TAKE TWO INTERACTIVE SOFTWARE INC
Form 10-Q
February 08, 2017

Table of Contents

UNITED STATES
SECURITIES AND EXCHANGE COMMISSION

WASHINGTON, D.C. 20549

FORM 10-Q

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

For the quarterly period ended December 31, 2016

OR

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

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

TAKE-TWO INTERACTIVE SOFTWARE, INC.

(Exact Name of Registrant as Specified in Its Charter)

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

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

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

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

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

Large accelerated filer ý Accelerated filer o Non-accelerated filer o Smaller reporting company o

(Do not check if a smaller reporting company)

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

As of January 31, 2017, there were 101,410,198 shares of the Registrant's Common Stock outstanding, net of treasury stock.

Table of Contents

INDEX

PART I.	**FINANCIAL INFORMATION**	2
Item 1.	Financial Statements (Unaudited)	2
	Condensed Consolidated Balance Sheets	2
	Condensed Consolidated Statements of Operations	3
	Condensed Consolidated Statements of Comprehensive Income (Loss)	4
	Condensed Consolidated Statements of Cash Flows	5
	Notes to Condensed Consolidated Financial Statements	6
Item 2.	Management's Discussion and Analysis of Financial Condition and Results of Operations	23
Item 3.	Quantitative and Qualitative Disclosures About Market Risk	41
Item 4.	Controls and Procedures	42
PART II.	**OTHER INFORMATION**	44
Item 1.	Legal Proceedings	44
Item 1A.	Risk Factors	44
Item 2.	Unregistered Sales of Equity Securities and Use of Proceeds	44
Item 6.	Exhibits	45
	Signatures	47

(All other items in this report are inapplicable)

Table of Contents

PART I. FINANCIAL INFORMATION

Item 1. Financial Statements (Unaudited)

TAKE-TWO INTERACTIVE SOFTWARE, INC.

CONDENSED CONSOLIDATED BALANCE SHEETS

(in thousands, except per share amounts)

	December 31, 2016 (Unaudited)	March 31, 2016
ASSETS		
Current assets:		
Cash and cash equivalents	**1,039,430**	798,742
Short-term investments	**404,523**	470,820
Restricted cash	**278,541**	261,169
Accounts receivable, net of allowances of $107,347 and $45,552 at December 31, 2016 and March 31, 2016, respectively	**327,430**	168,527
Inventory	**26,665**	15,888
Software development costs and licenses	**126,185**	178,387
Deferred cost of goods sold	**177,946**	98,474
Prepaid expenses and other	**70,456**	53,269
Total current assets	**2,451,176**	2,045,276
Fixed assets, net	**65,799**	77,127
Software development costs and licenses, net of current portion	**327,117**	214,831
Deferred cost of goods sold, net of current portion		17,915
Goodwill	**213,522**	217,080
Other intangibles, net	**3,211**	4,609
Other assets	**28,274**	13,439
Total assets	**3,089,099**	2,590,277
LIABILITIES AND STOCKHOLDERS' EQUITY		
Current liabilities:		
Accounts payable	**54,248**	30,448
Accrued expenses and other current liabilities	**736,176**	607,479
Deferred revenue	**1,073,393**	582,484
Total current liabilities	**1,863,817**	1,220,411
Long-term debt	**258,876**	497,935
Non-current deferred revenue	**11,255**	216,319
Other long-term liabilities	**134,230**	74,227
Total liabilities	**2,268,178**	2,008,892
Commitments and Contingencies (See Note 13)		
Stockholders' equity:		
Preferred stock, $.01 par value, 5,000 shares authorized; no shares issued and outstanding at December 31, 2016 and March 31, 2016		

Common stock, $.01 par value, 200,000 shares authorized; 117,990 and 103,765 shares issued and 100,798 and 86,573 outstanding at December 31, 2016 and March 31, 2016, respectively	**1,180**	1,038
Additional paid-in capital	**1,370,278**	1,088,628
Treasury stock, at cost; 17,192 common shares at December 31, 2016 and March 31, 2016	**(303,388)**	(303,388)
Accumulated deficit	**(198,974)**	(166,997)
Accumulated other comprehensive loss	**(48,175)**	(37,896)
Total stockholders' equity	**820,921**	581,385
Total liabilities and stockholders' equity	**3,089,099**	2,590,277

See accompanying Notes.

