ELECTRONIC ARTS INC.
Form 10-Q
November 04, 2014
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UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
WASHINGTON, D.C. 20549
FORM 10-Q

þ QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934
For the Quarterly Period Ended September 30, 2014
OR

¨ TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934
For the Transition Period from to
Commission File No. 000-17948
ELECTRONIC ARTS INC.
(Exact name of registrant as specified in its charter)

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

(650) 628-1500
(Registrant's telephone number, including area code)

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

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

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

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

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act). YES ¨ NO þ

As of October 31, 2014, there were 310,936,350 shares of the Registrant's Common Stock, par value $0.01 per share, outstanding.

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PART I – FINANCIAL INFORMATION

Item 1. Condensed Consolidated Financial Statements (Unaudited)
ELECTRONIC ARTS INC. AND SUBSIDIARIES
CONDENSED CONSOLIDATED BALANCE SHEETS

(Unaudited) (In millions, except par value data)	September 30, 2014	March 31, 2014 [(a)]
ASSETS		
Current assets:		
Cash and cash equivalents	$1,624	$1,782
Short-term investments	764	583
Receivables, net of allowances of $141 and $186, respectively	829	327
Inventories	67	56
Deferred income taxes, net	58	74
Other current assets	190	316
Total current assets	3,532	3,138
Property and equipment, net	483	510
Goodwill	1,723	1,723
Acquisition-related intangibles, net	143	177
Deferred income taxes, net	9	28
Other assets	141	140
TOTAL ASSETS	$6,031	$5,716
LIABILITIES AND STOCKHOLDERS' EQUITY		
Current liabilities:		
Accounts payable	$191	$119
Accrued and other current liabilities	915	781
Deferred net revenue (online-enabled games)	1,281	1,490
Total current liabilities	2,387	2,390
0.75% convertible senior notes due 2016, net	591	580
Income tax obligations	89	189
Deferred income taxes, net	85	18
Other liabilities	209	117
Total liabilities	3,361	3,294
Commitments and contingencies (See Note 13)		
Stockholders' equity:		
Preferred stock, $0.01 par value. 10 shares authorized	—	—
Common stock, $0.01 par value. 1,000 shares authorized; 312 and 311 shares issued and outstanding, respectively	3	3
Paid-in capital	2,247	2,353
Retained earnings	367	29
Accumulated other comprehensive income	53	37
Total stockholders' equity	2,670	2,422
TOTAL LIABILITIES AND STOCKHOLDERS' EQUITY	$6,031	$5,716

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

(a) Derived from audited consolidated financial statements.

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ELECTRONIC ARTS INC. AND SUBSIDIARIES
CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS

(Unaudited)	Three Months Ended September 30,		Six Months Ended September 30,	
(In millions, except per share data)	2014	2013	2014	2013
Net revenue:				
Product	$536	$350	1,293	893
Service and other	454	345	911	751
Total net revenue	990	695	$2,204	$1,644
Cost of revenue:				
Product	347	341	599	471
Service and other	80	72	195	136
Total cost of revenue	427	413	794	607
Gross profit	563	282	1,410	1,037
Operating expenses:				
Research and development	261	283	526	561
Marketing and sales	183	164	313	311
General and administrative	92	129	180	214
Acquisition-related contingent consideration	(1)	(44)	(2)	(37)
Amortization of intangibles	4	4	7	8
Restructuring and other charges	—	(2)	—	(1)
Total operating expenses	539	534	1,024	1,056
Operating income (loss)	24	(252)	386	(19)
Interest and other income (expense), net	(6)	(8)	(14)	(13)
Income (loss) before provision for income taxes	18	(260)	372	(32)
Provision for income taxes	15	13	34	19
Net income (loss)	$3	$(273)	$338	$(51)
Net income (loss) per share:				
Basic	$0.01	$(0.89)	$1.08	$(0.17)
Diluted	$0.01	$(0.89)	$1.05	$(0.17)
Number of shares used in computation:				
Basic	313	308	312	306
Diluted	322	308	322	306

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

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ELECTRONIC ARTS INC. AND SUBSIDIARIES
CONDENSED CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME

(Unaudited)	Three Months Ended September 30,		Six Months Ended September 30,	
(In millions)	2014	2013	2014	2013
Net income (loss)	$3	$(273)	$338	$(51)
Other comprehensive income (loss), net of tax:				
Change in unrealized net gains and losses on available-for-sale securities	—	1	—	—
Change in unrealized net gains and losses on derivative instruments	11	(9)	10	(11)
Reclassification adjustment for net realized losses on derivative instruments	2	—	7	2
Foreign currency translation adjustments	(21)	14	(1)	2
Total other comprehensive income (loss), net of tax	(8)	6	16	(7)
Total comprehensive income (loss)	$(5)	$(267)	$354	$(58)

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

ELECTRONIC ARTS INC. AND SUBSIDIARIES
CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS

(Unaudited)	Six Months Ended September 30,	
(In millions)	2014	2013
OPERATING ACTIVITIES		
Net income (loss)	$338	$(51)
Adjustments to reconcile net income (loss) to net cash provided by (used in) operating activities:		
Depreciation, amortization and accretion	112	112
Stock-based compensation	69	71
Acquisition-related contingent consideration	(2)	(37)
Change in assets and liabilities:		
Receivables, net	(508)	(278)
Inventories	(11)	(15)
Other assets	138	8
Accounts payable	83	77
Accrued and other liabilities	173	(37)
Deferred income taxes, net	4	5
Deferred net revenue (online-enabled games)	(209)	(109)
Net cash provided by (used in) operating activities	187	(254)
INVESTING ACTIVITIES		
Capital expenditures	(48)	(53)
Proceeds from maturities and sales of short-term investments	352	250
Purchase of short-term investments	(537)	(191)
Acquisition of subsidiaries, net of cash acquired	—	(5)
Net cash provided by (used in) investing activities	(233)	1
FINANCING ACTIVITIES		
Proceeds from issuance of common stock	26	50
Excess tax benefit from stock-based compensation	14	—
Repurchase and retirement of common stock	(145)	—
Acquisition-related contingent consideration payment	—	(1)
Net cash provided by (used in) financing activities	(105)	49
Effect of foreign exchange on cash and cash equivalents	(7)	2
Decrease in cash and cash equivalents	(158)	(202)
Beginning cash and cash equivalents	1,782	1,292
Ending cash and cash equivalents	$1,624	$1,090
Supplemental cash flow information:		
Cash paid (refunded) during the period for income taxes, net	$(11)	$15
Cash paid during the period for interest	$3	$3

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

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ELECTRONIC ARTS INC. AND SUBSIDIARIES
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS
(Unaudited)

(1) DESCRIPTION OF BUSINESS AND BASIS OF PRESENTATION

We develop, market, publish and distribute game software content and services that can be played by consumers on a variety of platforms, including video game consoles (such as PlayStation 3 and 4 from Sony and Xbox 360 and Xbox One from Microsoft), personal computers ("PCs"), mobile phones and tablets. Our ability to deliver games and services across multiple platforms, through multiple distribution channels, and directly to consumers (online and wirelessly) has been, and will continue to be, a cornerstone of our product strategy. We have adopted new business models and alternative revenue streams (such as subscription, micro-transactions, and advertising) in connection with our online and wireless product and service offerings. Some of our games are based on our wholly-owned intellectual property (e.g., Battlefield, Mass Effect, Need for Speed, Dragon Age, The Sims, Bejeweled, and Plants vs. Zombies), and some of our games leverage content that we license from others (e.g., FIFA, Madden NFL and Star Wars). We also publish and distribute games developed by third parties (e.g., Titanfall). Our goal is to turn our intellectual properties into year-round businesses available on a range of platforms. Our products and services may be purchased through physical and online retailers, platform providers such as console manufacturers and mobile carriers via digital downloads, as well as directly through our own distribution platform, including online portals such as Origin.

Our fiscal year is reported on a 52- or 53-week period that ends on the Saturday nearest March 31. Our results of operations for the fiscal years ending or ended, as the case may be, March 31, 2015 and 2014 contain 52 weeks each, and ends or ended, as the case may be, on March 28, 2015 and March 29, 2014, respectively. Our results of operations for the three and six months ended September 30, 2014 and 2013 contained 13 and 26 weeks each and ended on September 27, 2014 and September 28, 2013, respectively. For simplicity of disclosure, all fiscal periods are referred to as ending on a calendar month end.

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

These Condensed Consolidated Financial Statements should be read in conjunction with the Consolidated Financial Statements and Notes thereto included in our Annual Report on Form 10-K for the fiscal year ended March 31, 2014, as filed with the United States Securities and Exchange Commission ("SEC") on May 21, 2014.

Change in Estimated Offering Period

Prior to July 1, 2013, for most sales, we estimated the offering period to be six months and recognized revenue over this period in the month after delivery. During the three months ended September 30, 2013, we completed our fiscal 2014 annual evaluation of the estimated offering period and noted that generally, consumers were playing our games online over a longer period of time. Based on this, we concluded that for physical software sales made after June 30, 2013, the estimated offering period should be increased to nine months, resulting in revenue being recognized over a longer period of time. This change in estimate resulted in an estimated decrease to net revenue and net income of $474 million and a decrease of $1.50 of diluted earnings per share for fiscal year 2014. During the three months ended September 30, 2014, this change in estimate resulted in an estimated increase to net revenue and net income of $181 million and an increase of $0.56 of diluted earnings per share. During the six months ended September 30, 2014, this change in estimate resulted in an estimated increase to net revenue and net income of $286 million and an increase of $0.89 of diluted earnings per share. The estimated offering period for digitally distributed software games did not change and is six months. We completed our fiscal 2015 annual evaluation during the second quarter and determined that the estimated offering period for physical software sales and digital sales continues to be nine months and six months, respectively.

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Recently Adopted Accounting Standards

On April 1, 2014, we adopted ASU 2013-11, Presentation of an Unrecognized Tax Benefit When a Net Operating Loss Carryforward, a Similar Tax Loss, or a Tax Credit Carryforward Exists. Under the new accounting standard, an unrecognized tax benefit is required to be presented as a reduction to a deferred tax asset if the disallowance of the uncertain tax position would reduce an available tax loss or tax credit carryforward instead of resulting in a cash tax liability. The ASU applies prospectively to all unrecognized tax benefits that exist as of the adoption date. As a result of the adoption, we reduced: (a) noncurrent income tax obligations by $96 million; (b) current deferred income tax assets by $18 million; and (c) noncurrent deferred income tax assets by $11 million. We increased noncurrent deferred income tax liabilities by $67 million. As the new accounting standard only impacted presentation, it did not have an impact on the Company’s net financial position, results of operations, or cash flows.

Impact of Recently Issued Accounting Standards

In May 2014, the FASB issued ASU No. 2014-09, Revenue from Contracts with Customers, which requires an entity to recognize the amount of revenue to which it expects to be entitled for the transfer of promised goods or services to customers. The ASU will replace most existing revenue recognition guidance in U.S. GAAP when it becomes effective. The new standard is effective for annual reporting periods beginning after December 15, 2016. Early application is not permitted. The standard permits the use of either the retrospective or cumulative effect transition method. The Company is evaluating the effect that ASU 2014-09 will have on its Condensed Consolidated Financial Statements and related disclosures. The Company has not yet selected a transition method nor has it determined the effect of the standard on its ongoing financial reporting. We expect to adopt this new standard in the first quarter of fiscal year 2018.

