benzies filed a complaint in the Supreme Court of the State of New York, New York County against us, and certain of our subsidiaries and employees. We removed this case to the United States District Court for the Southern District of New York, but the case was subsequently remanded to state court. The complaint claims damages of at least \$150,000 and contains allegations of breach of fiduciary duty; fraudulent inducement and fraudulent concealment; aiding and abetting breach of fiduciary duty; breach of various contracts; breach of implied duty of good faith and fair dealing; tortious interference with contract; unjust enrichment; reformation; constructive trust; declaration of rights; constructive discharge; defamation and fraud. Motion practice in both the federal and state actions is ongoing. While we believe that we have meritorious defenses to these claims, and we intend to vigorously defend against them and to pursue any counterclaims, we have accrued what we believe to be an adequate amount for this matter, which amounts are classified in Business reorganization within Accrued expenses and other current liabilities in our Condensed Consolidated Balance Sheet (see Note 8). We do not believe that the ultimate outcome of such litigation, even if in excess of our current accrual, will have a material adverse effect on our business, financial condition or results of operations.

13. BUSINESS REORGANIZATION

In the first quarter of fiscal 2018, we announced and initiated actions to implement a strategic reorganization at one of our labels (the "2018 Plan"). In connection with this initiative, we incurred business reorganization expenses of \$700 during the three months ended December 31, 2017 due to true-up of estimates for employee separation costs and \$13,012 during the nine months ended December 31, 2017 due primarily to employee separation costs. Through December 31, 2017, we paid \$3,029 related to these reorganization activities. As of December 31, 2017, \$5,170 remained accrued for in Accrued expenses and other current liabilities and \$4,813 in Other non-current liabilities. Although we may record additional expense or benefit in future periods to true-up estimates, we do not expect to incur additional reorganization costs in connection with the 2018 Plan.

14. INCOME TAXES

On December 22, 2017, the United States ("U.S.") enacted comprehensive tax legislation commonly referred as the "Tax Cuts and Jobs Act" (herein referred to as the "Act"). The Act makes broad and complex changes to the U.S. tax code, which could materially affect us. The Act reduces the U.S. federal corporate tax rate from 35% to 21%, effective January 1, 2018 and requires companies to pay a one-time transition tax on the previously untaxed earnings of certain foreign subsidiaries. In addition, the Act makes other changes that may affect us, beginning April 1, 2018. These changes include but are not limited to (1) a Base Erosion Anti-abuse Tax (BEAT), which is a new minimum tax, (2) generally eliminating U.S. federal income taxes on dividends from foreign subsidiaries, (3) a new provision that taxes global intangible low-taxed income (GILTI), (4) the repeal of the domestic production activity deduction, and (5) other base broadening provisions.

The SEC issued Staff Accounting Bulletin No. 118, Income Tax Accounting Implications of the Tax Cuts and Jobs Act (SAB 118), which provides guidance on accounting for the Act's impact. SAB 118 provides a measurement period, which should not extend beyond one year from the Act enactment date, during which a company acting in good faith may complete the accounting for the impact of the Act under ASC 740. In accordance with SAB 118, the income tax effects of the Act must be reflected in the reporting period in which the accounting under ASC Topic 740 is complete. To the extent the accounting for certain income tax effects of the Act is incomplete, we can determine a reasonable estimate for those effects and record a provisional estimate.

During the three months ended December 31, 2017, we recorded discrete income tax expense of \$18,078 related to the one-time transition tax on the previously untaxed earnings of certain foreign subsidiaries. In addition, as a result of the decrease in the U.S. federal corporate income tax rate from 35% to 21%, we estimated a decrease to net deferred tax assets of \$47,677 and corresponding decrease to valuation allowance of \$47,677, resulting in no impact to our tax provision. The re-measurement of a deferred tax liability relating to indefinite lived intangibles, which cannot be used to offset deferred tax assets, resulted in a discrete tax benefit of \$6,202.

We are currently evaluating the potential impact of the Act, and the amounts recorded represent provisional estimates for certain identified income tax effects, for which the accounting is incomplete but a reasonable estimate can be

determined. Additional information and further analysis is required to determine the untaxed earnings of certain foreign subsidiaries and to evaluate the complexities of the new tax law along with additional interpretative guidance that may be issued. The impact of the Act may differ from these estimates, possibly materially, due to changes in interpretations and assumptions we have made, guidance that may be issued and actions we may take as a result of the Act. We expect to continue to analyze the Act and its impacts and record any adjustments to provisional estimates no later than the third quarter of fiscal 2019. We are also reviewing whether the Act will affect our existing intention to indefinitely reinvest earnings of our foreign subsidiaries and therefore have not recorded any tax liabilities associated with the repatriation of foreign earnings.

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We are also currently analyzing other provisions of the Act that are effective for us April 1, 2018. These provisions include BEAT, the elimination of U.S. federal income taxes on dividends from foreign subsidiaries, GILTI, and other base broadening provisions.

The benefit from income taxes for the three months ended December 31, 2017 is based on our projected annual effective tax rate for fiscal year 2018, adjusted for specific items that are required to be recognized in the period in which they are incurred. The benefit from income taxes was \$12,914 for the three months ended December 31, 2017 as compared to \$2,282 for the prior year period.

As a result of phasing in the reduction in U.S. corporate income tax rate, which was effective January 1, 2018, for our fiscal fourth quarter, our blended statutory rate is 31.6%. When compared to the statutory rate of 31.6%, the effective tax rate of (105.6)% for the three months ended December 31, 2017, was primarily due to provisional amounts recorded as a result of the Act as described above, a tax benefit of \$9,773 as a result of changes in our valuation allowance relating to temporary items and tax carryforwards anticipated to be utilized, as well as \$12,555 of discrete tax benefits recorded during the three months ended December 31, 2017 from changes in unrecognized tax benefits primarily due to expiration of the statute of limitations and \$4,131 of excess tax benefits from employee stock compensation as a component of the benefit from income taxes (previously excess tax benefit and tax deficiencies were recognized in additional paid-in-capital). To a lesser extent, our rate was also impacted by tax credits and geographic mix of earnings.

The benefit from income taxes reported for the nine months ended December 31, 2017 is based on our projected annual effective tax rate for fiscal year 2018, adjusted for specific items that are required to be recognized in the period in which they are incurred. The benefit from income taxes was \$37,331 for the nine months ended December 31, 2017, as compared to \$2,169 for the prior year period.

When compared to the statutory rate of 31.6%, the effective tax rate of (82.3)% for the nine months ended December 31, 2017 was primarily due to provisional amounts recorded as a result of the Act as described above, a tax benefit of \$14,437 as a result of changes in our valuation allowance relating to temporary items and tax carryforwards anticipated to be utilized, a tax benefit of \$8,891 as result of tax credits anticipated to be utilized, as well as \$11,174 of discrete tax benefits recorded during the nine months ended December 31, 2017 from changes in unrecognized tax benefits primarily due to expiration of the statute of limitations and \$28,624 for excess tax benefits from employee stock compensation as a component of the benefit from income taxes (previously excess tax benefit and tax deficiencies were recognized in additional paid-in-capital). To a lesser extent, our rate was also impacted by geographic mix of earnings.

We are regularly examined by domestic and foreign taxing authorities. Examinations may result in tax assessments in excess of amounts claimed and the payment of additional taxes. We believe our tax positions comply with applicable tax law, and that we have adequately provided for reasonably foreseeable tax assessments. It is possible that settlement of audits or the expiration of the statute of limitations may have an impact on our effective tax rate in future periods.

15. SHARE REPURCHASE

Our Board of Directors has authorized the repurchase of up to 14,217,683 shares of our common stock. Under this program, we may purchase shares from time to time through a variety of methods, including in the open market or through privately negotiated transactions, in accordance with applicable securities laws. Repurchases are subject to the availability of stock, prevailing market conditions, the trading price of the stock, the Company's financial performance and other conditions. The program may be suspended or discontinued at any time for any reason.

During the three and nine months ended December 31, 2017 we repurchased 1,063,750 shares of our common stock in the open market for \$110,147, including commissions of \$10, as part of the program. We have repurchased a total of 6,235,080 shares of our common stock under the program and as of December 31, 2017. 7,982,603 shares of our common stock remain available for repurchase under the share repurchase program.

Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations

CAUTIONARY NOTE ABOUT FORWARD-LOOKING STATEMENTS

The statements contained herein which are not historical facts are considered forward-looking statements under federal securities laws and may be identified by words such as "anticipates," "believes," "estimates," "expects," "intends," "plans," "potential," "predicts," "projects," "seeks," "should" "will," or words of similar meaning and include, but are not limited to, statements regarding the outlook for the Company's future business and financial performance. Such forward-looking statements are based on the current beliefs of our management as well as assumptions made by and information currently available to them, which are subject to inherent uncertainties, risks and changes in circumstances that are difficult to predict. Actual outcomes and

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results may vary materially from these forward-looking statements based on a variety of risks and uncertainties including those contained herein, in the Company's Annual Report on Form 10-K for the fiscal year ended March 31, 2017, in the section entitled "Risk Factors," and the Company's other periodic filings with the Securities and Exchange Commission. All forward-looking statements are qualified by these cautionary statements and speak only as of the date they are made. The Company undertakes no obligation to update any forward-looking statement, whether as a result of new information, future events or otherwise.

Our Management's Discussion and Analysis of Financial Condition and Results of Operations ("MD&A") is provided in addition to the accompanying Condensed Consolidated Financial Statements and notes to assist readers in understanding our results of operations, financial condition and cash flows. The following discussion should be read in conjunction with the MD&A and our annual consolidated financial statements and the notes thereto, included in our Annual Report on Form 10-K for the fiscal year ended March 31, 2017.

Overview

Our Business

We are a leading developer, publisher and marketer of interactive entertainment for consumers around the globe. We develop and publish products principally through our two wholly-owned labels Rockstar Games and 2K, as well as our new Private Division label and Social Point, a leading developer of mobile games. Our products are currently designed for console gaming systems such as Sony's PlayStation®4 ("PS4") and PlayStation®3 ("PS3"), Microsoft's Xbox One® ("Xbox One") and Xbox 360® ("Xbox 360"), Nintendo's Switch, and personal computers ("PC"), including smartphones and tablets. We deliver our products through physical retail, digital download, online platforms and cloud streaming services.