Table of Contents

TAKE-TWO INTERACTIVE SOFTWARE, INC.

CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS (Unaudited)

(in thousands, except per share amounts)

	Three Months Ended December 31,		Nine Months Ended December 31,	
	2016	**2015**	**2016**	**2015**
Net revenue	**476,473**	414,221	**1,208,192**	1,036,492
Cost of goods sold	**311,074**	257,861	**708,059**	604,416
Gross profit	**165,399**	156,360	**500,133**	432,076
Selling and marketing	**95,820**	59,846	**247,141**	160,289
General and administrative	**52,939**	49,061	**149,367**	148,057
Research and development	**37,589**	27,944	**101,494**	86,499
Business reorganization		71,172		71,172
Depreciation and amortization	**7,460**	7,534	**22,329**	21,462
Total operating expenses	**193,808**	215,557	**520,331**	487,479
Loss from operations	**(28,409)**	(59,197)	**(20,198)**	(55,403)
Interest and other, net	**(3,715)**	(8,018)	**(15,298)**	(23,948)
Gain on long-term investments, net			**1,350**	
Loss before income taxes	**(32,124)**	(67,215)	**(34,146)**	(79,351)
Benefit from income taxes	**(2,282)**	(24,802)	**(2,169)**	(24,650)
Net loss	**(29,842)**	(42,413)	**(31,977)**	(54,701)
Loss per share:				
Basic and diluted loss per share	**$ (0.33)**	$ (0.51)	**$ (0.37)**	$ (0.66)

See accompanying Notes.

Table of Contents

TAKE-TWO INTERACTIVE SOFTWARE, INC.

CONDENSED CONSOLIDATED STATEMENTS OF COMPREHENSIVE LOSS (Unaudited)

(in thousands)

	Three Months Ended December 31,		Nine Months Ended December 31,	
	2016	**2015**	**2016**	**2015**
Net loss	**$ (29,842)**	$ (42,413)	**$ (31,977)**	$ (54,701)
Other comprehensive loss:				
Foreign currency translation adjustment	**(5,040)**	(5,281)	**(10,067)**	(3,961)
Reclassification to earnings for realized gains on cash flow hedges		(17)		(17)
Change in fair value of effective cash flow hedges		(17)		(17)
Available-for-sale securities:				
Unrealized loss, net on available-for-sale securities, net of taxes	**(264)**	(114)	**(221)**	(159)
Reclassification to earnings for realized gains, net on available for sale securities, net of taxes		26	**9**	26
Change in fair value of available for sale securities	**(264)**	(88)	**(212)**	(133)
Other comprehensive loss	**(5,304)**	(5,386)	**(10,279)**	(4,111)
Comprehensive loss	**$ (35,146)**	$ (47,799)	**$ (42,256)**	$ (58,812)

See accompanying Notes.

Table of Contents

TAKE-TWO INTERACTIVE SOFTWARE, INC.

CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS (Unaudited)

(in thousands)