(2) FAIR VALUE MEASUREMENTS

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

Fair Value Hierarchy

The three levels of inputs that may be used to measure fair value are as follows:

- Level 1. Quoted prices in active markets for identical assets or liabilities.
- Level 2. Observable inputs other than quoted prices included within Level 1, such as quoted prices for similar assets or liabilities, quoted prices in markets with insufficient volume or infrequent transactions (less active markets), or model-derived valuations in which all significant inputs are observable or can be derived principally from or corroborated with observable market data for substantially the full term of the assets or liabilities.
- Level 3. Unobservable inputs to the valuation methodology that are significant to the measurement of the fair value of assets or liabilities.

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Assets and Liabilities Measured at Fair Value on a Recurring Basis

As of September 30, 2014 and March 31, 2014, our assets and liabilities that were measured and recorded at fair value on a recurring basis were as follows (in millions):

		Fair Value Measurements at Reporting Date Using			
		Quoted Prices in Active Markets for Identical Financial Instruments	Significant Other Observable Inputs	Significant Unobservable Inputs	
	As of September 30, 2014	(Level 1)	(Level 2)	(Level 3)	Balance Sheet Classification
Assets					
Money market funds	$6	$6	$—	$—	Cash equivalents
Available-for-sale securities:					
Corporate bonds	389	—	389	—	Short-term investments
U.S. Treasury securities	165	165	—	—	Short-term investments
U.S. agency securities	146	—	146	—	Short-term investments and cash equivalents
Commercial paper	99	—	99	—	Short-term investments and cash equivalents
Foreign currency derivatives	12	—	12	—	Other current assets
Deferred compensation plan assets [(a)]	10	10	—	—	Other assets
Total assets at fair value	$827	$181	$646	$—	
Liabilities					
Foreign currency derivatives	$6	$—	$6	$—	Accrued and other current liabilities
Deferred compensation plan liabilities	10	10	—	—	Other liabilities
Total liabilities at fair value	$16	$10	$6	$—	

	Fair Value Measurements Using Significant Unobservable Inputs (Level 3)
	Contingent Consideration
Balance as of March 31, 2014	$4
Change in fair value [(c)]	(2)
Payments [(d)]	(2)
Balance as of September 30, 2014 [(b)]	$—

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		Fair Value Measurements at Reporting Date Using			
	As of March 31, 2014	Quoted Prices in Active Markets for Identical Financial Instruments (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)	Balance Sheet Classification
Assets					
Money market funds	$588	$588	$—	$—	Cash equivalents
Available-for-sale securities:					
Corporate bonds	279	—	279	—	Short-term investments
Commercial paper	146	—	146	—	Short-term investments and cash equivalents
U.S. Treasury securities	118	118	—	—	Short-term investments and cash equivalents
U.S. agency securities	89	—	89	—	Short-term investments and cash equivalents
Deferred compensation plan assets [(a)]	9	9	—	—	Other assets
Total assets at fair value	$1,229	$715	$514	$—	
Liabilities					
Contingent consideration [(b)]	$4	$—	$—	$4	Accrued and other current liabilities and other liabilities
Foreign currency derivatives	6	—	6	—	Accrued and other current liabilities
Deferred compensation plan liabilities	9	9	—	—	Other liabilities
Total liabilities at fair value	$19	$9	$6	$4	

	Fair Value Measurements Using Significant Unobservable Inputs (Level 3)
	Contingent Consideration
Balance as of March 31, 2013	$43
Change in fair value [(c)]	(35)
Payment [(d)]	(4)
Balance as of March 31, 2014 [(b)]	$4

(a) The Deferred Compensation Plan assets consist of various mutual funds. See Note 15 in our Annual Report on Form 10-K for the fiscal year ended March 31, 2014, for additional information regarding our Deferred Compensation Plan.

(b) The immaterial contingent consideration as of September 30, 2014 represents the estimated fair value of the additional variable cash consideration payable in connection with our acquisition of KlickNation Corporation (“KlickNation”) that is contingent upon the achievement of certain performance milestones. The $4 million contingent consideration as of March 31, 2014 represents the estimated fair value of the additional variable cash consideration payable in connection with our acquisitions of KlickNation and Chillingo Limited (“Chillingo”) that are contingent upon the achievement of certain performance milestones. We estimated the fair value of the acquisition-related contingent consideration payable using probability-weighted discounted cash flow models, and applied a discount rate that appropriately captures the risk associated with the obligation. The weighted average of the discount rates used during the six months ended September 30, 2014 was 17 percent. The weighted average of the discount rates used during the fiscal year 2014 was 18 percent. The significant unobservable input used in the fair value measurement of the contingent consideration payable are forecasted earnings. Significant changes in forecasted earnings would result in a significantly higher or lower fair value measurement. At September 30, 2014 and March 31, 2014, the fair market value of acquisition-related contingent consideration was immaterial and $4 million, respectively, compared to a maximum potential payout of $3 million and $10 million, respectively.

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

(d) During the six months ended September 30, 2014, we made payments totaling $2 million to settle certain performance milestones achieved in connection with one of our acquisitions. During fiscal year 2014, we made payments of $4 million to settle certain performance milestones achieved in connection with two of our acquisitions.

(3) FINANCIAL INSTRUMENTS

Cash and Cash Equivalents

As of September 30, 2014 and March 31, 2014, our cash and cash equivalents were $1,624 million and $1,782 million, respectively. Cash equivalents were valued at their carrying amounts as they approximate fair value due to the short maturities of these financial instruments.

Short-Term Investments

Short-term investments consisted of the following as of September 30, 2014 and March 31, 2014 (in millions):

	As of September 30, 2014				As of March 31, 2014			
	Cost or Amortized Cost	Gross Unrealized		Fair Value	Cost or Amortized Cost	Gross Unrealized		Fair Value
		Gains	Losses			Gains	Losses	
Corporate bonds	$389	$—	$—	$389	$279	$—	$—	$279
U.S. Treasury securities	165	—	—	165	114	—	—	114
U.S. agency securities	141	—	—	141	80	—	—	80
Commercial paper	69	—	—	69	110	—	—	110
Short-term investments	$764	$—	$—	$764	$583	$—	$—	$583

We evaluate our investments for impairment quarterly. Factors considered in the review of investments with an unrealized loss include the credit quality of the issuer, the duration that the fair value has been less than the adjusted cost basis, the severity of the impairment, the reason for the decline in value and potential recovery period, the financial condition and near-term prospects of the investees, our intent to sell and ability to hold the investment for a period of time sufficient to allow for any anticipated recovery in market value, and any contractual terms impacting the prepayment or settlement process. Based on our review, we did not consider these investments to be other-than-temporarily impaired as of September 30, 2014 and March 31, 2014.

The following table summarizes the amortized cost and fair value of our short-term investments, classified by stated maturity as of September 30, 2014 and March 31, 2014 (in millions):

	As of September 30, 2014		As of March 31, 2014	
	Amortized Cost	Fair Value	Amortized Cost	Fair Value
Short-term investments				
Due in 1 year or less	$345	$345	$318	$318
Due in 1-2 years	203	203	156	156
Due in 2-3 years	209	209	104	104
Due in 3-4 years	7	7	5	5
Short-term investments	$764	$764	$583	$583

0.75% Convertible Senior Notes Due 2016

The following table summarizes the carrying value and fair value of our 0.75% Convertible Senior Notes due 2016 as of September 30, 2014 and March 31, 2014 (in millions):

	As of September 30, 2014		As of March 31, 2014	
	Carrying Value	Fair Value	Carrying Value	Fair Value

0.75% Convertible Senior Notes due 2016	$591	$787	$580	$731

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The carrying value of the 0.75% Convertible Senior Notes due 2016 excludes the fair value of the equity conversion feature, which was classified as equity upon issuance, while the fair value is based on quoted market prices for the 0.75% Convertible Senior Notes due 2016, which includes the equity conversion feature. The fair value of the 0.75% Convertible Senior Notes due 2016 is classified as Level 2 within the fair value hierarchy. See Note 12 for additional information related to our 0.75% Convertible Senior Notes due 2016.

(4) DERIVATIVE FINANCIAL INSTRUMENTS

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

We transact business in various foreign currencies and have significant international sales and expenses denominated in foreign currencies, subjecting us to foreign currency risk. We purchase foreign currency forward contracts, generally with maturities of 15 months or less, to reduce the volatility of cash flows primarily related to forecasted revenue and expenses denominated in certain foreign currencies. Our cash flow risks are primarily related to fluctuations in the Euro, British pound sterling, Canadian dollar, and Swedish Krona. In addition, we utilize foreign currency forward contracts to mitigate foreign exchange rate risk associated with foreign-currency-denominated monetary assets and liabilities, primarily intercompany receivables and payables. The foreign currency forward contracts not designated as hedging instruments generally have a contractual term of approximately 3 months or less and are transacted near month-end. We do not use foreign currency forward contracts for speculative or trading purposes.

Cash Flow Hedging Activities

Certain of our forward contracts are designated and qualify as cash flow hedges. The effectiveness of the cash flow hedge contracts, including time value, is assessed monthly using regression analysis, as well as other timing and probability criteria. To qualify for hedge accounting treatment, all hedging relationships are formally documented at the inception of the hedges and must be highly effective in offsetting changes to future cash flows on hedged transactions. The derivative assets or liabilities associated with our hedging activities are recorded at fair value in other current assets or accrued and other liabilities on our Condensed Consolidated Balance Sheets. The effective portion of gains or losses resulting from changes in the fair value of these hedges is initially reported, net of tax, as a component of accumulated other comprehensive income in stockholders' equity. The gross amount of the effective portion of gains or losses resulting from changes in the fair value of these hedges is subsequently reclassified into net revenue or research and development expenses, as appropriate, in the period when the forecasted transaction is recognized in our Condensed Consolidated Statements of Operations. In the event that the gains or losses in accumulated other comprehensive income are deemed to be ineffective, the ineffective portion of gains or losses resulting from changes in fair value, if any, is reclassified to interest and other income (expense), net, in our Condensed Consolidated Statements of Operations. In the event that the underlying forecasted transactions do not occur, or it becomes remote that they will occur, within the defined hedge period, the gains or losses on the related cash flow hedges are reclassified from accumulated other comprehensive income to interest and other income (expense), net, in our Condensed Consolidated Statements of Operations.

Total gross notional amounts and fair values for currency derivatives with cash flow hedge accounting designation are as follows:

	As of September 30, 2014			As of March 31, 2014		
	Notional	Fair Value		Notional	Fair Value	
	Amount	Asset	Liability	Amount	Asset	Liability
Forward contracts to purchase	$121	—	5	$179	—	3
Forward contracts to sell	$246	11	—	$363	—	2

The net impact of the effective portion of gains and losses from our cash flow hedging activities in our Condensed Consolidated Statements of Operations for three months ended September 30, 2014 and 2013 was immaterial.

The net impact of the effective portion of gains and losses from our cash flow hedging activities in our Condensed Consolidated Statements of Operations was a loss of $7 million for the six months ended September 30, 2014 and immaterial for the six months ended September 30, 2013.

During the three and six months ended September 30, 2014, we reclassified an immaterial amount of the ineffective portion of gains or losses resulting from changes in fair value into interest and other income (expense), net.