We endeavor to be the most creative, innovative and efficient company in our industry. Our core strategy is to capitalize on the popularity of video games by developing and publishing high-quality interactive entertainment experiences across a range of genres. We focus on building compelling entertainment franchises by publishing a select number of titles for which we can create sequels and incremental revenue opportunities through add-on content, microtransactions and online play. Most of our intellectual property is internally owned and developed, which we believe best positions us financially and competitively. We have established a portfolio of proprietary software content for the major hardware platforms in a wide range of genres, including action, adventure, family/casual, racing, role-playing, shooter, sports and strategy, which we distribute worldwide. We believe that our commitment to creativity and innovation is a distinguishing strength, enabling us to differentiate our products in the marketplace by combining advanced technology with compelling storylines and characters that provide unique gameplay experiences for consumers. We have created, acquired or licensed a group of highly recognizable brands to match the broad consumer demographics we serve, ranging from adults to children and game enthusiasts to casual gamers. Another cornerstone of our strategy is to support the success of our products in the marketplace through innovative marketing programs and global distribution on platforms and through channels that are relevant to our target audience.

Our revenue is primarily derived from the sale of internally developed software titles and software titles developed by third parties. Operating margins are dependent in part upon our ability to release new, commercially successful software products and to manage effectively their development costs. We have internal development studios located in Canada, China, Czech Republic, India, Spain, the United Kingdom and the United States.

Software titles published by our Rockstar Games label are primarily internally developed. We expect Rockstar Games, our wholly-owned publisher of the Grand Theft Auto, Max Payne, Midnight Club, Red Dead and other popular franchises, to continue to be a leader in the action/adventure product category and to create groundbreaking entertainment by leveraging our existing titles as well as by developing new brands. We believe that Rockstar has established a uniquely original, popular cultural phenomenon with its Grand Theft Auto series, which is the interactive entertainment industry's most iconic and critically acclaimed brand and has sold-in over 275 million units. The latest installment, Grand Theft Auto V, was released on Sony's PS3 and Microsoft's Xbox 360 in September 2013, on Sony's PS4 and Microsoft's Xbox One in November 2014, and on PC in April 2015. Grand Theft Auto V includes access to Grand Theft Auto Online, which initially launched in October 2013. Rockstar Games is also well known for developing brands in other genres, including the L.A. Noire, Bully and Manhunt franchises. Rockstar Games

continues to expand on our established franchises by developing sequels, offering downloadable episodes, content and virtual currency, and releasing titles for smartphones and tablets.

Our 2K label has published a variety of popular entertainment properties across all key platforms and across a range of genres including shooter, action, role-playing, strategy, sports and family/casual entertainment. We expect 2K to continue to develop new, successful franchises in the future. 2K's internally owned and developed franchises include the critically acclaimed, multi-million unit selling BioShock, Mafia, Sid Meier's Civilization and XCOM series. 2K also publishes externally developed brands, such as Battleborn, Borderlands and Evolve. 2K's realistic sports simulation titles include our flagship NBA 2K series, which continues to be the top-ranked NBA basketball video game, and the WWE 2K professional wrestling series.

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On December 14, 2017, we announced the formation of Private Division, our new label that is dedicated to bringing titles from top independent developers to market. Private Division will publish several upcoming titles based on new IP from renowned industry creative talent, including the previously announced Ancestors: The Humankind Odyssey from Panache Digital Game, a studio led by the creator of the Assassin's Creed franchise Patrice Désilets; an unannounced role-playing game ("RPG") currently codenamed Project Wight from The Outsiders, a studio formed by ex-DICE developers David Goldfarb and Ben Cousins; an unannounced RPG from Obsidian Entertainment led by Tim Cain and Leonard Boyarsky, co-creators of Fallout; and an unannounced sci-fi first-person shooter from V1 Interactive, a studio founded by Halo co-creator Marcus Lehto. Additionally, Private Division is the publisher of Kerbal Space Program, which we acquired in May 2017.

On January 31, 2017, we acquired privately-held Social Point S.L. ("Social Point") for \$175 million in cash and the issuance of 1,480,168 shares of our common stock, plus potential earn-out consideration of up to an aggregate of \$25.9 million in cash and shares of our common stock. Founded in 2008 and headquartered in Barcelona, Spain, Social Point is a developer of popular free-to-play mobile games that focuses on delivering high-quality, deeply-engaging entertainment experiences. Social Point currently has multiple profitable titles in the market, including its two most successful games, Dragon City and Monster Legends. In addition, Social Point has a robust development pipeline with a number of exciting games planned for launch over the next two years.

We are continuing to execute on our growth initiatives in Asia, where our strategy is to broaden the distribution of our existing products and expand our online gaming presence, especially in China and South Korea. 2K has secured a multi-year license from the NBA to develop an online version of the NBA simulation game in China, Taiwan, South Korea and Southeast Asia. In October 2012, NBA 2K Online, our free-to-play NBA simulation game, which was co-developed by 2K and Tencent, launched commercially on the Tencent Games portal in China.

Trends and Factors Affecting our Business

Product Release Schedule. Our financial results are affected by the timing of our product releases and the commercial success of those titles. Our Grand Theft Auto products in particular have historically accounted for a significant portion of our revenue. Sales of Grand Theft Auto products generated 38.1% of our net revenue for the nine months ended December 31, 2017. The timing of our Grand Theft Auto product releases may affect our financial performance on a quarterly and annual basis.

Economic Environment and Retailer Performance. We continue to monitor economic conditions that may unfavorably affect our businesses, such as deteriorating consumer demand, pricing pressure on our products, credit quality of our receivables, and foreign currency exchange rates. Our business is dependent upon a limited number of customers that account for a significant portion of our revenue. Our five largest customers accounted for 67.1% and 65.8% of net revenue during the nine months ended December 31, 2017 and 2016, respectively. As of December 31, 2017 and March 31, 2017, our five largest customers comprised 67.2% and 69.9% of our gross accounts receivable, respectively, with our significant customers (those that individually comprised more than 10% of our gross accounts receivable balance) accounting for 55.8% and 57.6% of such balance at December 31, 2017 and March 31, 2017, respectively. We had three customers who accounted for 29.7%, 14.2%, and 11.9% of our gross accounts receivable as of December 31, 2017 and two customers who accounted for 40.2% and 17.4% of our gross accounts receivable as of March 31, 2017. The economic environment has affected our customers in the past, and may do so in the future. Bankruptcies or consolidations of our large retail customers could seriously hurt our business, due to uncollectible accounts receivables and the concentration of purchasing power among the remaining large retailers. Certain of our large customers sell used copies of our games, which may negatively affect our business by reducing demand for new copies of our games. While the downloadable content that we now offer for certain of our titles may serve to reduce used game sales, we expect used game sales to continue to adversely affect our business.

Hardware Platforms. We derive most of our revenue from the sale of products made for video game consoles manufactured by third parties, such as Sony's PS4 and PS3 and Microsoft's Xbox One and Xbox 360, which comprised 81.9% of our net revenue by product platform for the nine months ended December 31, 2017. The success of our business is dependent upon the consumer acceptance of these consoles and continued growth in the installed base of these platforms. When new hardware platforms are introduced, demand for software used on older platforms

typically declines, which may negatively affect our business during the market transition to the new consoles. We continually monitor console hardware sales. We manage our product delivery on each current and future platform in a manner we believe to be most effective to maximize our revenue opportunities and achieve the desired return on our investments in product development. Accordingly, our strategy is to focus our development efforts on a select number of the highest quality titles for these platforms, while also expanding our offerings for emerging platforms such as tablets, smartphones and online games.

Online Content and Digital Distribution. The interactive entertainment software industry is delivering a growing amount of content through digital online delivery methods. We provide a variety of online delivered products and offerings. Most of our titles that are available through retailers as packaged goods products are also available through direct digital download (from websites we own and others owned by third parties). In addition, we aim to drive ongoing engagement and incremental revenue from recurrent consumer spending on our titles through virtual currency, add-on content, and microtransactions. We also publish

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an expanding variety of titles for tablets and smartphones, which are delivered to consumers through digital download via the Internet. Our "Results of Operations" discloses that net revenue from digital online channels comprised 61.8% of our net revenue by distribution channel for the nine months ended December 31, 2017. We expect online delivery of games and game offerings to continue to grow and to become an increasing part of our business over the long-term.

Product Releases

We released the following key titles during the nine months ended December 31, 2017:

| Title | Publishing Label | Internal or External Development | Platform(s) | Date Released |
|-------------------------------|------------------|----------------------------------|--|--------------------|
| NBA 2K18 | 2K | Internal | Xbox 360, Xbox One, PS3, PS4, PC, Switch (digital) | September 19, 2017 |
| WWE 2K18 | 2K | Internal/External | PS4, Xbox One | October 13, 2017 |
| NBA 2K18 | 2K | Internal | Switch (physical) | October 17, 2017 |
| WWE 2K18 | 2K | Internal/External | PC | October 17, 2017 |
| L.A. Noire | Rockstar Games | Internal | PS4, Xbox One, Switch | November 14, 2017 |
| WWE 2K18 | 2K | Internal/External | Switch | December 6, 2017 |
| L.A. Noire: The VR Case Files | Rockstar Games | Internal | HTC Vive | December 15, 2017 |

Product Pipeline

We have announced the following future key titles to date (this list does not represent all titles currently in development):

| Title | Publishing Label | Internal or External Development | Platform(s) | Expected Release Date |
|--|------------------|----------------------------------|---------------|-----------------------------|
| Kerbal Space Program: Enhanced Edition | Private Division | External | PS4, Xbox One | January 16, 2018 (released) |
| Red Dead Redemption 2 | Rockstar Games | Internal | PS4, Xbox One | October 26, 2018 |

Critical Accounting Policies and Estimates

Our most critical accounting policies, which are those that require significant judgment, include: revenue recognition; price protection and allowances for returns; capitalization and recognition of software development costs and licenses; fair value estimates including inventory obsolescence, and valuation of goodwill, intangible assets and long-lived assets; valuation and recognition of stock-based compensation; and income taxes. In-depth descriptions of these can be found in our Annual Report on Form 10-K for the fiscal year ended March 31, 2017.