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Balance Sheet Hedging Activities

Our foreign currency forward contracts that are not designated as hedging instruments are accounted for as derivatives whereby the fair value of the contracts are reported as other current assets or accrued and other current liabilities on our Condensed Consolidated Balance Sheets, and gains and losses resulting from changes in the fair value are reported in interest and other income (expense), net, in our Condensed Consolidated Statements of Operations. The gains and losses on these foreign currency forward contracts generally offset the gains and losses in the underlying foreign-currency-denominated monetary assets and liabilities, which are also reported in interest and other income (expense), net, in our Condensed Consolidated Statements of Operations. The fair value of our foreign currency forward contracts was measured using Level 2 inputs. Total gross notional amounts and fair values for currency derivatives that are not designated as hedging instruments are accounted for as follows:

	As of September 30, 2014			As of March 31, 2014		
	Notional	Fair Value		Notional	Fair Value	
	Amount	Asset	Liability	Amount	Asset	Liability
Forward contracts to purchase	$77	$—	$1	$140	$—	$1
Forward contracts to sell	$444	$1	$—	$232	$—	$—

The effect of foreign currency forward contracts not designated as hedging instruments in our Condensed Consolidated Statements of Operations for the three and six months ended September 30, 2014 and 2013, was as follows (in millions):

	Location of Gain (Loss) Recognized in Income on Derivative	Amount of Gain (Loss) Recognized in Income on Derivative			
		Three Months Ended September 30,		Six Months Ended September 30,	
		2014	2013	2014	2013
Foreign currency forward contracts not designated as hedging instruments	Interest and other income (expense), net	$18	$(5)	$19	$(5)

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(5) ACCUMULATED OTHER COMPREHENSIVE INCOME (LOSS)

The changes in accumulated other comprehensive income (loss) by component, net of tax, for the three months ended September 30, 2014 and 2013 are as follows (in millions):

	Unrealized Gains (Losses) on Available-for-Sale Securities	Unrealized Gains (Losses) on Derivative Instruments	Foreign Currency Translation Adjustments	Total
Balances as of June 30, 2014	$ (4)	$(6)	$71	$61
Other comprehensive income (loss) before reclassifications	—	11	(21)	(10)
Amounts reclassified from accumulated other comprehensive income	—	2	—	2
Net current-period other comprehensive income (loss)	—	13	(21)	(8)
Balance as of September 30, 2014	$ (4)	$7	$50	$53

	Unrealized Gains (Losses) on Available-for-Sale Securities	Unrealized Gains (Losses) on Derivative Instruments	Foreign Currency Translation Adjustments	Total
Balances as of June 30, 2013	$ (5)	$—	$61	$56
Other comprehensive income (loss) before reclassifications	1	(9)	14	6
Amounts reclassified from accumulated other comprehensive income	—	—	—	—
Net current-period other comprehensive income (loss)	1	(9)	14	6
Balance as of September 30, 2013	$ (4)	$(9)	$75	$62

The changes in accumulated other comprehensive income (loss) by component, net of tax, for the six months ended September 30, 2014 and 2013 are as follows (in millions):

	Unrealized Gains (Losses) on Available-for-Sale Securities	Unrealized Gains (Losses) on Derivative Instruments	Foreign Currency Translation Adjustments	Total
Balances as of March 31, 2014	$ (4)	$(10)	$51	$37
Other comprehensive income (loss) before reclassifications	—	10	(1)	9
Amounts reclassified from accumulated other comprehensive income	—	7	—	7
Net current-period other comprehensive income (loss)	—	17	(1)	16
Balances as of September 30, 2014	$ (4)	$7	$50	$53

	Unrealized Gains (Losses) on Available-for-Sale Securities	Unrealized Gains (Losses) on Derivative Instruments	Foreign Currency Translation Adjustments	Total
Balances as of March 31, 2013	$ (4)	$—	$73	$69
	—	(11)	2	(9)

Other comprehensive income (loss) before reclassifications				
Amounts reclassified from accumulated other comprehensive income	—	2	—	2
Net current-period other comprehensive income (loss)	—	(9)	2	(7)
Balances as of September 30, 2013	$ (4)	$(9)	$75	$62

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The effects on net income of amounts reclassified from accumulated other comprehensive income (loss) for the three and six months ended September 30, 2014 were as follows (in millions):

	Amount Reclassified From Accumulated Other Comprehensive Income (loss)	
Statement of Operations Classification	Three Months Ended September 30, 2014	Six Months Ended September 30, 2014
Net revenue	$2	$5
Research and development	—	2
Total amount reclassified, net of tax	$2	$7

The effects on net income of amounts reclassified from accumulated other comprehensive income (loss) for the three and six months ended September 30, 2013 was immaterial and included in net revenue and research and development.

(6) BUSINESS COMBINATIONS

During the six months ended September 30, 2014, there were no acquisitions. During the six months ended September 30, 2013, we completed one acquisition that did not have a significant impact on our Condensed Consolidated Financial Statements.

(7) GOODWILL AND ACQUISITION-RELATED INTANGIBLES, NET

The changes in the carrying amount of goodwill for the six months ended September 30, 2014 are as follows (in millions):

	As of March 31, 2014	Activity	Effects of Foreign Currency Translation	As of September 30, 2014
Goodwill	$2,091	$—	$—	$2,091
Accumulated impairment	(368)	—	—	(368)
Total	$1,723	$—	$—	$1,723

Goodwill represents the excess of the purchase price over the fair value of the underlying acquired net tangible and intangible assets. Goodwill is not amortized, but rather subject to at least an annual assessment for impairment by applying a fair value-based test.

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

	As of September 30, 2014			As of March 31, 2014		
	Gross Carrying Amount	Accumulated Amortization	Acquisition-Related Intangibles, Net	Gross Carrying Amount	Accumulated Amortization	Acquisition-Related Intangibles, Net
Developed and core technology	$531	$ (413)	$ 118	$531	$ (385)	$ 146
Trade names and trademarks	130	(108)	22	130	(105)	25
Registered user base and other intangibles	87	(87)	—	87	(87)	—
Carrier contracts and related	85	(82)	3	85	(79)	6
Total	$833	$ (690)	$ 143	$833	$ (656)	$ 177

Amortization of intangibles for the three and six months ended September 30, 2014 and 2013 are classified in the Condensed Consolidated Statement of Operations as follows (in millions):

	Three Months Ended September 30,		Six Months Ended September 30,	
	2014	2013	2014	2013
Cost of service and other	$9	$6	19	12
Cost of product	3	8	7	17

Operating expenses	4	4	7	8
Total	$16	$18	$33	$37

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Acquisition-related intangible assets are amortized using the straight-line method over the lesser of their estimated useful lives or the agreement terms, typically from 2 to 14 years. As of September 30, 2014 and March 31, 2014, the weighted-average remaining useful life for acquisition-related intangible assets was approximately 3.1 years and 3.4 years, respectively.

As of September 30, 2014, future amortization of acquisition-related intangibles that will be recorded in the Condensed Consolidated Statement of Operations is estimated as follows (in millions):

Fiscal Year Ending March 31,	
2015 (remaining six months)	$32
2016	53
2017	32
2018	12
2019	8
2020	6
Thereafter	—
Total	$143

(8) RESTRUCTURING AND OTHER CHARGES

Restructuring and other restructuring plan-related information as of September 30, 2014 was as follows (in millions):

	Fiscal 2011 Restructuring	Other Restructurings and Reorganization		
	Other	Facilities-related	Other	Total
Balances as of March 31, 2013	$57	$4	$1	$62
Charges to operations	(2)	1	—	(1)
Charges settled in cash	(8)	(3)	—	(11)
Balances as of March 31, 2014	47	2	1	50
Charges to operations	—	—	—	—
Charges settled in cash	(15)	—	—	(15)
Balances as of September 30, 2014	$32	$2	$1	$35

Fiscal 2011 Restructuring

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

Since the inception of the fiscal 2011 restructuring plan through September 30, 2014, we have incurred charges of $172 million, consisting of (1) $129 million related to the amendment of certain licensing agreements and other intangible asset impairment costs, (2) $31 million related to the amendment of certain developer agreements, and (3) $12 million in employee-related expenses. The $32 million restructuring accrual as of September 30, 2014 is expected to be settled by December 2015. We do not expect to incur any additional restructuring charges under this plan.

Other Restructurings and Reorganization

We also engaged in various other restructurings and a reorganization based on management decisions made in fiscal years 2013 and 2009. We do not expect to incur any additional restructuring charges under these plans. The $3 million restructuring accrual as of September 30, 2014 related to our other restructuring plans is expected to be settled by April 2020.

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(9) ROYALTIES AND LICENSES

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

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

Our contracts with some licensors include minimum guaranteed royalty payments, which are initially recorded as an asset and as a liability at the contractual amount when no performance remains with the licensor. When performance remains with the licensor, we record guarantee payments as an asset when actually paid and as a liability when incurred, rather than recording the asset and liability upon execution of the contract. Royalty liabilities are classified as current liabilities to the extent such royalty payments are contractually due within the next 12 months.

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

During the three months ended September 30, 2014, we did not recognize any losses or impairment charges on royalty-based commitments. During the six months ended September 30, 2014, we recognized a loss of $122 million on a previously unrecognized licensed intellectual property commitment. The $122 million loss relates to the termination of certain rights we previously had to use a licensor’s intellectual property. In addition, because the loss will be paid in installments through March 2022, our accrued loss was computed using the effective interest method. We currently estimate recognizing in future periods through March 2022, approximately $33 million for the accretion of interest expense related to this obligation. This interest expense will be included in cost of revenue in our Condensed Consolidated Statement of Operations. During the three months ended September 30, 2013, we recognized losses of $10 million on previously unrecognized royalty-based commitments. During the six months ended September 30, 2013, we recognized total losses of $27 million, inclusive of impairment charges of $17 million on royalty-based assets recognized during the three months ended June 30, 2013.

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

	As of September 30, 2014	As of March 31, 2014
Other current assets	$57	$97
Other assets	37	58
Royalty-related assets	$94	$155

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At any given time, depending on the timing of our payments to our co-publishing and/or distribution affiliates, content licensors, and/or independent software developers, we classify any recognized unpaid royalty amounts due to these parties as accrued liabilities. The current and long-term portions of accrued royalties, included in accrued and other current liabilities and other liabilities, consisted of (in millions):

	As of September 30, 2014	As of March 31, 2014
Accrued royalties	$148	$73
Other accrued expenses	—	7
Other liabilities	149	53
Royalty-related liabilities	$297	$133

In addition, as of September 30, 2014, we were committed to pay approximately $1,066 million to content licensors, independent software developers, and co-publishing and/or distribution affiliates, but performance remained with the counterparty (i.e., delivery of the product or content or other factors) and such commitments were therefore not recorded in our Condensed Consolidated Financial Statements. See Note 13 for further information on our developer and licensor commitments.

(10) BALANCE SHEET DETAILS

Inventories

Inventories as of September 30, 2014 and March 31, 2014 consisted of (in millions):

	As of September 30, 2014	As of March 31, 2014
Finished goods	$64	$55
Raw materials and work in process	3	1
Inventories	$67	$56

Property and Equipment, Net

Property and equipment, net, as of September 30, 2014 and March 31, 2014 consisted of (in millions):

	As of September 30, 2014	As of March 31, 2014
Computer, equipment and software	$733	$718
Buildings	329	327
Leasehold improvements	131	129
Office equipment, furniture and fixtures	66	67
Land	63	63
Warehouse, equipment and other	9	10
Construction in progress	5	5
	1,336	1,319
Less: accumulated depreciation	(853)	(809)
Property and equipment, net	$483	$510

During the three and six months ended September 30, 2014, depreciation expense associated with property and equipment was $33 million and $64 million, respectively. During the three and six months ended September 30, 2013, depreciation expense associated with property and equipment was $32 million and $62 million, respectively.

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Accrued and Other Current Liabilities

Accrued and other current liabilities as of September 30, 2014 and March 31, 2014 consisted of (in millions):

	As of September 30, 2014	As of March 31, 2014
Other accrued expenses	$386	$328
Accrued compensation and benefits	161	259
Accrued royalties	148	73
Deferred net revenue (other)	220	121
Accrued and other current liabilities	$915	$781

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

Deferred Net Revenue (Online-Enabled Games)

Deferred net revenue (online-enabled games) was $1,281 million and $1,490 million as of September 30, 2014 and March 31, 2014, respectively. Deferred net revenue (online-enabled games) generally includes the unrecognized revenue from bundled sales of certain online-enabled games for which we do not have vendor-specific objective evidence of fair value ("VSOE") for the obligation to provide unspecified updates. We recognize revenue from the sale of online-enabled games for which we do not have VSOE for the unspecified updates on a straight-line basis, generally over an estimated nine-month period beginning in the month after shipment for physical games sold through retail and an estimated six-month period for digitally-distributed games. However, we expense the cost of revenue related to these transactions during the period in which the product is delivered (rather than on a deferred basis).

(11) INCOME TAXES

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

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

The provision for income taxes reported for the three and six months ended September 30, 2014 is based on our projected annual effective tax rate for fiscal year 2015, and also includes certain discrete items recorded during the period. Our effective tax rate for the three and six months ended September 30, 2014 was a tax expense of 83.3 percent and 9.1 percent, respectively, as compared to a tax expense of 5.0 percent and 59.4 percent, respectively, for the same period of fiscal year 2014. The effective tax rate for the three and six months ended September 30, 2014 and

2013 differs from the statutory rate of 35.0 percent primarily due to the utilization of U.S. deferred tax assets which were subject to a valuation allowance and non-U.S. profits subject to a reduced or zero tax rate. The effective tax rate for the three and six months ended September 30, 2014 differs from the same period in fiscal year 2014 primarily due to differences in the pre-tax income or loss. In addition, the effective tax rate for the six months ended September 30, 2014 differs from the same period in fiscal year 2014 primarily due to a discrete expense of $14 million recorded in the six months ended September 30, 2014 for excess tax benefits from stock-based compensation deductions allocated directly to contributed capital.

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During the three and six months ended September 30, 2014, we recorded a net decrease of $1 million and $2 million in gross unrecognized tax benefits. The total gross unrecognized tax benefits as of September 30, 2014 is $230 million. A portion of our unrecognized tax benefits will affect our effective tax rate if they are recognized upon favorable resolution of the uncertain tax positions. As of September 30, 2014, if recognized, approximately $73 million of the unrecognized tax benefits would affect our effective tax rate and approximately $157 million would result in adjustments to deferred tax assets with corresponding adjustments to the valuation allowance.

During the three months ended September 30, 2014, we recorded a net decrease of $1 million for accrued interest and penalties related to tax positions taken on our tax returns and an immaterial amount for the six months ended September 30, 2014. As of September 30, 2014, the combined amount of accrued interest and penalties related to uncertain tax positions included in income tax obligations on our Condensed Consolidated Balance Sheet was approximately $16 million.

We file income tax returns in the United States, including various state and local jurisdictions. Our subsidiaries file tax returns in various foreign jurisdictions, including Canada, France, Germany, Switzerland and the United Kingdom. The IRS is currently examining our returns for fiscal years 2009 through 2011, and we remain subject to income tax examination by the IRS for fiscal years after 2011. We are also currently under income tax examination in the United Kingdom for fiscal years 2010 and 2012, in Germany for fiscal years 2008 through 2012, in Spain for fiscal years 2010 through 2013. We remain subject to income tax examination for several other jurisdictions including in Canada for fiscal years after 2005, in France for fiscal years after 2011, in Germany for fiscal years after 2012, in the United Kingdom for fiscal years 2011 and after 2012, and in Switzerland for fiscal years after 2007.

The timing of the resolution of income tax examinations is highly uncertain, and the amounts ultimately paid, if any, upon resolution of the issues raised by the taxing authorities may differ materially from the amounts accrued for each year. Although potential resolution of uncertain tax positions involve multiple tax periods and jurisdictions, it is reasonably possible that a reduction of up to $8 million of unrecognized tax benefits may occur within the next 12 months, some of which, depending on the nature of the settlement or expiration of statutes of limitations, may affect the Company’s income tax provision and therefore benefit the resulting effective tax rate. The actual amount could vary significantly depending on the ultimate timing and nature of any settlements.

(12) FINANCING ARRANGEMENTS

0.75% Convertible Senior Notes Due 2016

In July 2011, we issued $632.5 million aggregate principal amount of 0.75% Convertible Senior Notes due 2016 (the “Notes”). The Notes are senior unsecured obligations which pay interest semiannually in arrears at a rate of 0.75% per annum on January 15 and July 15 of each year, beginning on January 15, 2012 and will mature on July 15, 2016, unless purchased earlier or converted in accordance with their terms prior to such date. The Notes are senior in right of payment to any unsecured indebtedness that is expressly subordinated in right of payment to the Notes.

The Notes are convertible into cash and shares of our common stock based on an initial conversion value of 31.5075 shares of our common stock per $1,000 principal amount of Notes (equivalent to an initial conversion price of approximately $31.74 per share). Upon conversion of the Notes, holders will receive cash up to the principal amount of each Note, and any excess conversion value will be delivered in shares of our common stock. Prior to April 15, 2016, the Notes are convertible only if (1) the last reported sale price of the common stock for at least 20 trading days (whether or not consecutive) during the period of 30 consecutive trading days ending on the last trading day of the immediately preceding fiscal quarter is greater than or equal to 130 percent of the conversion price ($41.26 per share) on each applicable trading day; (2) during the five business day period after any ten consecutive trading day period in which the trading price per $1,000 principal amount of notes falls below 98 percent of the last reported sale price of our common stock multiplied by the conversion rate on each trading day; or (3) specified corporate transactions, including a change in control, occur. On or after April 15, 2016, a holder may convert any of its Notes at any time prior to the close of business on the second scheduled trading day immediately preceding the maturity date. The conversion rate is subject to customary anti-dilution adjustments (for example, certain dividend distributions or tender or exchange offer of our common stock), but will not be adjusted for any accrued and unpaid interest. The Notes are not redeemable prior to maturity except for specified corporate transactions and events of default, and no sinking fund is provided for the Notes. The Notes do not contain any financial covenants.

We separately account for the liability and equity components of the Notes. The carrying amount of the equity component representing the conversion option is equal to the fair value of the Convertible Note Hedge, as described below, which is a substantially identical instrument and was purchased on the same day as the Notes. The carrying amount of the liability

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component was determined by deducting the fair value of the equity component from the par value of the Notes as a whole, and represents the fair value of a similar liability that does not have an associated convertible feature. A liability of $525 million as of the date of issuance was recognized for the principal amount of the Notes representing the present value of the Notes' cash flows using a discount rate of 4.54 percent. The excess of the principal amount of the liability component over its carrying amount is amortized to interest expense over the term of the 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 $15 million of issuance costs paid in July 2011 related to the Notes issuance, we allocated $13 million to the liability component and $2 million to the equity component. Debt issuance costs attributable to the liability component are being amortized to interest expense over the term of the Notes, and issuance costs attributable to the equity component were netted with the equity component in additional paid-in capital.
The carrying values of the liability and equity components of the Notes are reflected in our Condensed Consolidated Balance Sheet as follows (in millions):

	As of September 30, 2014	As of March 31, 2014
Principal amount of Notes	$633	$633
Unamortized debt discount of the liability component	(42)	(53)
Net carrying amount of Notes	$591	$580
Equity component, net	$105	$105

As of September 30, 2014, the remaining life of the Notes is approximately 1.8 years.
Convertible Note Hedge and Warrants Issuance
In July 2011, we entered into privately negotiated convertible note hedge transactions (the "Convertible Note Hedge") with certain counterparties to reduce the potential dilution with respect to our common stock upon conversion of the Notes. The Convertible Note Hedge, subject to customary anti-dilution adjustments, provides us with the option to acquire, on a net settlement basis, approximately 19.9 million shares of our common stock at a strike price of $31.74, which corresponds to the conversion price of the Notes and is equal to the number of shares of our common stock that notionally underlie the Notes. As of September 30, 2014, we have not purchased any shares under the Convertible Note Hedge. We paid $107 million for the Convertible Note Hedge, which was recorded as an equity transaction.
Separately, in July 2011 we also entered into privately negotiated warrant transactions with the certain counterparties whereby we sold to independent third parties warrants (the "Warrants") to acquire, subject to customary anti-dilution adjustments that are substantially the same as the anti-dilution provisions contained in the Notes, up to 19.9 million shares of our common stock (which is also equal to the number of shares of our common stock that notionally underlie the Notes), with a strike price of $41.14. The Warrants could have a dilutive effect with respect to our common stock to the extent that the market price per share of our common stock exceeds $41.14 on or prior to the expiration date of the Warrants. We received proceeds of $65 million from the sale of the Warrants.
Effect of conversion on earning per share ("EPS")
The Notes have no impact on diluted EPS until the average quarterly price of our common stock exceeds the conversion price of $31.74 per share. Prior to conversion, we will include the effect of the additional shares that may be issued if our common stock price exceeds $31.74 per share using the treasury stock method. If the average price of our common stock exceeds $41.14 per share for a quarterly period, we will also include the effect of the additional potential shares that may be issued related to the Warrants using the treasury stock method. Prior to conversion, the Convertible Note Hedge is not considered for purposes of the EPS calculation, as its effect would be anti-dilutive. Upon conversion, the Convertible Note Hedge is expected to offset the dilutive effect of the Notes when the stock price is above $31.74 per share. See Note 15 for additional information related to our EPS.
Credit Facility
On August 30, 2012, we entered into a $500 million senior unsecured revolving credit facility with a syndicate of banks. The credit facility terminates on February 29, 2016 and contains an option to arrange with existing lenders

and/or new lenders for them to provide up to an aggregate of $250 million in additional commitments for revolving loans. Proceeds of loans made under the credit facility may be used for general corporate purposes.

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The loans bear interest, at our option, at the base rate plus an applicable spread or an adjusted LIBOR rate plus an applicable spread, in each case with such spread being determined based on our consolidated leverage ratio for the preceding fiscal quarter. We are also obligated to pay other customary fees for a credit facility of this size and type. Interest is due and payable in arrears quarterly for loans bearing interest at the base rate and at the end of an interest period (or at each three month interval in the case of loans with interest periods greater than three months) in the case of loans bearing interest at the adjusted LIBOR rate. Principal, together with all accrued and unpaid interest, is due and payable on February 29, 2016.