Revenue Recognition

As part of our on-going assessment of estimated service periods, during the three months ended June 30, 2017, we extended Grand Theft Auto V's estimated service period from 41 to 50 months, or through December 2018. We expect this change in estimated service period to have a material impact on our Consolidated Financial Statements for fiscal 2018. The impact of this change in estimate is further discussed in Note 1 - Basis of Presentation and Significant Accounting Policies in the Notes to our Condensed Consolidated Financial Statements.

Recently Adopted and Recently Issued Accounting Pronouncements

See Note 1 - Basis of Presentation and Significant Accounting Policies in the Notes to our Condensed Consolidated Financial Statements for further discussion.

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Results of Operations

The following table sets forth, for the periods indicated, our Condensed Consolidated Statements of Operations, net revenue by geographic region, net revenue by product platform and net revenue by distribution channel:

| (thousands of dollars) | Three Months Ended December 31, | | | | Nine Months Ended December 31, | | | |
|------------------------------------|---------------------------------|---------|------------|---------|--------------------------------|---------|-------------|---------|
| | 2017 | | 2016 | | 2017 | | 2016 | |
| Net revenue | \$480,840 | 100.0 % | \$476,473 | 100.0 % | \$1,342,618 | 100.0 % | \$1,208,192 | 100.0 % |
| Cost of goods sold | 267,983 | 55.7 % | 311,074 | 65.3 % | 709,100 | 52.8 % | 708,059 | 58.6 % |
| Gross profit | 212,857 | 44.3 % | 165,399 | 34.7 % | 633,518 | 47.2 % | 500,133 | 41.4 % |
| Selling and marketing | 79,513 | 16.5 % | 95,820 | 20.1 % | 208,641 | 15.5 % | 247,141 | 20.5 % |
| General and administrative | 65,951 | 13.7 % | 52,939 | 11.1 % | 187,378 | 14.0 % | 149,367 | 12.4 % |
| Research and development | 49,977 | 10.4 % | 37,589 | 7.9 % | 142,245 | 10.6 % | 101,494 | 8.4 % |
| Depreciation and amortization | 7,864 | 1.6 % | 7,460 | 1.6 % | 34,490 | 2.6 % | 22,329 | 1.8 % |
| Business reorganization | 700 | 0.1 % | — | — % | 13,012 | 1.0 % | — | — % |
| Total operating expenses | 204,005 | 42.4 % | 193,808 | 40.7 % | 585,766 | 43.6 % | 520,331 | 43.1 % |
| Income (loss) from operations | 8,852 | 1.8 % | (28,409) | (6.0)% | 47,752 | 3.6 % | (20,198) | (1.7)% |
| Interest and other, net | 3,374 | 0.7 % | (3,715) | (0.8)% | (2,403) | (0.2)% | (15,298) | (1.3)% |
| Gain on long-term investments, net | — | — | — | — % | — | — % | 1,350 | 0.1 % |
| Income (loss) before income taxes | 12,226 | 2.5 % | (32,124) | (6.7)% | 45,349 | 3.4 % | (34,146) | (2.8)% |
| Benefit from income taxes | (12,914) | (2.7)% | (2,282) | (0.5)% | (37,331) | (2.8)% | (2,169) | (0.2)% |
| Net income (loss) | \$25,140 | 5.2 % | \$(29,842) | (6.3)% | \$82,680 | 6.2 % | \$(31,977) | (2.6)% |

| | Three Months Ended December 31, | | | | Nine Months Ended December 31, | | | |
|--------------------------------------|---------------------------------|-------|-----------|-------|--------------------------------|-------|-----------|-------|
| | 2017 | | 2016 | | 2017 | | 2016 | |
| Net revenue by geographic region: | | | | | | | | |
| United States | \$262,338 | 54.6% | \$257,504 | 54.0% | \$796,603 | 59.3% | \$703,088 | 58.2% |
| International | 218,502 | 45.4% | 218,969 | 46.0% | 546,015 | 40.7% | 505,104 | 41.8% |
| Net revenue by product platform: | | | | | | | | |
| Console | \$394,461 | 82.0% | \$354,220 | 74.3% | \$1,099,843 | 81.9% | \$961,285 | 79.6% |
| PC and other | 86,379 | 18.0% | 122,253 | 25.7% | 242,775 | 18.1% | 246,907 | 20.4% |
| Net revenue by distribution channel: | | | | | | | | |
| Digital online | \$258,442 | 53.7% | \$240,213 | 50.4% | \$829,564 | 61.8% | \$643,051 | 53.2% |
| Physical retail and other | 222,398 | 46.3% | 236,260 | 49.6% | 513,054 | 38.2% | 565,141 | 46.8% |

Three Months Ended December 31, 2017 Compared to December 31, 2016

| (thousands of dollars) | 2017 | % | 2016 | % | Increase/ (decrease) | % Increase/ (decrease) |
|---|-----------|--------|-----------|--------|----------------------|------------------------|
| Net revenue | \$480,840 | 100.0% | \$476,473 | 100.0% | \$4,367 | 0.9 % |
| Internal royalties | 112,996 | 23.5 % | 103,613 | 21.7 % | 9,383 | 9.1 % |
| Product costs | 69,492 | 14.5 % | 70,089 | 14.7 % | (597) | (0.9)% |
| Software development costs and royalties(1) | 54,008 | 11.2 % | 109,900 | 23.1 % | (55,892) | (50.9)% |
| Licenses | 31,487 | 6.5 % | 27,472 | 5.8 % | 4,015 | 14.6 % |
| Cost of goods sold | 267,983 | 55.7 % | 311,074 | 65.3 % | (43,091) | (13.9)% |
| Gross profit | \$212,857 | 44.3 % | \$165,399 | 34.7 % | \$47,458 | 28.7 % |

(1) Includes \$(8,262) and \$6,022 of stock-based compensation expense in 2017 and 2016, respectively, in software development costs and royalties.

For the three months ended December 31, 2017, net revenue increased by \$4.4 million as compared to the prior year period. This increase was due primarily to (i) an aggregate increase of \$25.9 million from our NBA 2K franchise, (ii) an increase of \$21.9 million from L.A. Noire due to releases in the current quarter on PS4, Xbox One, Switch, and HTC Vive, (iii) \$10.6 million from Social Point titles with no comparable revenues in prior year period, as it was acquired in January 2017, and (iv) a net increase of

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\$6.4 million from our Grand Theft Auto franchise. These increases were partially offset by a decrease of \$52.4 million from our Civilization franchise due to Civilization VI, which released in October 2016, and a decrease of \$7.5 million from Battleborn, which released in May 2016.

Net revenue from console games increased by \$40.2 million and accounted for 82.0% of our total net revenue for the three months ended December 31, 2017, as compared to 74.3% for the prior year period. The increase in net revenue from console games was due primarily to higher net revenues from our NBA 2K franchise, L.A. Noire due to releases in the current quarter on PS4, Xbox One, and Switch, and Grand Theft Auto Online. These increases were offset by lower net revenues from Grand Theft Auto V, our WWE 2K franchise, and Battleborn, which released in May 2016. Net revenue from PC and other decreased by \$35.9 million and accounted for 18.0% of our total net revenue for the three months ended December 31, 2017, as compared to 25.7% for the prior year period. The decrease in net revenue from PC and other was due primarily to lower net revenues from Civilization VI, which released in October 2016. The decrease was partially offset by increases in net revenues from Social Point titles with no comparable revenues in the prior year period, as it was acquired in January 2017, and WWE SuperCard.

Net revenue from digital online channels increased by \$18.2 million and accounted for 53.7% of our total net revenue for the three months ended December 31, 2017, as compared to 50.4% for the prior year period. The increase in net revenue from digital online channels was due to higher net revenue from Grand Theft Auto Online, our NBA 2K franchise, our WWE 2K franchise, and net revenue from Social Point titles with no comparable revenues in prior year period, as it was acquired in January 2017. These increases were partially offset by lower net revenues from Civilization VI, which released in October 2016, and Grand Theft Auto V. Net revenue from physical retail and other channels decreased by \$13.9 million and accounted for 46.3% of our total net revenues for the three months ended December 31, 2017, as compared to 49.6% for the same period in the prior year period. The decrease in net revenue from physical retail and other channels was due primarily to lower net revenues from Grand Theft Auto V, Civilization VI, which released in October 2016, and our WWE 2K franchise. These decreases were partially offset by higher net revenue from L.A. Noire, which released on PS4, Xbox One, Switch and HTC Vive, and our NBA 2K franchise.

Revenues from recurrent consumer spending on our titles through virtual currency, add-on content, and microtransactions increased by \$60.4 million and accounted for 32.0% of net revenue for the three months ended December 31, 2017, as compared to 19.6% of net revenue for the prior year period. The increase in revenues from recurrent consumer spending was primarily due to higher net revenues from Grand Theft Auto Online, our NBA 2K franchise, Social Point titles with no comparable revenues in the prior year period, as it was acquired in January 2017, and WWE SuperCard.

Gross profit as a percentage of net revenue for the three months ended December 31, 2017 was 44.3% as compared to 34.7% for the prior year period. The increase was due primarily to lower software development costs due to (i) lower stock-based compensation expense as a result of forfeited share-based awards and (ii) Mafia III and Civilization VI releasing in the prior year period, partially offset by higher internal royalties as a percentage of net revenue due to the timing of when royalties are earned.

Net revenue earned outside of the United States was relatively flat compared to the prior year period and decreased by \$0.5 million, accounting for 45.4% of our total net revenue for the three months ended December 31, 2017, as compared to 46.0% in the prior year period. Changes in foreign currency exchange rates increased net revenue by \$5.3 million and increased gross profit by \$2.8 million for the three months ended December 31, 2017 as compared to the prior year period.