The credit agreement contains customary affirmative and negative covenants, including covenants that limit or restrict our ability to, among other things, incur subsidiary indebtedness, grant liens, dispose of all or substantially all assets and pay dividends or make distributions, in each case subject to customary exceptions for a credit facility of this size and type. We are also required to maintain compliance with a capitalization ratio and maintain a minimum level of total liquidity and a minimum level of domestic liquidity.

The credit agreement contains customary events of default, including among others, non-payment defaults, covenant defaults, bankruptcy and insolvency defaults and a change of control default, in each case, subject to customary exceptions for a credit facility of this size and type. The occurrence of an event of default could result in the acceleration of the obligations under the credit agreement, an obligation by any guarantors to repay the obligations in full and an increase in the applicable interest rate.

As of September 30, 2014, no amounts were outstanding under the credit facility. During the three months ended September 30, 2012, we paid $2 million of debt issuance costs in connection with obtaining this credit facility. These costs are deferred and are being amortized to interest expense over the 3.5 years term of the credit facility.

The following table summarizes our interest expense recognized for the three and six months ended September 30, 2014 and 2013 that is included in interest and other income (expense), net on our Condensed Consolidated Statements of Operations (in millions):

	Three Months Ended September 30,		Six Months Ended September 30,	
	2014	2013	2014	2013
Amortization of debt discount	$(6)	$(5)	$(11)	$(10)
Amortization of debt issuance costs	(1)	(1)	(2)	(2)
Coupon interest expense	(1)	(1)	(2)	(2)
Other interest expense	—	(1)	(1)	(1)
Total interest expense	$(8)	$(8)	$(16)	$(15)

(13) COMMITMENTS AND CONTINGENCIES

Lease Commitments

As of September 30, 2014, we leased certain facilities, furniture and equipment under non-cancelable operating lease agreements. We were required to pay property taxes, insurance and normal maintenance costs for certain of these facilities and any increases over the base year of these expenses on the remainder of our facilities.

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

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

In addition, we have certain celebrity, league and content license contracts that contain minimum guarantee payments and marketing commitments that may not be dependent on any deliverables. Celebrities and organizations with whom we have contracts include, but are not limited to: FIFA (Fédération Internationale de Football Association), FIFPRO Foundation, FAPL (Football Association Premier League Limited), and DFL Deutsche Fußball Liga GmbH (German Soccer League) (professional soccer); Dr. Ing. h.c. F. Porsche AG, Ferrari S.p.A. (Need For Speed and Real Racing games); National Basketball Association (professional basketball); PGA TOUR (professional golf); National Hockey League and NHL Players' Association (professional hockey); National Football League Properties, PLAYERS Inc., and Red Bear Inc. (professional football); Zuffa, LLC (Ultimate Fighting Championship); ESPN (content in EA SPORTS games); Hasbro, Inc. (certain of Hasbro's board game intellectual

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properties); Disney Interactive (Star Wars); Fox Digital Entertainment, Inc. (The Simpsons); and Universal Studios Inc. These developer and content license commitments represent the sum of (1) the cash payments due under non-royalty-bearing licenses and services agreements and (2) the minimum guaranteed payments and advances against royalties due under royalty-bearing licenses and services agreements, the majority of which are conditional upon performance by the counterparty. These minimum guarantee payments and any related marketing commitments are included in the table below.

The following table summarizes our minimum contractual obligations as of September 30, 2014 (in millions):

		Fiscal Years Ending March 31,						
	Total	2015 (Remaining six mos.)	2016	2017	2018	2019	2020	Thereafter
Unrecognized commitments								
Developer/licensor commitments	$1,066	$51	$263	$274	$147	$112	$76	$143
Marketing commitments	239	30	39	64	21	21	21	43
Operating leases	167	24	46	32	22	16	9	18
0.75% Convertible Senior Notes due 2016 interest [(a)]	9	2	5	2	—	—	—	—
Other purchase obligations	96	16	35	20	13	11	1	—
Total unrecognized commitments	1,577	123	388	392	203	160	107	204
Recognized commitments								
0.75% Convertible Senior Notes due 2016 principal [(a)]	633	—	—	633	—	—	—	—
Licensing and lease obligations [(b)]	181	11	22	23	23	24	25	53
Total recognized commitments	814	11	22	656	23	24	25	53
Total commitments	$2,391	$134	$410	$1,048	$226	$184	$132	$257

(a) Included in the $9 million coupon interest on the 0.75% Convertible Senior Notes due 2016 is $1 million of accrued interest recognized as of September 30, 2014. We will be obligated to pay the $632.5 million principal amount of the 0.75% Convertible Senior Notes due 2016 in cash and any excess conversion value in shares of our common stock upon redemption of the Notes at maturity on July 15, 2016 or upon earlier redemption. The $632.5 million principal amount excludes $42 million of unamortized discount of the liability component. See Note 12 for additional information regarding our 0.75% Convertible Senior Notes due 2016.

(b) See Note 8 for additional information regarding recognized commitments resulting from our restructuring plans. Lease commitments have not been reduced for approximately $6 million due in the future from third parties under non-cancelable sub-leases. See Note 9 for additional information regarding recognized obligations from our licensing-related commitments.

The unrecognized amounts represented in the table above reflect our minimum cash obligations for the respective fiscal years, but do not necessarily represent the periods in which they will be recognized and expensed in our Condensed Consolidated Financial Statements. In addition, the amounts in the table above are presented based on the dates the amounts are contractually due as of September 30, 2014; however, certain payment obligations may be accelerated depending on the performance of our operating results.

In addition to what is included in the table above, as of September 30, 2014, we had a liability for unrecognized tax benefits and an accrual for the payment of related interest totaling $89 million, of which we are unable to make a reasonably reliable estimate of when cash settlement with a taxing authority will occur.

Also, in addition to what is included in the table above as of September 30, 2014, in connection with our KlickNation acquisition, we may be required to pay an additional $3 million of cash consideration based upon the achievement of certain performance milestones through March 31, 2015. As of September 30, 2014, the accrued contingent consideration on our Condensed Consolidated Balance Sheet representing the estimated fair value of the contingent consideration was immaterial.

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Legal Proceedings

We are a defendant in several actions that allege we misappropriated the likenesses of various college athletes in certain of our college-themed sports games. In September 2013, we reached an agreement to settle all actions brought by college athletes against us. We recognized a $30 million accrual during the second quarter of fiscal year 2014 associated with the anticipated settlement. On September 3, 2014, the United States District Court for the Northern District of California granted preliminary approval of the settlement and set a hearing for May 14, 2015, to determine whether to grant its final approval of the settlement.

On December 17, 2013, a purported shareholder class action lawsuit was filed in the United States District Court for the Northern District of California against the Company and certain of its officers by an individual purporting to represent a class of purchasers of EA common stock. A second purported shareholder class action lawsuit alleging substantially similar claims was subsequently filed in the same court. These lawsuits have been consolidated into one action. The lawsuits, which assert claims under Section 10(b) and 20(a) of the Securities Exchange Act of 1934, allege, among other things, that the Company and certain of its officers issued materially false and misleading statements regarding the rollout of the Company's Battlefield 4 game. On October 20, 2014, the court granted our motion to dismiss all claims with leave for the plaintiffs to amend their complaint. As of the date of this filing, no amended complaint has been filed.

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

(14) STOCK-BASED COMPENSATION

Valuation Assumptions

We estimate the fair value of share-based payment awards on the date of grant. We recognize compensation costs for stock-based payment awards to employees based on the grant-date fair value using a straight-line approach over the service period for which such awards are expected to vest. For awards with only service conditions that have a graded vesting schedule, we recognize compensation costs on a straight-line basis over the requisite service period for the entire award.

We determine the fair value of our share-based payment awards as follows:

- Restricted Stock Units, Restricted Stock, and Performance-Based Restricted Stock Units. The fair value of restricted stock units, restricted stock, and performance-based restricted stock units (other than market-based restricted stock units) is determined based on the quoted market price of our common stock on the date of grant. Performance-based restricted stock units include grants made in connection with certain acquisitions.

- Market-Based Restricted Stock Units. Market-based restricted stock units consist of grants of performance-based restricted stock units to certain members of executive management that vest contingent upon the achievement of pre-determined market and service conditions (referred to herein as "market-based restricted stock units"). The fair value of our market-based restricted stock units is determined using a Monte-Carlo simulation model. Key assumptions for the Monte-Carlo simulation model are the risk-free interest rate, expected volatility, expected dividends and correlation coefficient.

- Stock Options and Employee Stock Purchase Plan. The fair value of stock options and stock purchase rights granted pursuant to our equity incentive plans and our 2000 Employee Stock Purchase Plan ("ESPP"), respectively, is determined using the Black-Scholes valuation model based on the multiple-award valuation method. Key assumptions of the Black-Scholes valuation model are the risk-free interest rate, expected volatility, expected term and expected dividends.

The determination of the fair value of market-based restricted stock units, stock options and ESPP is affected by assumptions regarding subjective and complex variables. Generally, our assumptions are based on historical information and judgment is required to determine if historical trends may be indicators of future outcomes.

There were no significant stock options granted during the three and six months ended September 30, 2013.

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

	Stock Option Grants		ESPP	
	Three Months Ended September 30,	Six Months Ended September 30,	Three Months Ended September 30,	
	2014	2014	2014	2013
Risk-free interest rate	1.2 - 1.9%	1.1 - 1.9%	0.04 - 0.1%	0.1 %
Expected volatility	36 - 38%	36 - 40%	34 - 35%	36 - 37%
Weighted-average volatility	37 %	38 %	35 %	37 %
Expected term	4.5	4.5	6 - 12 months	6 - 12 months
Expected dividends	None	None	None	None

There were no market-based restricted stock units granted during the three months ended September 30, 2014 and 2013.

Stock-Based Compensation Expense

Employee stock-based compensation expense recognized during the three and six months ended September 30, 2014 and 2013 was calculated based on awards ultimately expected to vest and has been reduced for estimated forfeitures. In subsequent periods, if actual forfeitures differ from those estimates, an adjustment to stock-based compensation expense will be recognized at that time.

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

	Three Months Ended September 30,		Six Months Ended September 30,	
	2014	2013	2014	2013
Cost of revenue	$1	$1	$1	$1
Research and development	23	23	39	43
Marketing and sales	6	6	10	13
General and administrative	10	8	19	14
Stock-based compensation expense	$40	$38	$69	$71

We did not recognize any benefit from income taxes related to our stock-based compensation expense recognized during the three and six months ended September 30, 2014 and 2013.

As of September 30, 2014, our total unrecognized compensation cost related to stock options was $21 million and is expected to be recognized over a weighted-average service period of 2.8 years. As of September 30, 2014, our total unrecognized compensation cost related to restricted stock and restricted stock units (collectively referred to as “restricted stock rights”) was $283 million and is expected to be recognized over a weighted-average service period of 1.7 years. Of the $283 million of unrecognized compensation cost, $17 million relates to market-based restricted stock units.

During the three and six months ended September 30, 2014, we recognized $2 million and $14 million, respectively, of tax expense for the excess tax benefits resulting from stock-based compensation deductions; this amount is allocated directly to contributed capital and reported in the financing activities on our Condensed Consolidated Statement of Cash Flows.