Operating Expenses

| (thousands of dollars) | 2017 | % of net revenue | 2016 | % of net revenue | Increase/ (decrease) | % Increase/ (decrease) |
|----------------------------|----------|------------------------|----------|------------------------|-------------------------|------------------------------|
| Selling and marketing | \$79,513 | 16.5 % | \$95,820 | 20.1 % | \$(16,307) | (17.0) % |
| General and administrative | 65,951 | 13.7 % | 52,939 | 11.1 % | 13,012 | 24.6 % |
| Research and development | 49,977 | 10.4 % | 37,589 | 7.9 % | 12,388 | 33.0 % |

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| | | | | | | | | | |
|-------------------------------|-----------|------|---|-----------|------|---|----------|-------|---|
| Depreciation and amortization | 7,864 | 1.6 | % | 7,460 | 1.6 | % | 404 | 5.4 | % |
| Business reorganization | 700 | 0.1 | % | — | — | % | 700 | 100.0 | % |
| Total operating expenses(1) | \$204,005 | 42.4 | % | \$193,808 | 40.7 | % | \$10,197 | 5.3 | % |

(1) Includes stock-based compensation expense, which was allocated as follows (in thousands):

| | 2017 | 2016 |
|----------------------------|----------|----------|
| Selling and marketing | \$3,015 | \$2,441 |
| General and administrative | \$16,051 | \$10,382 |
| Research and development | \$2,224 | \$3,243 |

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Changes in foreign currency exchange rates increased total operating expenses by \$4.0 million for the three months ended December 31, 2017, as compared to the prior year period.

Selling and marketing

Selling and marketing expenses decreased by \$16.3 million for the three months ended December 31, 2017, as compared to the prior year period, due primarily to \$18.4 million in lower advertising expenses. Advertising expenses were lower in the current period due primarily to prior year period advertising expenses for Mafia III and Civilization VI, both of which released in October 2016, with no corresponding advertising expense in the current year, partially offset by higher advertising expenses for Grand Theft Auto Online and L.A. Noire. The overall decrease was partially offset by higher personnel costs, due to higher bonuses and higher headcount, including from our acquisition of Social Point.

General and administrative

General and administrative expenses increased by \$13.0 million for the three months ended December 31, 2017, as compared to the prior year period, due to (i) increases in personnel expenses for additional headcount, including from our acquisition of Social Point, (ii) increases in professional fees, including stock and incentive compensation expense related primarily to our management agreement with ZelnickMedia due to the increase in our share price, (iii) increases in IT related expenses from the purchasing of computer hardware and software, and (iv) increases in rent expense due to new locations, including our new corporate headquarters in New York and for Social Point, as well as increased rent at other locations. General and administrative expenses for the three months ended December 31, 2017 and 2016 included occupancy expense (primarily rent, utilities and office expenses) of \$4.5 million and \$4.2 million, respectively, related to our development studios.

Research and development

Research and development expenses increased by \$12.4 million for the three months ended December 31, 2017, as compared to the prior year period. The increase was primarily due to increases in personnel expenses, from additional headcount, including our acquisition of Social Point and an increase in production and development expenses for titles that have not reached technological feasibility.

Depreciation and Amortization

Depreciation and amortization expenses increased by \$0.4 million for the three months ended December 31, 2017 and were relatively flat compared to the prior year period.

Business reorganization

During the three months ended December 31, 2017, we recognized \$0.7 million of business reorganization expense due to the true-up of an estimate relating to employee separation costs in connection with the implementation of a strategic reorganization at one of our labels, with no corresponding costs in the prior year period.

Interest and other, net

Interest and other, net was income of \$3.4 million for the three months ended December 31, 2017, as compared to expense of \$3.7 million for the prior year period. The change was due primarily to lower interest expense as a result of the settlement of our 1.75% Convertible Notes due 2016 (the "1.75% Convertible Notes") in December 2016 and higher interest income due to the nature of our investments and the rise in interest rates, partially offset by lower foreign exchange transaction gains.

Benefit from Income Taxes

The benefit from income taxes for the three months ended December 31, 2017 is based on our projected annual effective tax rate for fiscal year 2018, adjusted for specific items that are required to be recognized in the period in which they are incurred. The benefit from income taxes was \$12.9 million for the three months ended December 31, 2017 as compared to \$2.3 million for the prior year period.

On December 22, 2017, The Tax and Jobs Act (the "Act") was enacted, which lowers U.S. corporate income tax rates as of January 1, 2018. Accordingly, for fiscal year 2018, our blended statutory rate is 31.6%. When compared to the statutory rate of 31.6%, the effective tax rate of (105.6)% for the three months ended December 31, 2017, was primarily due to provisional amounts recorded as a result of the Act (as described in Note 14 of our Condensed Consolidated Financial Statements), recorded tax benefit of \$9.8 million as a result of changes in our valuation

allowance relating to temporary items and tax carryforwards anticipated to be utilized, as well as \$12.6 million of discrete tax benefits recorded during the three months ended December 31, 2017 from changes in unrecognized tax benefits primarily due to expiration in statute of limitations, and \$4.1 million for excess tax benefits from employee stock-based compensation as a component of the benefit from income taxes (previously excess tax benefit and tax

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deficiencies were recognized in additional paid-in-capital). To a lesser extent, our rate was impacted by tax credits and geographic mix of earnings.

In the prior year period, when compared to the statutory rate of 35%, the effective tax rate of 7.1% was lower primarily due to the impact of projected tax benefits relating to tax credits, geographic mix of earnings, and changes in valuation allowance.

The change in effective tax rate, when compared to the prior year period, is primarily due to provisional amounts recorded as a result of the Act (as described in Note 14) as well as the impact of the rate change on our projected annual effective tax rate, discrete tax benefits recorded during the three month period ended December 31, 2017 of \$12.6 million from changes in unrecognized tax benefits primarily due to expiration of statute of limitations, \$4.1 million of excess tax benefits from employee stock-based compensation as a component of the benefit from income taxes (previously excess tax benefit and tax deficiencies were recognized in additional paid-in-capital), and increased benefits from tax credits and changes in valuation allowance.

We anticipate that additional excess tax benefits, tax credits as well as changes in valuation allowance may arise in future period which could have a significant impact on our effective tax rate.

We are regularly examined by domestic and foreign taxing authorities. Examinations may result in tax assessments in excess of amounts claimed and the payment of additional taxes. We believe our tax positions comply with applicable tax law, and that we have adequately provided for reasonably foreseeable tax assessments. It is possible that settlement of audits and/or the expiration of the statute of limitations could have an impact on our effective tax rate in future periods.

Net income (loss) and earnings (loss) per share

For the three months ended December 31, 2017, net income was \$25.1 million, as compared to net loss of \$29.8 million in the prior year period. For the three months ended December 31, 2017, basic and diluted earnings per share were \$0.22 and \$0.21, respectively, as compared to loss per share of \$0.33 in the prior year period. Basic weighted average shares of 113.7 million were 23.3 million shares higher as compared to the prior year period, due primarily to the settlement of our 1.75% Convertible Notes and our 1.00% Convertible Notes, which were converted to shares of our common stock using the stated conversion rate and, to a lesser extent, the vesting of restricted stock awards. See Note 10 to our Condensed Consolidated Financial Statements for additional information regarding earnings per share. Nine Months Ended December 31, 2017 Compared to December 31, 2016

| (thousands of dollars) | 2017 | % | 2016 | % | Increase/ (decrease) | % Increase/ (decrease) |
|---|-------------|--------|-------------|--------|-------------------------|------------------------------|
| Net revenue | \$1,342,618 | 100.0% | \$1,208,192 | 100.0% | \$134,426 | 11.1 % |
| Internal royalties | 294,749 | 22.0 % | 240,711 | 19.9 % | 54,038 | 22.4 % |
| Software development costs and royalties ⁽¹⁾ | 164,419 | 12.2 % | 218,753 | 18.1 % | (54,334) | (24.8)% |
| Product costs | 156,124 | 11.6 % | 170,127 | 14.1 % | (14,003) | (8.2)% |
| Licenses | 93,808 | 7.0 % | 78,468 | 6.5 % | 15,340 | 19.5 % |
| Cost of goods sold | 709,100 | 52.8 % | 708,059 | 58.6 % | 1,041 | 0.1 % |
| Gross profit | \$633,518 | 47.2 % | \$500,133 | 41.4 % | 133,385 | 26.7 % |

⁽¹⁾ Includes \$23,284 and \$15,974 of stock-based compensation expense in 2017 and 2016, respectively, in software development costs and royalties.

For the nine months ended December 31, 2017, net revenue increased by \$134.4 million as compared to the prior year period. This increase was due primarily to (i) an increase of \$122.5 million from our NBA 2K franchise, (ii) an increase of \$43.8 million from our Grand Theft Auto franchise, (iii) \$26.3 million from Social Point titles with no comparable revenues in prior year period as it was acquired in January 2017, and (iv) an increase of \$21.6 million from L.A. Noire due to releases on PS4, Xbox One, Switch, and HTC Vive. These increases were partially offset by a decrease of \$41.0 million in Civilization VI, which released in October 2016 and a decrease of \$25.0 million from BioShock: The Collection, which released in September 2016.

Net revenue from console games increased by \$138.6 million and accounted for 81.9% of our total net revenue for the nine months ended December 31, 2017, as compared to 79.6% for the prior year period. The increase in net revenue from console games was due primarily to our NBA 2K franchise and Grand Theft Auto Online. These increases were partially offset by lower net revenues from Grand Theft Auto V and BioShock: The Collection, which released in September 2016. Net revenue from PC and other decreased by \$4.1 million and accounted for 18.1% of our total net revenue for the nine months ended December 31, 2017, as compared to 20.4% for the prior year period. The decrease in net revenue from PC and other was due primarily to lower net revenues from Civilization VI, which released in October 2016, Grand Theft Auto V, and Battleborn, which released in May

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2016. These decreases were partially offset by net revenues from Social Point titles with no comparable revenues in the prior year period as it was acquired in January 2017 and higher net revenues from WWE SuperCard, our NBA 2K franchise, Grand Theft Auto Online, our XCOM franchise, and Carnival Games.