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Stock Options

The following table summarizes our stock option activity for the six months ended September 30, 2014:

	Options (in thousands)	Weighted-Average Exercise Prices	Weighted-Average Remaining Contractual Term (in years)	Aggregate Intrinsic Value (in millions)
Outstanding as of March 31, 2014	5,311	$ 37.43		
Granted	1,244	35.75		
Exercised	(291)	20.51		
Forfeited, cancelled or expired	(210)	49.83		
Outstanding as of September 30, 2014	6,054	$ 37.47	5.35	$ 34
Vested and expected to vest	5,671	$ 37.85	5.07	$ 32
Exercisable as of September 30, 2014	3,744	$ 41.43	2.85	$ 22

The aggregate intrinsic value represents the total pre-tax intrinsic value based on our closing stock price as of September 30, 2014, which would have been received by the option holders had all the option holders exercised their options as of that date. The weighted-average grant date fair values of stock options granted during the three and six months ended September 30, 2014 were $12.06 and $12.01, respectively. We issue new common stock from our authorized shares upon the exercise of stock options.

Restricted Stock Rights

The following table summarizes our restricted stock rights activity, excluding performance-based restricted stock unit activity which is discussed below, for the six months ended September 30, 2014:

	Restricted Stock Rights (in thousands)	Weighted-Average Grant Date Fair Values
Balance as of March 31, 2014	13,536	$ 19.70
Granted	3,893	35.70
Vested	(4,705)	19.63
Forfeited or cancelled	(930)	22.53
Balance as of September 30, 2014	11,794	$ 24.79

The weighted-average grant date fair values of restricted stock rights granted during the three and six months ended September 30, 2014 were $36.79 and $35.70 respectively.

Performance-Based Restricted Stock Units

The following table summarizes our performance-based restricted stock unit activity for the six months ended September 30, 2014:

	Performance-Based Restricted Stock Units (in thousands)	Weighted-Average Grant Date Fair Values
Balance as of March 31, 2014	54	$ 15.39
Vested	(49)	15.39
Forfeited or cancelled	(5)	15.39
Balance as of September 30, 2014	—	—

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Market-Based Restricted Stock Units

Our market-based restricted stock units vest contingent upon the achievement of pre-determined market and service conditions. If these market conditions are not met but service conditions are met, the restricted stock units will not vest; however, any compensation expense we have recognized to date will not be reversed. The number of shares of common stock to be received at vesting will range from zero percent to 200 percent of the target number of stock units based on our total stockholder return ("TSR") relative to the performance of companies in the NASDAQ-100 Index for each measurement period, generally over a three year period. In the table below, we present shares granted at 100 percent of target of the number of stock units that may potentially vest. The maximum number of common shares that could vest is approximately 0.4 million for market-based restricted stock units granted during the six months ended September 30, 2014. As of September 30, 2014, the maximum number of shares that could vest is approximately 1.3 million for market-based restricted stock units outstanding.

The following table summarizes our market-based restricted stock unit activity for the six months ended September 30, 2014:

	Market-Based Restricted Stock Units (in thousands)	Weighted-Average Grant Date Fair Value
Balance as of March 31, 2014	978	$24.83
Granted	193	46.96
Vested	(671)	21.45
Vested above target	192	16.80
Forfeited or cancelled	(29)	33.70
Balance as of September 30, 2014	663	$31.97

Stock Repurchase Program

In May 2014, a special committee of our Board of Directors, on behalf of the full Board of Directors, authorized a new program to repurchase up to $750 million of our common stock. This new stock repurchase program, which expires on May 31, 2016, supersedes and replaces the stock repurchase authorization approved by our Board of Directors in July 2012. Under this program, we may purchase stock in the open market or through privately-negotiated transactions in accordance with applicable securities laws, including pursuant to pre-arranged stock trading plans. The timing and actual amount of the stock repurchases will depend on several factors including price, capital availability, regulatory requirements, alternative investment opportunities and other market conditions. We are not obligated to repurchase any specific number of shares under this program and it may be modified, suspended or discontinued at any time. During the three and six months ended September 30, 2014, we repurchased approximately 2.6 million and 4.0 million shares of our common stock for approximately $95 million and $145 million, respectively. During the three and six months ended September 30, 2013, we did not repurchase any shares of our common stock.

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(15) NET INCOME (LOSS) PER SHARE

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

	Three Months Ended September 30,		Six Months Ended September 30,	
(In millions, except per share amounts)	2014	2013	2014	2013
Net income (loss)	$3	$(273)	$338	$(51)
Shares used to compute net income (loss) per share:				
Weighted-average common stock outstanding — basic	313	308	312	306
Dilutive potential common shares related to stock award plans and from assumed exercise of stock options	6	—	8	—
Dilutive potential common shares related to the Notes	3	—	2	—
Weighted-average common stock outstanding — diluted	322	308	322	306
Net income (loss) per share:				
Basic	$0.01	$(0.89)	$1.08	$(0.17)
Diluted	$0.01	$(0.89)	$1.05	$(0.17)

For the three and six months ended September 30, 2014, options to purchase, restricted stock units and restricted stock to be released in the amount of 4 million shares were excluded from the treasury stock method computation of diluted shares as their inclusion would have had an antidilutive effect.

As a result of our net loss for the three and six months ended September 30, 2013, we have excluded all outstanding equity-based instruments from the diluted loss per share calculation as their inclusion would have had an antidilutive effect. Had we reported net income for these periods, an additional 8 million shares of common stock would have been included in the number of shares to calculated Diluted EPS for both the three and six months ended September 30, 2013.

For the three and six months ended September 30, 2013, potentially dilutive shares of common stock related to our 0.75% Convertible Senior Notes due 2016 issued during fiscal year 2012, which have a conversion price of $31.74 per share and the associated Warrants, which have a conversion price of $41.14 per share, were excluded from the computation of Diluted EPS as their inclusion would have had an antidilutive effect resulting from the conversion price. The associated Convertible Note Hedge was excluded from the computation of diluted shares as the impact is always considered antidilutive. See Note 12 for additional information related to our 0.75% Convertible Senior Notes due 2016 and related Convertible Note Hedge and Warrants.

(16) SEGMENT INFORMATION

Our reporting segment is based upon: our internal organizational structure; the manner in which our operations are managed; the criteria used by our Chief Executive Officer, our Chief Operating Decision Maker (“CODM”), to evaluate segment performance; the availability of separate financial information; and overall materiality considerations.
Prior to the third quarter of fiscal 2014, our “EA Labels” operating segment was comprised of our five labels: EA Games, EA SPORTS, Maxis, PopCap and All Play. Our CODM regularly reviewed the aggregated results of the five labels to assess overall performance and allocate resources.
In September 2013, we announced the appointment of a new Chief Executive Officer. Our new Chief Executive Officer subsequently made a number of changes to our internal organizational structure and the manner in which our operations are managed. In addition, we redefined our definition of segment profit for management reporting. Our CODM currently reviews total company operating results to assess overall performance and allocate resources.

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The following table summarizes the financial performance of our current segment operating profit and a reconciliation to our consolidated operating income for the three and six months ended September 30, 2014 and 2013. Our current segment operating profit differs from the prior "EA Labels" segment profit primarily due to the inclusion of (1) our Switzerland distribution revenues and expenses and (2) certain corporate and other functional costs such as our Global Publishing and Marketing organization expenses, which were previously not allocated to the EA Labels. Prior periods below have been restated to reflect our current reporting segment structure (in millions):

	Three Months Ended September 30,		Six Months Ended September 30,	
	2014	2013	2014	2013
Segment:				
Net revenue before revenue deferral	$1,220	$1,040	$1,995	$1,535
Depreciation	(33)	(32)	(64)	(62)
Other expenses	(878)	(865)	(1,537)	(1,491)
Segment operating profit (loss)	309	143	394	(18)
Reconciliation to consolidated operating income:				
Other:				
Revenue deferral	(1,035)	(879)	(1,658)	(1,234)
Recognition of revenue deferral	805	534	1,867	1,343
Amortization of intangibles	(16)	(18)	(33)	(37)
Acquisition-related contingent consideration	1	44	2	37
Restructuring and other charges	—	2	—	1
Stock-based compensation	(40)	(38)	(69)	(71)
Loss on licensed intellectual property commitment	—	—	(122)	—
Other expenses	—	(40)	5	(40)
Consolidated operating income (loss)	$24	$(252)	$386	$(19)

Our segment profit differs from consolidated operating income primarily due to the exclusion of (1) the deferral of certain net revenue related to online-enabled games (see Note 10 for additional information regarding deferred net revenue (online-enabled games)), (2) certain non-cash costs such as stock-based compensation, (3) acquisition-related expenses such as amortization of intangibles and acquisition-related contingent consideration, and (4) other significant non-recurring costs that may not be indicative of the company's core business, operating results or future outlook. Our CODM reviews assets on a consolidated basis and not on a segment basis.

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Information about our total net revenue by revenue composition and by platform for the three and six months ended September 30, 2014 and 2013 is presented below (in millions):

	Three Months Ended September 30,		Six Months Ended September 30,	
	2014	2013	2014	2013
Packaged goods and other	$482	$245	$1,160	$712
Digital	508	450	1,044	932
Net revenue	$990	$695	$2,204	$1,644

	Three Months Ended September 30,		Six Months Ended September 30,	
	2014	2013	2014	2013
Platform net revenue				
Xbox One, PlayStation 4	$317	$—	$610	$—
Xbox 360, PlayStation 3	308	298	851	792
Other consoles	6	11	9	15
Total consoles	631	309	1,470	807
PC / Browser	208	274	439	572
Mobile	123	75	246	188
Other	28	37	49	77
Net revenue	$990	$695	$2,204	$1,644

Information about our operations in North America and internationally as of and for the three and six months ended September 30, 2014 and 2013 is presented below (in millions):

	Three Months Ended September 30,		Six Months Ended September 30,	
	2014	2013	2014	2013
Net revenue from unaffiliated customers				
North America	$433	$303	$955	$698
International	557	392	1,249	946
Net revenue	$990	$695	$2,204	$1,644

	As of September 30,	
	2014	2013
Long-lived assets		
North America	$1,886	$1,981
International	463	493
Total	$2,349	$2,474

We attribute net revenue from external customers to individual countries based on the location of the legal entity that sells the products and/or services. Note that revenue attributed to the legal entity that makes the sale is often not the country where the consumer resides. For example, revenue generated by our Swiss legal entities includes digital revenue from consumers who reside outside of Switzerland, including consumers who reside outside of Europe. Revenue generated by our Swiss legal entities during the three and six months ended September 30, 2014 represented $195 million and $635 million, or 20 percent and 29 percent, of our total net revenue, respectively. Revenue generated by our Swiss legal entities during the three and six months ended September 30, 2013 represented $136 million and $539 million, or 20 percent and 33 percent, of our total net revenue, respectively. Revenue generated in the United States represents over 99 percent of our total North America net revenue. There were no other countries with net revenue greater than 10 percent.

Our direct sales to GameStop Corp. represented approximately 16 percent and 14 percent of total net revenue, respectively, during the three and six months ended September 30, 2014. Our direct sales to GameStop Corp.

represented approximately 16 percent and 12 percent of total net revenue for the three and six months ended September 30, 2013, respectively.

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Report of Independent Registered Public Accounting Firm

The Board of Directors and Stockholders
Electronic Arts Inc.:

We have reviewed the accompanying condensed consolidated balance sheet of Electronic Arts Inc. and subsidiaries (the Company) as of September 27, 2014, and the related condensed consolidated statements of operations and comprehensive income (loss), for the three-month and six-month periods ended September 27, 2014 and September 28, 2013, and the related condensed consolidated statements of cash flows for the six-month periods ended September 27, 2014 and September 28, 2013. These condensed consolidated financial statements are the responsibility of the Company's management.

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

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

We have previously audited, in accordance with standards of the Public Company Accounting Oversight Board (United States), the consolidated balance sheet of Electronic Arts Inc. and subsidiaries as of March 29, 2014, and the related consolidated statements of operations, comprehensive income (loss), stockholders' equity, and cash flows for the year then ended (not presented herein); and in our report dated May 21, 2014, we expressed an unqualified opinion on those consolidated financial statements. In our opinion, the information set forth in the accompanying condensed consolidated balance sheet as of March 29, 2014, is fairly stated, in all material respects, in relation to the consolidated balance sheet from which it has been derived.

/s/ KPMG LLP
Santa Clara, California
November 4, 2014

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

CAUTIONARY NOTE ABOUT FORWARD-LOOKING STATEMENTS

This Quarterly Report contains forward-looking statements within the meaning of the Private Securities Litigation Reform Act of 1995. All statements, other than statements of historical fact, made in this Quarterly Report are forward looking. Examples of forward-looking statements include statements related to industry prospects, our future economic performance including anticipated revenues and expenditures, results of operations or financial position, and other financial items, our business plans and objectives, including our intended product releases, and may include certain assumptions that underlie the forward-looking statements. We use words such as "anticipate," "believe," "expect," "intend," "estimate" (and the negative of any of these terms), "future" and similar expressions to help identify forward-looking statements. These forward-looking statements are subject to business and economic risk and reflect management's current expectations, and involve subjects that are inherently uncertain and difficult to predict. Our actual results could differ materially from those in the forward-looking statements. We will not necessarily update information if any forward-looking statement later turns out to be inaccurate. Risks and uncertainties that may affect our future results include, but are not limited to, those discussed in this report under the heading "Risk Factors" in Part II, Item 1A, as well as in our Annual Report on Form 10-K for the fiscal year ended March 31, 2014 as filed with the Securities and Exchange Commission ("SEC") on May 21, 2014 and in other documents we have filed with the SEC.

OVERVIEW

The following overview is a high-level discussion of our operating results, as well as some of the trends and drivers that affect our business. Management believes that an understanding of these trends and drivers is important in order to understand our results for the three and six months ended September 30, 2014, as well as our future prospects. This summary is not intended to be exhaustive, nor is it intended to be a substitute for the detailed discussion and analysis provided elsewhere in this Form 10-Q, including in the remainder of "Management's Discussion and Analysis of Financial Condition and Results of Operations ("MD&A")," "Risk Factors," and the Condensed Consolidated Financial Statements and related Notes. Additional information can be found in the "Business" section of our Annual Report on Form 10-K for the fiscal year ended March 31, 2014 as filed with the SEC on May 21, 2014 and in other documents we have filed with the SEC.

About Electronic Arts

We develop, market, publish and distribute game software content and services that can be played by consumers on a variety of platforms, including video game consoles (such as PlayStation 3 and 4 from Sony and Xbox 360 and Xbox One from Microsoft), personal computers, mobile phones and tablets. Our ability to deliver games and services across multiple platforms, through multiple distribution channels, and directly to consumers (online and wirelessly) has been, and will continue to be, a cornerstone of our product strategy. We have adopted new business models and alternative revenue streams (such as subscription, micro-transactions, and advertising) in connection with our online and wireless product and service offerings. Some of our games are based on our wholly-owned intellectual property (e.g., Battlefield, Mass Effect, Need for Speed, Dragon Age, The Sims, Bejeweled, and Plants vs. Zombies), and some of our games leverage content that we license from others (e.g., FIFA, Madden NFL and Star Wars). We also publish and distribute games developed by third parties (e.g., Titanfall). Our goal is to turn our intellectual properties into year-round businesses available on a range of platforms. Our products and services may be purchased through physical and online retailers, platform providers such as console manufacturers and mobile carriers via digital downloads, as well as directly through our own distribution platform, including online portals such as Origin.

Financial Results

Total net revenue for the three months ended September 30, 2014 was $990 million, an increase of $295 million, or 42 percent, as compared to the three months ended September 30, 2013. Net revenue for the three months ended September 30, 2014 was driven by FIFA 14, Battlefield 4, and Titanfall. At September 30, 2014, deferred net revenue associated with sales of online-enabled games increased by $230 million as compared to June 30, 2014, directly decreasing the amount of reported net revenue during the three months ended September 30, 2014. At September 30, 2013, deferred net revenue associated with sales of online-enabled games increased by $345 million as compared to

June 30, 2013, directly decreasing the amount of reported net revenue during the three months ended September 30, 2013. Disregarding the impact of the deferred net revenue, reported net revenue would have increased by approximately $180 million, or 17 percent, during the three months ended September 30, 2014 as compared to the three months ended September 30, 2013.

International net revenue was $557 million, or 56 percent of total net revenue during the three months ended September 30, 2014, compared to $392 million, or 56 percent of total net revenue during the three months ended September 30, 2013, an increase of $165 million, or 42 percent. We estimate that foreign exchange rates (primarily due to the British pound sterling) increased reported International net revenue by approximately $9 million, or 2 percent, for the three months ended September 30, 2014 as compared to the exchange rates in effect for the three months ended September 30, 2013. Excluding the effect of foreign exchange rates from International net revenue, we estimate that International net revenue increased by approximately $156 million, or 40 percent for three months ended September 30, 2014 as compared to three months ended September 30, 2013. This increase is primarily due to our FIFA and Battlefield franchises, and Titanfall, partially offset by decreased revenue in our SimCity, Crysis, and Dead Space franchises.

Net income for the three months ended September 30, 2014 was $3 million as compared to a net loss of $273 million for the three months ended September 30, 2013. Diluted earnings per share for the three months ended September 30, 2014 was $0.01 as compared to a diluted loss per share of $0.89 for the three months ended September 30, 2013. Net income increased for the three months ended September 30, 2014 as compared to the three months ended September 30, 2013 primarily as a result of a $295 million increase in net revenue and a 16.3 percent increase in gross profit percentage, partially offset by a $5 million increase in operating expenses.

Trends in Our Business

Console System Transition. In November 2013, the PlayStation 4 from Sony and Xbox One from Microsoft were released. EA delivered five major products for each of these new-generation console systems around the time of their launch, and we are continuing to make significant investments in products and services for these new consoles. We also expect to continue to develop and market products and services for the Microsoft Xbox 360 and the Sony PlayStation 3. Industry sales of major games for these legacy consoles declined significantly during our 2014 fiscal year. This sales decline trend is likely to continue and may accelerate. The success of our products and services for the new-generation consoles depends in part on the commercial success and adequate supply of, as well as our ability to develop commercially successful products and services for, these consoles.

Digital Transformation. Our business continues to transform from a traditional packaged goods business model to one in which our games and services are sold and delivered via a network connection, with digitally-delivered content, features and services helping to extend the life of the respective game offering. For example, many of our products that traditionally have been sold only as packaged goods products can now also be purchased and downloaded via a network connection. We also include digitally-delivered content, features and services as part of the product offering, either made available for free or at additional cost. Additionally, our mobile and PC free-to-play games are available solely via digital delivery and are typically monetized through a micro-transaction business model through which we sell incremental content and/or features in discrete transactions. In addition, our EA Access for the Xbox One is a subscription service that offers players access to a selection of EA games and other benefits for a monthly or annual fee.

We significantly increased the digital revenue that we derive from wireless, Internet-derived and advertising products and services from $1,159 million in fiscal year 2012 to $1,440 million in fiscal year 2013. During fiscal year 2014, digital revenue was $1,833 million and we expect this portion of our business to continue to grow in fiscal 2015 and beyond.

Mobile and PC Free-to-Play Games. The proliferation of mobile phones and tablets has significantly increased the consumer base for mobile games. The broad consumer acceptance of free-to-play business models, which allow consumers to try new games with no up-front cost and pay for additional content or in-game items through micro-transactions, has led to growth in the mobile gaming industry. Likewise, the mass introduction and wide consumer acceptance of free-to-play, micro-transaction-based PC games played over the Internet has also broadened our consumer base. We expect revenue generated from mobile and PC free-to-play games to remain an important part of our business.

We track an estimate of monthly active users (“MAUs”) for our mobile business, which we believe is a useful indicator of player engagement trends. For the three months ended September 30, 2014, we had average MAUs of over 155 million. MAUs are the aggregate number of individuals who accessed a particular game on a particular device in the last 30 days as of the measurement date. Average MAUs for a particular period is the average of the MAUs at each month-end during that period. We include in this calculation data provided by our third party publishing partners for certain games that we develop but we exclude information from third party titles that we publish. Our methodology for calculating MAU may differ from the methodology used by other companies to calculate this metric.

Concentration of Sales Among the Most Popular Games. In all major segments of our industry, we see a larger portion of games sales concentrated on the most popular titles, and many of those titles are sequels of prior games. We have responded to this trend by significantly reducing the number of games that we produce to provide greater focus on our most promising intellectual properties. For example, in fiscal year 2011, we published over 30 titles for consoles and PC, while in fiscal year

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2014 we published 11; in fiscal year 2015, we expect to release 10 titles for console and PC. We have similarly reduced the number of major mobile titles that we publish.

Recent Developments

In May 2014, a special committee of our Board of Directors, on behalf of the full Board of Directors, authorized a new program to repurchase up to $750 million of our common stock. This new stock repurchase program, which expires on May 31, 2016, supersedes and replaces the stock repurchase authorization approved by our Board of Directors in July 2012. Under this program, we may purchase stock in the open market or through privately-negotiated transactions in accordance with applicable securities laws, including pursuant to pre-arranged stock trading plans. The timing and actual amount of the stock repurchases will depend on several factors including price, capital availability, regulatory requirements, alternative investment opportunities and other market conditions. We are not obligated to repurchase any specific number of shares under this program and it may be modified, suspended or discontinued at any time.

During the three and six months ended September 30, 2014, we repurchased and retired approximately 2.6 million and 4.0 million shares of our common stock for approximately $95 million and $145 million, respectively. We continue to actively repurchase shares under this program.

CRITICAL ACCOUNTING POLICIES AND ESTIMATES

Our Condensed Consolidated Financial Statements have been prepared in accordance with accounting principles generally accepted in the United States (“U.S. GAAP”). The preparation of these Condensed Consolidated Financial Statements requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities, contingent assets and liabilities, and revenue and expenses during the reporting periods. The policies discussed below are considered by management to be critical because they are not only important to the portrayal of our financial condition and results of operations, but also because application and interpretation of these policies requires both management judgment and estimates of matters that are inherently uncertain and unknown. As a result, actual results may differ materially from our estimates.