Net revenue from digital online channels increased by \$186.5 million and accounted for 61.8% of our total net revenue for the nine months ended December 31, 2017, as compared to 53.2% for the prior year period. The increase in net revenue from digital online channels was due to higher net revenues from our NBA 2K franchise and Grand Theft Auto Online, partially offset by lower net revenues from Civilization VI, which released in October 2016, and Grand Theft Auto V. Net revenue from physical retail and other channels decreased by \$52.1 million and accounted for 38.2% of our total net revenues for the nine months ended December 31, 2017, as compared to 46.8% for the same period in the prior year period. The decrease in net revenue from physical retail and other channels was due primarily to lower net revenues from Grand Theft Auto V, BioShock: The Collection, which released in September 2016, Civilization VI, which released in October 2016, and Battleborn, which released in May 2016. These decreases were partially offset by higher net revenues from L.A. Noire due to releases on PS4, Xbox One, Switch, and HTC Vive as well as in-game advertising revenue from Social Point titles with no comparable revenues in the prior year period. Revenues from recurrent consumer spending on our titles through virtual currency, add-on content, and microtransactions increased by \$220.7 million and accounted for 40.3% of net revenue for the nine months ended December 31, 2017, as compared to 26.5% of net revenue for the prior year period. The increase in revenues from recurrent consumer spending was primarily due to higher net revenues from Grand Theft Auto Online, our NBA 2K franchise, WWE Supercard, and Social Point titles with no comparable revenues in prior year period as it was acquired in January 2017.

Gross profit as a percentage of net revenue for the nine months ended December 31, 2017 was 47.2% as compared to 41.4% for the prior year period. The percentage increase was due primarily to lower software development costs as a percentage of net revenue due to Mafia III and Civilization VI releasing in the prior year period, as well as lower product costs as a percentage of net revenue due to the decrease in net revenue from physical and retail sales. The increase was offset by higher internal royalties as a percentage of net revenue due to the timing of when royalties are earned and higher stock-based compensation costs as a percentage of net revenue due to previously issued share based awards, which were historically classified as liability awards, being modified to equity awards during the period. This modification reflects the impact of differences between the share price at the time of the modification and contractually stipulated cash settlement values of the awards prior to the modification. This impact was partially offset by a reversal of expense due to forfeited awards.

Net revenue earned outside of the United States increased by \$40.9 million, and accounted for 40.7% of our total net revenue for the nine months ended December 31, 2017, as compared to 41.8% in the prior year period. The increase in net revenue outside of the United States was due primarily to Grand Theft Auto Online, our NBA franchise, and Social Point titles with no comparable revenues in the prior year period. These increases were offset by a decrease in Civilization VI, which released in October 2016 and a decrease in Grand Theft Auto V. Changes in foreign currency exchange rates increased net revenue by \$3.6 million and increased gross profit by \$1.8 million for the nine months ended December 31, 2017 as compared to the prior year period.

Operating Expenses

| (thousands of dollars) | 2017 | % of net revenue | 2016 | % of net revenue | Increase/ (decrease) | % Increase/ (decrease) |
|-------------------------------|-----------|------------------------|-----------|------------------------|-------------------------|------------------------------|
| Selling and marketing | \$208,641 | 15.5 % | \$247,141 | 20.5 % | \$(38,500) | (15.6 %) % |
| General and administrative | 187,378 | 14.0 % | 149,367 | 12.4 % | 38,011 | 25.4 % |
| Research and development | 142,245 | 10.6 % | 101,494 | 8.4 % | 40,751 | 40.2 % |
| Depreciation and amortization | 34,490 | 2.6 % | 22,329 | 1.8 % | 12,161 | 54.5 % |
| Business reorganization | 13,012 | 1.0 % | — | — % | 13,012 | 100.0 % |
| Total operating expenses (1) | \$585,766 | 43.6 % | \$520,331 | 43.1 % | \$65,435 | 12.6 % |

(1) Includes stock-based compensation expense, which was allocated as follows (in thousands):

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| | 2017 | 2016 |
|----------------------------|----------|----------|
| Selling and marketing | \$8,787 | \$7,269 |
| General and administrative | \$48,629 | \$26,861 |
| Research and development | \$12,990 | \$5,317 |
| Business reorganization | \$2,421 | \$— |

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Changes in foreign currency exchange rates increased total operating expenses by \$2.6 million for the nine months ended December 31, 2017, as compared to the prior year period.

Selling and marketing

Selling and marketing expenses decreased by \$38.5 million for the nine months ended December 31, 2017, as compared to the prior year period, due primarily to \$49.8 million in lower advertising expenses. Advertising expenses were lower in the current year period due primarily to the releases of Mafia III and Civilization VI in October 2016 and Battleborn in May 2016, partially offset by higher marketing in the current year period for Grand Theft Auto Online and Read Dead Redemption 2. The overall decrease was partially offset by higher personnel expenses, primarily due to higher incentive compensation expense.

General and administrative

General and administrative expenses increased by \$38.0 million for the nine months ended December 31, 2017, as compared to the prior year period, due primarily to increases in personnel expenses, including stock and incentive compensation expense, due to additional headcount, including our acquisition of Social Point, increases in professional fees, related primarily to our management agreement with ZelnickMedia as a result of the increase in our share price, and increases in rent expense due to new locations, including our new corporate headquarters in New York and for Social Point, as well as increased rent at other locations. The overall increase was partially offset primarily by a \$7.0 million reduction of expense related to the fair value as of December 31, 2017 of contingent consideration included in the Social Point acquisition.

General and administrative expenses for the nine months ended December 31, 2017 and 2016 included occupancy expense (primarily rent, utilities and office expenses) of \$13.2 million and \$11.8 million, respectively, related to our development studios.

Research and development

Research and development expenses increased by \$40.8 million for the nine months ended December 31, 2017, as compared to the prior year period, due primarily to increased personnel expense due to increased headcount, including our acquisition of Social Point, and due to a \$5.4 million stock compensation charge due to a share-based award modification. These increases were partially offset by lower production expenses for titles that have not reached technological feasibility.

Depreciation and Amortization

Depreciation and amortization expenses for the nine months ended December 31, 2017 increased by \$12.2 million, as compared to the prior year period, due primarily to the recognition of an \$11.3 million impairment charge in September 2017, as a result of our decision not to proceed with further development of certain IPR&D from our acquisition of Social Point.

Business reorganization

During the nine months ended December 31, 2017, we announced and initiated actions to implement a strategic reorganization at one of our labels. In connection with this initiative, we incurred business reorganization expenses of \$13.0 million for the nine months ended December 31, 2017 due primarily to employee separation costs, with no corresponding costs in the prior year period.

Interest and other, net

Interest and other, net was an expense of \$2.4 million for the nine months ended December 31, 2017, as compared to \$15.3 million for the prior year period. The decrease was due primarily to lower interest expense as a result of the settlement of our 1.75% Convertible Notes in December 2016 and higher gains on early conversions of our 1.00% Convertible Notes as well as higher interest income due to the nature of our investments and the rise in interest rates, partially offset by foreign exchange transaction losses in the nine months ended December 31, 2017 as compared to foreign exchange transaction gains in the prior year period.

Benefit from Income Taxes

The benefit from income taxes for the nine months ended December 31, 2017 is based on our projected annual effective tax rate for fiscal year 2018, adjusted for specific items that are required to be recognized in the period in which they are incurred. The benefit from income taxes was \$37.3 million for the nine months ended December 31,

2017, as compared to a benefit of \$2.2 million for the prior year period.

When compared to the statutory rate of 31.6%, the effective tax rate of (82.3)% for the nine months ended December 31, 2017 was primarily due to provisional amounts recorded as a result of the Act (as described in Note 14), recorded tax benefit of \$14.4 million as a result of changes in our valuation allowance relating to temporary items and tax carryforwards anticipated to be utilized, \$8.9 million tax benefit resulting from tax credits anticipated to be utilized, as well as discrete tax benefits recorded during the nine month period of \$11.2 million from changes in unrecognized tax benefits primarily due to expiration of statute of

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limitations and \$28.6 million of excess tax benefits from employee stock-based compensation as a component of the benefit from income taxes (previously excess tax benefit and tax deficiencies were recognized in additional paid-in-capital). To a lesser extent, our rate was also impacted by tax credits and geographic mix of earnings. In the prior year period, when compared to the statutory rate of 35%, the effective tax rate of 6.4% was lower primarily due to projected tax benefits relating to tax credits, geographic mix of earnings, and changes in valuation allowance.

The change in effective tax rate, when compared to the prior year period, is primarily due to provisional amounts recorded as a result of the Act (as described in Note 14) as well as the impact on the overall rate change in our projected annual effective tax rate, discrete tax benefits recorded during the nine months ended December 31, 2017 of \$11.2 million from changes in unrecognized tax benefit primarily due to expiration of statute of limitations, \$28.6 million for excess tax benefits from employee stock compensation as a component of the benefit from income taxes (previously excess tax benefit and tax deficiencies were recognized in additional paid-in-capital), and increased benefits from tax credits and changes in valuation allowance.

We anticipate that additional excess tax benefits, tax credits, as well as changes in valuation allowance may arise in future periods, which could have a significant impact on our effective tax rate.

We are regularly examined by domestic and foreign taxing authorities. Examinations may result in tax assessments in excess of amounts claimed and the payment of additional taxes. We believe our tax positions comply with applicable tax law, and that we have adequately provided for reasonably foreseeable tax assessments. It is possible that settlement of audits or the expiration of the statute of limitations could have an impact on our effective tax rate in future periods.

Net income (loss) and earnings (loss) per share

For the nine months ended December 31, 2017, net income was \$82.7 million, as compared to a net loss of \$32.0 million in the prior year period. For the nine months ended December 31, 2017, basic earnings per share was \$0.76 compared to loss per share of \$0.37 and diluted earnings per share was \$0.74 as compared to loss per share of \$0.37 in the prior year period. Basic weighted average shares of 108.7 million were 21.9 million shares higher as compared to the prior year period, due primarily to the settlement of our 1.75% Convertible Notes and our 1.00% Convertible Notes by converting those notes to shares of our common stock using the stated conversion rate and, to a lesser extent, the vesting of restricted stock awards. See Note 10 to our Condensed Consolidated Financial Statements for additional information regarding earnings per share.

Liquidity and Capital Resources

Our primary cash requirements have been to fund (i) the development, manufacturing and marketing of our published products, (ii) working capital, (iii) acquisitions and (iv) capital expenditures. We expect to rely on cash and cash equivalents as well as on short-term investments, funds provided by our operating activities and our Credit Agreement to satisfy our working capital needs.

Short-term Investments

As of December 31, 2017, we had \$547.3 million of short-term investments, which are highly liquid in nature and represent an investment of cash that is available for current operations. From time to time, we may purchase additional short-term investments depending on future market conditions and liquidity needs.

Credit Agreement

In December 2017, we entered into a Seventh Amendment to our Second Amended and Restated Credit Agreement (as amended, the "Credit Agreement"). The Credit Agreement provides for borrowings of up to \$100.0 million, which may be increased by up to \$100.0 million pursuant to the terms of the Credit Agreement, and is secured by substantially all of our assets and the equity of our subsidiaries. The Credit Agreement expires on August 18, 2019. Revolving loans under the Credit Agreement bear interest at our election of (a) 0.25% to 0.75% above a certain base rate (4.50% at December 31, 2017), or (b) 1.25% to 1.75% above the LIBOR Rate (approximately 1.57% at December 31, 2017), with the margin rate subject to the achievement of certain average liquidity levels. We are also required to pay a monthly fee on the unused available balance, ranging from 0.25% to 0.375% based on availability.

Availability under the Credit Agreement is unrestricted when liquidity is at least \$300.0 million. When liquidity is below \$300.0 million, availability under the Credit Agreement is restricted by our United States and United Kingdom based accounts receivable and inventory balances. The Credit Agreement also allows for the issuance of letters of credit in an aggregate amount of up to \$5.0 million.

As of December 31, 2017, there was \$98.3 million available to borrow under the Credit Agreement and we had \$1.7 million of letters of credit outstanding. At December 31, 2017, we had no outstanding borrowings under the Credit Agreement.

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The Credit Agreement contains covenants that substantially limit us and our subsidiaries' ability to: create, incur, assume or be liable for indebtedness; dispose of assets outside the ordinary course of business; acquire, merge or consolidate with or into another person or entity; create, incur or allow any lien on any of their respective properties; make investments; or pay dividends or make distributions (each subject to certain limitations); or optionally prepay any indebtedness (subject to certain exceptions, including an exception permitting the redemption of our unsecured convertible senior notes upon the meeting of certain minimum liquidity requirements). In addition, the Credit Agreement provides for certain events of default such as nonpayment of principal and interest, breaches of representations and warranties, noncompliance with covenants, acts of insolvency, default on indebtedness held by third parties and default on certain material contracts (subject to certain limitations and cure periods). The Credit Agreement also contains a requirement that we maintain an interest coverage ratio of more than one to one for the trailing twelve-month period, if certain average liquidity levels fall below \$30.0 million.

1.00% Convertible Notes Due 2018

On June 18, 2013, we issued \$250.0 million aggregate principal amount of 1.00% Convertible Notes due 2018. The 1.00% Convertible Notes were issued at 98.5% of par value for proceeds of \$246.3 million. Interest on the 1.00% Convertible Notes is payable semi-annually in arrears on July 1st and January 1st of each year, commencing on January 1, 2014. The 1.00% Convertible Notes mature on July 1, 2018, unless earlier repurchased by the Company or converted. We do not have the right to redeem the 1.00% Convertible Notes prior to maturity. We also granted the underwriters a 30-day option to purchase up to an additional \$37.5 million principal amount of 1.00% Convertible Notes to cover overallotments, if any. On July 17, 2013, we closed our public offering of \$37.5 million principal amount of our 1.00% Convertible Notes as a result of the underwriters exercising their overallotment option in full on July 12, 2013, bringing the total proceeds to \$283.2 million.

The 1.00% Convertible Notes are convertible at an initial conversion rate of 46.4727 shares of our common stock per \$1,000 principal amount of 1.00% Convertible Notes (representing an initial conversion price of approximately \$21.52 per share of common stock for a total of approximately 13,361,000 underlying conversion shares) subject to adjustment in certain circumstances. Holders were able to convert the 1.00% Convertible Notes at their option prior to the close of business on the business day immediately preceding January 1, 2018 only under the following circumstances: (1) during any fiscal quarter commencing after September 30, 2013, if the last reported sale price of the common stock for at least 20 trading days (whether or not consecutive) during a period of 30 consecutive trading days ending on the last trading day of the preceding fiscal quarter is greater than or equal to 130% of the applicable conversion price on each applicable trading day; (2) during the five business day period after any 10 consecutive trading day period (the "measurement period") in which the trading price per \$1 principal amount of 1.00% Convertible Notes for each day of that measurement period was less than 98% of the product of the last reported sale price of our common stock and the applicable conversion rate on each such day; or (3) upon the occurrence of specified corporate events. On and after January 1, 2018 until the close of business on the business day immediately preceding the maturity date, holders may convert their 1.00% Convertible Notes at any time, regardless of the foregoing circumstances. Upon conversion, the 1.00% Convertible Notes may be settled, at our election, in cash, shares of our common stock, or a combination of cash and shares of our common stock. Accordingly, as of January 1, 2018, the 1.00% Convertible Notes may be converted at the holder's option through June 30, 2018. During the three months ended December 31, 2017, 1.00% Convertible Notes with an aggregate principal amount of \$40.1 million were tendered for conversion, which we elected to settle in shares of our common stock. Our intent and ability, given our option, would be to settle future conversions in shares of our common stock. As such, we have continued to classify these 1.00% Convertible Notes as long-term debt.

The indenture governing the 1.00% Convertible Notes contains customary terms and covenants and events of default.

Financial Condition

We are subject to credit risks, particularly if any of our receivables represent a limited number of customers or are concentrated in foreign markets. If we are unable to collect our accounts receivable as they become due, it could adversely affect our liquidity and working capital position.

Generally, we have been able to collect our accounts receivable in the ordinary course of business. We do not hold any collateral to secure payment from customers. We have trade credit insurance on the majority of our customers to mitigate accounts receivable risk.

A majority of our trade receivables are derived from sales to major retailers and distributors. Our five largest customers accounted for 67.1% and 65.8% of net revenue during the three months ended December 31, 2017 and 2016, respectively. As of December 31, 2017 and March 31, 2017, five customers accounted for 67.2% and 69.9% of our gross accounts receivable, respectively. Customers that individually accounted for more than 10% of our gross accounts receivable balance comprised 55.8% and 57.6% of such balances at December 31, 2017 and March 31, 2017, respectively. We had three customers who accounted for 29.7%, 14.2%, and 11.9% of our gross accounts receivable as of December 31, 2017, respectively, and two customers who accounted for 40.2% and 17.4% of our gross accounts receivable as of March 31, 2017, respectively. Based upon performing ongoing credit

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evaluations, maintaining trade credit insurance on a majority of our customers and our past collection experience, we believe that the receivable balances from these largest customers do not represent a significant credit risk, although we actively monitor each customer's credit worthiness and economic conditions that may affect our customers' business and access to capital. We are monitoring the current global economic conditions, including credit markets and other factors as it relates to our customers in order to manage the risk of uncollectible accounts receivable.

We believe our current cash and cash equivalents, short-term investments and projected cash flows from operations, along with availability under our Credit Agreement will provide us with sufficient liquidity to satisfy our cash requirements for working capital, capital expenditures and commitments on both a short-term and long-term basis.

As of December 31, 2017, the amount of cash and cash equivalents held outside of the U.S. by our foreign subsidiaries was \$306.0 million. These balances are dispersed across various locations around the world. We believe that such dispersion meets the business and liquidity needs of our foreign affiliates. In addition, we expect for the foreseeable future to have the ability to generate sufficient cash domestically to support ongoing operations.

On December 22, 2017, the U.S. enacted comprehensive tax legislation commonly referred to as the "Tax Cuts and Jobs Act" (herein referred to as the "Act"). The Act makes broad and complex changes to the U.S. tax code, which could materially affect us.

The Act includes a number of provisions, including international provisions, which generally establish a territorial-style system for taxing foreign-source income of domestic multinational corporations. We are reviewing whether the Act will affect our current intention to indefinitely reinvest undistributed earnings of our foreign subsidiaries and therefore have not recorded any tax liabilities associated with the repatriation of foreign earnings. Our Board of Directors has authorized the repurchase of up to 14,217,683 shares of our common stock. Under this program, we may purchase shares from time to time through a variety of methods, including in the open market or through privately negotiated transactions, in accordance with applicable securities laws. Repurchases are subject to the availability of stock, prevailing market conditions, the trading price of the stock, the Company's financial performance and other conditions. The program may be suspended or discontinued at any time for any reason.

During the three and nine months ended December 31, 2017 we repurchased 1,063,750 shares of our common stock in the open market for \$110.1 million as part of the program. We have repurchased a total of 6,235,080 shares of our common stock under the program, and as of December 31, 2017, 7,982,603 shares of our common stock remain available for repurchase under the share repurchase program.

Our changes in cash flows were as follows:

| | Nine Months Ended | |
|---|-------------------|-----------|
| | December 31, | |
| (thousands of dollars) | 2017 | 2016 |
| Net cash provided by operating activities | 204,085 | 239,602 |
| Net cash (used in) provided by investing activities | (182,515) | 48,187 |
| Net cash used in financing activities | (205,066) | (35,235) |
| Effects of foreign currency exchange rates on cash and cash equivalents | 14,555 | (11,866) |
| Net change in cash and cash equivalents | \$(168,941) | \$240,688 |

At December 31, 2017, we had \$774.5 million of cash and cash equivalents, compared to \$943.4 million at March 31, 2017. The decrease in cash and cash equivalents was due primarily to cash used in financing and investing activities.