Revenue Recognition, Sales Returns and Allowances, and Bad Debt Reserves

We derive revenue principally from sales of interactive software games, and related content and services on (1) video game consoles (such as Playstation 3 and 4 from Sony and Xbox 360 and Xbox One from Microsoft) and PCs, and (2) mobile phones and tablets. We evaluate revenue recognition based on the criteria set forth in FASB Accounting Standards Codification (“ASC”) 605, Revenue Recognition and ASC 985-605, Software: Revenue Recognition. We classify our revenue as either product revenue or service and other revenue.

Product revenue. Our product revenue includes revenue associated with the sale of software games or related content, whether delivered via a physical disc (e.g., packaged goods) or delivered digitally via the Internet (e.g., full-game downloads, micro-transactions), and licensing of game software to third-parties. Product revenue also includes revenue from mobile full game downloads that do not require our hosting support (e.g., premium mobile games), and sales of tangible products such as hardware, peripherals, or collectors’ items.

Service and other revenue. Our service revenue includes revenue recognized from time-based subscriptions and games or related content that requires our hosting support in order to utilize the game or related content (i.e., can only be played with an Internet connection). This includes (1) entitlements to content that are accessed through hosting services (e.g., micro-transactions for Internet-based, social network and freemium mobile games), (2) massively multi-player online (“MMO”) games (both software game and subscription sales), (3) subscriptions for our Battlefield Premium and Pogo-branded online game services, and (4) allocated service revenue from sales of software games with an online service element (i.e., “matchmaking” service). Our other revenue includes advertising and non-software licensing revenue.

With respect to the allocated service revenue from sales of software games with a matchmaking service mentioned above, our allocation of proceeds between product and service revenue for presentation purposes is based on management's best estimate of the selling price of the matchmaking service with the residual value allocated to product revenue. Our estimate of the selling price of the matchmaking service is comprised of several factors including, but not limited to, prior selling prices for the matchmaking service, prices charged separately by other third-party vendors for similar service offerings, and a cost-plus-margin approach. We review the estimated selling price of the online matchmaking service on a regular basis and use this methodology consistently to allocate revenue between product and service for software game sales with a matchmaking service.

We evaluate and recognize revenue when all four of the following criteria are met:

- Evidence of an arrangement. Evidence of an agreement with the customer that reflects the terms and conditions to deliver the related products or services must be present.

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

- Collection is deemed probable. Collection is deemed probable if we expect the customer to be able to pay amounts under the arrangement as those amounts become due. If we determine that collection is not probable as the amounts become due, we generally conclude that collection becomes probable upon cash collection.

- Delivery. For packaged goods, delivery is considered to occur when a product is shipped and the risk of loss and rewards of ownership have transferred to the customer. For digital downloads, delivery is considered to occur when the software is made available to the customer for download. For services and other, delivery is generally considered to occur as the service is delivered, which is determined based on the underlying service obligation.

Online-Enabled Games

The majority of our software games can be connected to the Internet whereby a consumer may be able to download unspecified content or updates on a when-and-if-available basis (“unspecified updates”) for use with the original game software. In addition, we may also offer an online matchmaking service that permits consumers to play against each other via the Internet without a separate fee. U.S. GAAP requires us to account for the consumer’s right to receive unspecified updates or the matchmaking service for no additional fee as a “bundled” sale, or multiple-element arrangement.

We have an established historical pattern of providing unspecified updates to online-enabled games (e.g., player roster updates to Madden NFL 25) at no additional charge to the consumer. We do not have vendor-specific objective evidence of fair value (“VSOE”) for these unspecified updates, and thus, as required by U.S. GAAP, we recognize revenue from the sale of these online-enabled games over the period we expect to offer the unspecified updates to the consumer (“estimated offering period”).

Estimated Offering Period

Because the offering period is not an explicitly defined period, we must make an estimate of the offering period. Determining the estimated offering period is inherently subjective and is subject to regular revision based on historical online usage. For example, in determining the estimated offering period for unspecified updates associated with our online-enabled games, we consider the period of time consumers are online as online connectivity is required. On an annual basis, we review consumers’ online gameplay of all online-enabled games that have been released 12 to 24 months prior to the evaluation date. For example, if our evaluation date is April 1, 2014, we evaluate all online-enabled games released between April 1, 2012 and March 31, 2013. Based on this population of games, for all players that register the game online within the first six months of release of the game to the general public, we compute the weighted-average number of days for each online-enabled game, based on when a player initially registers the game online to when that player last plays the game online. We then compute the weighted-average number of days for all online-enabled games by multiplying the weighted-average number of days for each online-enabled game by its relative percentage of total units sold from these online-enabled games (i.e., a game with more units sold will have a higher weighting to the overall computation than a game with fewer units sold). Under a similar computation, we also consider the estimated period of time between the date a game unit is sold to a reseller and the date the reseller sells the game unit to an end consumer (i.e., time in channel). Based on these two calculations we then consider the method of distribution. For example, physical software games sold at retail would have a composite offering period equal to the online gameplay plus time in channel as opposed to digitally distributed software games which are delivered immediately via digital download and thus have no concept of channel. Additionally, we consider results from prior years, known online gameplay trends, as well as disclosed service periods for competitors' games in determining the estimated offering period for future sales.

While we consistently apply this methodology, inherent assumptions used in this methodology include which online-enabled games to sample, whether to use only units that have registered online, whether to weight the number of days for each game, whether to weight the days based on the units sold of each game, determining the period of time between the date of sale to reseller and the date of sale to the consumer and assessing online gameplay trends.

Prior to July 1, 2013, for most sales, we estimated the offering period to be six months and recognized revenue over this period in the month after delivery. During the three months ended September 30, 2013, we completed our fiscal 2014 annual

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evaluation of the estimated offering period and noted that generally, consumers were playing our games online over a longer period of time. Based on this, we concluded that for physical software sales made after June 30, 2013, the estimated offering period should be increased to nine months, resulting in revenue being recognized over a longer period of time. This change in estimate resulted in an estimated decrease to net revenue and net income of $474 million and a decrease of $1.50 of diluted earnings per share for fiscal year 2014. During the three months ended September 30, 2014, this change in estimate resulted in an estimated increase to net revenue and net income of $181 million and an increase of $0.56 of diluted earnings per share. During the six months ended September 30, 2014, this change in estimate resulted in an estimated increase to net revenue and net income of $286 million and an increase of $0.89 of diluted earnings per share. The estimated offering period for digitally distributed games did not change and is six months. We completed our fiscal 2015 annual evaluation during the second quarter and determined that the estimated offering period for physical software sales and digital sales continues to be nine months and six months, respectively.

Other Multiple-Element Arrangements

In some of our multiple-element arrangements, we sell tangible products with software and/or software-related offerings. These tangible products are generally either peripherals or ancillary collectors' items, such as figurines and comic books. Revenue for these arrangements is allocated to each separate unit of accounting for each deliverable using the relative selling prices of each deliverable in the arrangement based on the selling price hierarchy described below. If the arrangement contains more than one software deliverable, the arrangement consideration is allocated to the software deliverables as a group and then allocated to each software deliverable in accordance with ASC 985-605.

We determine the selling price for a tangible product deliverable based on the following selling price hierarchy: VSOE (i.e., the price we charge when the tangible product is sold separately) if available, third-party evidence ("TPE") of fair value (i.e., the price charged by others for similar tangible products) if VSOE is not available, or our best estimate of selling price ("BESP") if neither VSOE nor TPE is available. Determining the BESP is a subjective process that is based on multiple factors including, but not limited to, recent selling prices and related discounts, market conditions, customer classes, sales channels and other factors. In accordance with ASC 605, provided the other three revenue recognition criteria other than delivery have been met, we recognize revenue upon delivery to the customer as we have no further obligations.

We must make assumptions and judgments in order to (1) determine whether and when each element is delivered, (2) determine whether VSOE exists for each undelivered element, and (3) allocate the total price among the various elements, as applicable. Changes to any of these assumptions and judgments, or changes to the elements in the arrangement, could cause a material increase or decrease in the amount of revenue that we report in a particular period.

In May 2014, the FASB issued ASU No. 2014-09, Revenue from Contracts with Customers, which requires an entity to recognize the amount of revenue to which it expects to be entitled for the transfer of promised goods or services to customers. The ASU will replace most existing revenue recognition guidance in U.S. GAAP when it becomes effective. The new standard is effective for annual reporting periods beginning after December 15, 2016. Early application is not permitted. The standard permits the use of either the retrospective or cumulative effect transition method. The Company is evaluating the effect that ASU 2014-09 will have on its Condensed Consolidated Financial Statements and related disclosures. The Company has not yet selected a transition method nor has it determined the effect of the standard on its ongoing financial reporting. We expect to adopt this new standard in the first quarter of fiscal year 2018.

Principal Agent Considerations

In accordance with ASC 605-45, Revenue Recognition: Principal Agent Considerations, we evaluate sales of our interactive software games via third party storefronts, including digital storefronts such as Xbox Live Marketplace, Sony PSN, Apple AppStore, Google Play, in order to determine whether or not we are acting as the principal or as an agent, which we consider in determining if revenue should be reported gross or net of fees retained by the storefront.

Key indicators that we evaluate in determining gross versus net treatment include but are not limited to the following:

- The party responsible for delivery/fulfillment of the product or service to the end consumer
- The party responsible for the billing, collection of fees and refunds to the consumer
- The storefront and Terms of Sale that govern the consumer's purchase of the product or service
- The party that sets the pricing with the consumer and has credit risk

Based on the evaluation of the above indicators, we have determined that we are generally acting as an agent and are not considered the primary obligor to consumers for our interactive software games distributed through third party digital storefronts. We therefore recognize revenue related to these arrangements on a net basis.

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Sales Returns and Allowances and Bad Debt Reserves

We reduce revenue primarily for estimated future returns and price protection which may occur with our distributors and retailers (“channel partners”). Price protection represents our practice to provide our channel partners with a credit allowance to lower their wholesale price on a particular product in the channel. The amount of the price protection is generally the difference between the old wholesale price and the new reduced wholesale price. In certain countries for our PC and console packaged goods software products, we also have a practice of allowing channel partners to return older software products in the channel in exchange for a credit allowance. As a general practice, we do not give cash refunds.

When evaluating the adequacy of sales returns and price protection allowances, we analyze the following: historical credit allowances, current sell-through of our channel partners’ inventory of our software products, current trends in retail and the video game industry, changes in customer demand, acceptance of our software products, and other related factors. In addition, we monitor the volume of sales to our channel partners and their inventories, as substantial overstocking in the distribution channel could result in high returns or higher price protection in subsequent periods.

In the future, actual returns and price protections may materially exceed our estimates as unsold software products in the distribution channels are exposed to rapid changes in consumer preferences, market conditions or technological obsolescence due to new platforms, product updates or competing software products. While we believe we can make reliable estimates regarding these matters, these estimates are inherently subjective. Accordingly, if our estimates change, our returns and price protection allowances would change and would impact the total net revenue, accounts receivable and deferred net revenue that we report.

We determine our allowance for doubtful accounts by evaluating the following: customer creditworthiness, current economic trends, historical experience, age of current accounts receivable balances, changes in financial condition or payment terms of our customers. Significant management judgment is required to estimate our allowance for doubtful accounts in any accounting period. The amount and timing of our bad debt expense and cash collection could change significantly as a result of a change in any of the evaluation factors mentioned above.

Fair Value Estimates

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

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

While we are required to make certain fair value assessments associated with the accounting for several types of transactions,