Net cash used in financing activities was primarily related to repurchases of common stock under our share repurchase program and tax payments related to net share settlements of our restricted stock awards. Net cash used in investing activities was primarily related to net purchases of available for sale securities, purchases of fixed assets, and other asset acquisitions. Net cash provided by operating activities was due primarily to cash generated from sales of virtual currency, NBA 2K18, Grand Theft Auto V, and WWE 2K18, partially offset by investments in software development and licenses, and the funding of internal royalty payments.

Contractual Obligations and Commitments

We have entered into various agreements in the ordinary course of business that require substantial cash commitments over the next several years. Other than agreements entered into in the ordinary course of business and in addition to

the agreements requiring known cash commitments as reported in Part II, Item 7 of our Annual Report on Form 10-K for the fiscal year ended March 31, 2017, we did not have any significant changes to our commitments since March 31, 2017.

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Legal and Other Proceedings: We are, or may become, subject to demands and claims (including intellectual property claims) and are involved in routine litigation in the ordinary course of business which we do not believe to be material to our business or financial statements. We have appropriately accrued amounts related to certain of these claims and legal and other proceedings. While it is reasonably possible that a loss may be incurred in excess of the amounts accrued in our financial statements, we believe that such losses, unless otherwise disclosed, would not be material. On April 11, 2016, we filed a declaratory judgment action in the United States District Court for the Southern District of New York seeking, among other things, a judicial declaration that Leslie Benzies, the former president of one of our subsidiaries with whom we had been in ongoing discussions regarding his separation of employment, is not entitled to any minimum allocation or financial parity with any other person under the applicable royalty plan. We believe we will prevail in this matter, although there can be no assurance of the outcome. On April 12, 2016, Mr. Benzies filed a complaint in the Supreme Court of the State of New York, New York County against us, and certain of our subsidiaries and employees. We removed this case to the United States District Court for the Southern District of New York, but the case was subsequently remanded to state court. The complaint claims damages of at least \$150 million and contains allegations of breach of fiduciary duty; fraudulent inducement and fraudulent concealment; aiding and abetting breach of fiduciary duty; breach of various contracts; breach of implied duty of good faith and fair dealing; tortious interference with contract; unjust enrichment; reformation; constructive trust; declaration of rights; constructive discharge; defamation and fraud. Motion practice in both the federal and state actions is ongoing. We believe that we have meritorious defenses to these claims, and we intend to vigorously defend against them and to pursue any counterclaims.

Off-Balance Sheet Arrangements

As of December 31, 2017 and March 31, 2017, we did not have any material relationships with unconsolidated entities or financial parties, such as entities often referred to as structured finance or variable interest entities, which would have been established for the purpose of facilitating off-balance sheet arrangements or other contractually narrow or limited purposes. As such, we are not exposed to any financing, liquidity, market or credit risk that could arise if we had engaged in such relationships.

International Operations

Net revenue earned outside of the United States is principally generated by our operations in Europe, Asia, Australia, Canada and Latin America. For the three months ended December 31, 2017 and 2016, 45.4% and 46.0%, respectively, and for the nine months ended December 31, 2017 and 2016, 40.7% and 41.8%, respectively, of our net revenue was earned outside of the United States. We are subject to risks inherent in foreign trade, including increased credit risks, tariffs and duties, fluctuations in foreign currency exchange rates, shipping delays and international political, regulatory and economic developments, all of which can have a significant effect on our operating results.

Fluctuations in Quarterly Operating Results and Seasonality

We have experienced fluctuations in quarterly and annual operating results as a result of the timing of the introduction of new titles; variations in sales of titles developed for particular platforms; market acceptance of our titles; development and promotional expenses relating to the introduction of new titles; sequels or enhancements of existing titles; projected and actual changes in platforms; the timing and success of title introductions by our competitors; product returns; changes in pricing policies by us and our competitors; the accuracy of retailers' forecasts of consumer demand; the size and timing of acquisitions; the timing of orders from major customers; and order cancellations and delays in product shipment. Sales of our products are also seasonal, with peak shipments typically occurring in the fourth calendar quarter as a result of increased demand for products during the holiday season. For certain of our software products with multiple element revenue arrangements where we do not have vendor-specific objective evidence ("VSOE") for each element and the deliverables are deemed more-than-inconsequential, we defer the recognition of our net revenues over an estimated service period, which generally ranges from 12 to 50 months. We regularly assess estimated service periods and update them when necessary. As a result, the quarter in which we generate the highest net sales volume may be different from the quarter in which we recognize the highest amount of net revenues. Quarterly comparisons of operating results are not necessarily indicative of future operating results.

Item 3. Quantitative and Qualitative Disclosures About Market Risk

Market risk is the potential loss arising from fluctuations in market rates and prices. Our market risk exposures primarily include fluctuations in interest rates and foreign currency exchange rates.

Interest Rate Risk

Our exposure to fluctuations in interest rates relates primarily to our short-term investment portfolio and variable rate debt under the Credit Agreement.

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We seek to manage our interest rate risk by maintaining a short-term investment portfolio that includes corporate bonds with high credit quality and maturities less than two years. Since short-term investments mature relatively quickly and can be reinvested at the then-current market rates, interest income on a portfolio consisting of short-term securities is more subject to market fluctuations than a portfolio of longer-term maturities. However, the fair value of a short-term portfolio is less sensitive to market fluctuations than a portfolio of longer-term securities. We do not currently use derivative financial instruments in our short-term investment portfolio. Our investments are held for purposes other than trading.

As of December 31, 2017, we had \$547.3 million of short-term investments, which included \$381.0 million of available-for-sale securities. The available-for-sale securities 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 (loss), net of tax, in stockholders' equity. We also had \$774.5 million of cash and cash equivalents that are comprised primarily of money market funds and bank-time deposits. We determined that, based on the composition of our investment portfolio, there was no material interest rate risk exposure to our Condensed Consolidated Financial Statements or liquidity as of December 31, 2017.

Historically, fluctuations in interest rates have not had a significant effect on our operating results. Under our Credit Agreement, outstanding balances bear interest at our election of (a) 0.25% to 0.75% above a certain base rate (4.50% at December 31, 2017), or (b) 1.25% to 1.75% above the LIBOR rate (approximately 1.57% at December 31, 2017), with the margin rate subject to the achievement of certain average liquidity levels. Changes in market rates may affect our future interest expense if there is an outstanding balance on our line of credit. At December 31, 2017, there were no outstanding borrowings under our Credit Agreement. The 1.00% Convertible Notes pay interest semi-annually at a fixed rate of 1.00% per annum, and we expect that there will be no fluctuation related to the 1.00% Convertible Notes affecting our cash component of interest expense. For additional details on our Convertible Notes, see Note 9 to our Condensed Consolidated Financial Statements.

Foreign Currency Exchange Rate Risk

We transact business in foreign currencies and are exposed to risks resulting from fluctuations in foreign currency exchange rates. Accounts relating to foreign operations are translated into United States dollars using prevailing exchange rates at the relevant period end. Translation adjustments are included as a separate component of stockholders' equity. For the three months ended December 31, 2017 and 2016, our foreign currency translation adjustment was a loss of \$0.4 million and a loss of \$5.0 million, respectively, and for the nine months ended December 31, 2017 and 2016, we recognized a foreign currency translation adjustment gain of \$23.4 million and a loss of \$10.1 million, respectively. For the three months ended December 31, 2017 and 2016, we recognized a foreign currency exchange transaction loss of \$0.2 million and a gain of \$1.1 million respectively, and for the nine months ended December 31, 2017 and 2016, we recognized a foreign currency exchange transaction loss of \$1.8 million and a gain of \$3.6 million, respectively, included in interest and other, net in our Condensed Consolidated Statements of Operations.

Balance Sheet Hedging Activities

We use foreign currency forward contracts to mitigate foreign currency exchange rate risk associated with non-functional currency denominated cash balances and inter-company funding loans, non-functional currency denominated accounts receivable and non-functional currency denominated accounts payable. These transactions are not designated as hedging instruments and are accounted for as derivatives whereby the fair value of the contracts is reported as either assets or liabilities on our Condensed Consolidated Balance Sheets, and gains and losses resulting from changes in the fair value are reported in interest and other, net, in our Condensed Consolidated Statements of Operations. We do not enter into derivative financial contracts for speculative or trading purposes. At December 31, 2017, we had \$130.8 million of forward contracts outstanding to sell foreign currencies in exchange for U.S. dollars and \$3.9 million of forward contracts outstanding to buy foreign currencies in exchange for U.S. dollars, all of which have maturities of less than one year. At March 31, 2017, we had \$177.5 million of forward contracts outstanding to sell foreign currencies in exchange for U.S. dollars and \$9.2 million of forward contracts outstanding to buy foreign currencies in exchange for U.S. dollars, all of which have maturities of less than one year. For the three months ended

December 31, 2017 and 2016, we recorded a loss of \$0.6 million and a gain of \$11.2 million, respectively, and for the nine months ended December 31, 2017 and 2016, we recorded a loss of \$15.3 million and a gain of \$11.7 million, respectively. As of December 31, 2017, the fair value of these outstanding forward contracts was a gain of \$0.1 million and was included in Prepaid expenses and other, and, as of March 31, 2017, the fair value of outstanding forward contracts was a loss of \$0.4 million and was included in Accrued and other current liabilities. The fair value of these outstanding forward contracts is estimated based on the prevailing exchange rates of the various hedged currencies as of the end of the period.

Our hedging programs are designed to reduce, but do not entirely eliminate, the effect of currency exchange rate movements. We believe the counterparties to these foreign currency forward contracts are creditworthy multinational commercial banks and that the risk of counterparty nonperformance is not material. 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. For the three months ended December 31, 2017, 45.4% of our revenue was generated outside the United States. Using sensitivity analysis, a hypothetical 10% increase in the value of the U.S. dollar against all currencies

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would decrease revenues by 4.5%, while a hypothetical 10% decrease in the value of the U.S. dollar against all currencies would increase revenues by 4.5%. In the opinion of management, a substantial portion of this fluctuation would be offset by cost of goods sold and operating expenses incurred in local currency.

Item 4. Controls and Procedures

Evaluation of Disclosure Controls and Procedures

Based on an evaluation under the supervision and with the participation of management, our principal executive officer and principal financial officer have concluded that 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 ("Exchange Act") were effective as of the end of the period covered by this report to ensure that information required to be disclosed by us in reports that we file or submit under the Exchange Act is (i) recorded, processed, summarized and reported within the time periods specified in the Securities and Exchange Commission rules and forms and (ii) accumulated and communicated to our management, including our principal executive officer and principal financial officer, as appropriate to allow timely decisions regarding required disclosure.

Changes in Internal Control Over Financial Reporting

There were no changes in our internal control over financial reporting during the quarter ended December 31, 2017, which were identified in connection with management's evaluation required by paragraph (d) of Rules 13a-15 and 15d-15 under the Exchange Act, that have materially affected, or are reasonably likely to materially affect, our internal control over financial reporting.

PART II. OTHER INFORMATION

Item 1. Legal Proceedings

We are, or may become, subject to demands and claims (including intellectual property claims) and are involved in routine litigation in the ordinary course of business, which we do not believe to be material to our business or financial statements. We have appropriately accrued amounts related to certain of these claims and legal and other proceedings. While it is reasonably possible that a loss may be incurred in excess of the amounts accrued in our financial statements, we believe that such losses, unless otherwise disclosed, would not be material.

On April 11, 2016, we filed a declaratory judgment action in the United States District Court for the Southern District of New York seeking, among other things, a judicial declaration that Leslie Benzies, the former president of one of our subsidiaries with whom we had been in ongoing discussions regarding his separation of employment, is not entitled to any minimum allocation or financial parity with any other person under the applicable royalty plan. We believe we will prevail in this matter, although there can be no assurance of the outcome. On April 12, 2016, Mr. Benzies filed a complaint in the Supreme Court of the State of New York, New York County against us, and certain of our subsidiaries and employees. We removed this case to the United States District Court for the Southern District of New York, but the case was subsequently remanded to state court. The complaint claims damages of at least \$150 million and contains allegations of breach of fiduciary duty; fraudulent inducement and fraudulent concealment; aiding and abetting breach of fiduciary duty; breach of various contracts; breach of implied duty of good faith and fair dealing; tortious interference with contract; unjust enrichment; reformation; constructive trust; declaration of rights; constructive discharge; defamation and fraud. Motion practice in both the federal and state actions is ongoing. We believe that we have meritorious defenses to these claims, and we intend to vigorously defend against them and to pursue any counterclaims.

Item 1A. Risk Factors

There have been no material changes to the Risk Factors disclosed in Item 1A of our Annual Report on Form 10-K for the fiscal year ended March 31, 2017. In addition to recommending that those risk factors be considered when reading this current report, we are providing the following updated risk factor.

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

On December 22, 2017, the U.S. enacted comprehensive tax legislation commonly referred to as the Tax Cuts and Jobs Act (herein referred to as the "Act"). The Act makes broad and complex changes to the U.S. tax code that could materially affect us. The Act reduces the U.S. federal corporate income tax rate from 35% to 21%, effective January 1, 2018 and requires companies to pay a one-time transition tax on the previously untaxed earnings of certain foreign subsidiaries. In addition, the Act makes other changes that may affect us, beginning April 1, 2018. These changes include but are not limited to (1) a Base Erosion Anti-abuse Tax (BEAT), which is a new minimum tax, (2) generally eliminating U.S. federal income taxes on dividends from foreign subsidiaries, (3) a new provision that taxes global intangible low-taxed income (GILTI), (4) the repeal of the domestic production activity deduction, and (5) other base broadening provisions.

We are currently evaluating the potential impact of the Act on our tax provision. It is possible that that these changes could have an adverse impact on our effective tax rate, tax payments, financial condition, or results of operations. The new tax law is complex and additional interpretative guidance may be issued that could affect interpretations and assumptions we have made, as well as actions we may take as a result of the Act.

In addition, numerous countries are evaluating their existing tax laws due in part to recommendations made by the Organization for Economic Co-operation and Development's ("OECD's") Base Erosion and Profit Shifting ("BEPS") project. Although we cannot predict whether, or in what form, any legislation based on such proposals may be adopted by the countries in which we do business, future tax reform based on such proposals may increase the amount of taxes we pay and adversely affect our operating results and cash flows.

We are a multinational corporation with operations in the U.S. and various other jurisdictions around the world. Accordingly, we are subject to tax in the U.S. and in various other jurisdictions. Significant judgment is required in determining our worldwide provision for income taxes, and, in the ordinary course of business, there are many transactions and calculations where the ultimate tax determination is uncertain. We are required to estimate future

taxes. Although we currently believe our tax estimates are reasonable, the estimation process is inherently uncertain, and such estimates are not binding on tax authorities. Further, our effective tax rate could be adversely affected by a variety of factors, including changes in the business, including the mix of earnings in countries with differing statutory tax rates, changes in tax elections, and changes in applicable tax laws. Additionally, tax determinations are regularly subject to audit by tax authorities, and developments in those audits could adversely affect our

income tax provision. Should the ultimate tax liability exceed estimates, our income tax provision and net income or loss could be adversely affected.

Historically, 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 earn a significant amount of our operating income and hold a significant portion of our cash outside the U.S. We are reviewing whether the Act will affect our existing intention to indefinitely reinvest earnings of our foreign subsidiaries and therefore hold the cash outside of the U.S. The Act imposes a one-time transition tax on the previously untaxed earnings of certain foreign subsidiaries and other significant changes that affect how U.S. companies are taxed on foreign earnings. These changes may result in higher effective tax rates for us.

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 U.S. 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 net income or loss and financial condition.

Item 2. Unregistered Sales of Equity Securities and Use of Proceeds

Issuer Purchases of Equity Securities

Share Repurchase Program—In January 2013, our Board of Directors authorized the repurchase of up to 7,500,000 shares of our common stock. On May 13, 2015, our Board of Directors approved an increase of 6,717,683 shares to our share repurchase program, increasing the total number of shares that we are permitted to repurchase to 14,217,683 shares of our common stock. The authorizations permit us to purchase shares from time to time through a variety of methods, including in the open market or through privately negotiated transactions, in accordance with applicable securities laws. Repurchases are subject to the availability of stock, prevailing market conditions, the trading price of the stock, our financial performance and other conditions. The program may be suspended or discontinued at any time for any reason. During the three months ended December 31, 2017, we repurchased 1,063,750 shares of our common stock in the open market for \$110.1 million, including immaterial commissions, as part of the program. As of December 31, 2017, we have repurchased a total of 6,235,080 shares of our common stock under this program and 7,982,603 shares of common stock remain available for repurchase under the Company's share repurchase program. The table below details the share repurchases that were made by us during the three months ended December 31, 2017:

| Period | Shares purchased | Average price per share | Total number of shares purchased as part of publicly announced plans or programs | Maximum number of shares that may yet be purchased under the repurchase program |
|---------------------|------------------|-------------------------|--|---|
| October 1-31, 2017 | — | \$— | — | 9,046,353 |
| November 1-30, 2017 | — | \$— | — | 9,046,353 |
| December 1-31, 2017 | 1,063,750 | \$103.54 | 1,063,750 | 7,982,603 |

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Item 6. Exhibits

Exhibits:

- 10.1 Management Agreement, dated as of November 17, 2017, by and between Take-Two Interactive Software, Inc. and ZelnickMedia Corporation (incorporated by reference to Exhibit 10.1 of the Company's Current Report on Form 8-K filed with the Securities and Exchange Commission on November 22, 2017)
- 10.2 Amendment to the Xbox 360 Publisher License Agreement, signed on December 12, 2017, by and between Take-Two Interactive Software, Inc. and Microsoft Corporation
- 10.3 Seventh Amendment, dated as of December 22, 2017, to Second Amended and Restated Credit Agreement, dated as of October 17, 2011, by and among Take-Two Interactive Software, Inc. each of its Subsidiaries identified on the signature pages thereto as Borrowers, each of its Subsidiaries identified on the signature pages thereto as Guarantors, the lender parties thereto, and Wells Fargo Capital Finance, Inc., as administrative agent
- 10.4 Amendment, dated as of December 15, 2017, to Amended and Restated Restricted Unit Agreement, dated as of May 20, 2016, by and between Take-Two Interactive Software, Inc. and ZelnickMedia Corporation
- 31.1 Chief Executive Officer Certification Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002
- 31.2 Chief Financial Officer Certification Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002
- 32.1 Chief Executive Officer Certification pursuant to 18 U.S.C. Section 1350, as adopted Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002
- 32.2 Chief Financial Officer Certification pursuant to 18 U.S.C. Section 1350, as adopted 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 Calculation Linkbase Document
- 101.LAB XBRL Taxonomy Label Linkbase Document
- 101.PRE XBRL Taxonomy Presentation Linkbase Document
- 101.DEF XBRL Taxonomy Extension Definition Document

Attached as Exhibit 101 to this report are the following formatted in XBRL (Extensible Business Reporting Language): (i) Condensed Consolidated Balance Sheets at December 31, 2017 and March 31, 2017, (ii) Condensed Consolidated Statements of Operations for the three and nine months ended December 31, 2017 and 2016, (iii) Condensed Consolidated Statements of Comprehensive Income (Loss) for the three and nine months ended December 31, 2017 and 2016, (iv) Condensed Consolidated Statements of Cash Flows for the nine months ended December 31, 2017 and 2016; and (v) Notes to Condensed Consolidated Financial Statements (Unaudited).

SIGNATURES

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.

TAKE-TWO INTERACTIVE
SOFTWARE, INC.
(Registrant)

Date: February 7, 2018 By: /s/ STRAUSS ZELNICK

Strauss Zelnick
Chairman and Chief Executive Officer
(Principal Executive Officer)

Date: February 7, 2018 By: /s/ LAINIE GOLDSTEIN

Lainie Goldstein
Chief Financial Officer
(Principal Financial Officer)