	Nine Months Ended December 31,	
	2016	**2015**
Operating activities:		
Net loss	**$ (31,977)**	$ (54,701)
Adjustments to reconcile net loss to net cash provided by operating activities:		
Amortization and impairment of software development costs and licenses	**130,019**	83,056
Depreciation and amortization	**22,329**	21,462
Amortization and impairment of intellectual property	**1,398**	160
Stock-based compensation	**55,421**	54,144
Amortization of discount on Convertible Notes	**17,870**	17,454
Amortization of debt issuance costs	**1,078**	1,181
Other, net	**(3,604)**	2,573
Changes in assets and liabilities:		
Restricted cash	**(17,372)**	(34,411)
Accounts receivable	**(160,095)**	(46,227)
Inventory	**(15,876)**	(374)
Software development costs and licenses	**(194,422)**	(170,074)
Prepaid expenses, other current and other non-current assets	**(31,460)**	(6,514)
Deferred revenue	**302,728**	184,955
Deferred cost of goods sold	**(66,502)**	(54,418)
Accounts payable, accrued expenses and other liabilities	**230,067**	190,557
Net cash provided by operating activities	**239,602**	188,823
Investing activities:		
Change in bank time deposits	**66,841**	(189,564)
Proceeds from available-for-sale securities	**101,357**	19,014
Purchases of available-for-sale securities	**(104,357)**	(25,768)
Purchases of fixed assets	**(14,369)**	(28,579)
Proceeds from sale of long-term investment	**1,350**	
Purchase of long-term investments	**(1,885)**	
Business acquisitions, net of cash acquired	**(750)**	
Net cash provided by (used in) investing activities	**48,187**	(224,897)
Financing activities:		
Excess tax benefit from stock-based compensation	**1,499**	1,509
Tax payment related to net share settlements on restricted stock awards	**(36,734)**	(14,506)
Repurchase of common stock		(26,552)
Net cash used in financing activities	**(35,235)**	(39,549)
Effects of foreign currency exchange rates on cash and cash equivalents	**(11,866)**	(256)
Net increase (decrease) in cash and cash equivalents	**240,688**	(75,879)
Cash and cash equivalents, beginning of year	**798,742**	911,120
Cash and cash equivalents, end of period	**$ 1,039,430**	$ 835,241

See accompanying Notes.

Table of Contents

TAKE-TWO INTERACTIVE SOFTWARE, INC.

Notes to Condensed Consolidated Financial Statements (Unaudited)

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

1. BASIS OF PRESENTATION AND SIGNIFICANT ACCOUNTING POLICIES

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

Basis of Presentation

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

Certain information and footnote disclosures normally included in financial statements prepared in accordance with accounting principles generally accepted in the United States have been omitted pursuant to the rules and regulations of the Securities and Exchange Commission, although we believe that the disclosures are adequate to make the information presented not misleading. These Condensed Consolidated Financial Statements and accompanying notes should be read in conjunction with our annual consolidated financial statements and the notes thereto, included in our Annual Report on Form 10-K for the fiscal year ended March 31, 2016.

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

The following is an update to our Significant Accounting Policies disclosed in our Annual Report on Form 10-K for the fiscal year ended March 31, 2016.

Revenue Recognition

Because the service period for our online-enabled games with significant post-contract customer support ("PCS") is not an explicitly defined period, we must make an estimate of the service offering period for purposes of recognizing revenue. As our franchise offerings with significant PCS are relatively new offerings, we have limited historical data to assess end-user game playing patterns. Therefore, the estimated service period for current deferred title offerings is based on our estimate of the economic game life of the respective title. Determining the estimated service period (or economic game life) is inherently subjective and is subject to regular revision based on numerous factors and considerations. The factors that we primarily consider as part of our process of initially determining

Table of Contents

TAKE-TWO INTERACTIVE SOFTWARE, INC.

Notes to Condensed Consolidated Financial Statements (Unaudited) (Continued)

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

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

and subsequently reassessing estimated service periods for our *Grand Theft Auto* and other franchise titles include:

- the period of time over which the substantial majority of a respective title's estimated lifetime game sales and in-game virtual currency sales are expected to occur;
- the period of time over which we plan to provide free unspecified add-on content updates, maintenance or other remaining material online support services associated with our online-enabled games;
- the time over which we plan to dedicate internal resources to support the online functionality of a title;
- known and expected online gameplay trends;
- the results from prior analyses;
- the nature of the game (e.g., annual title, genre, period of time between franchise title releases, etc.); and
- the disclosed service periods for competitors' games.

To the extent we have recorded significant amounts of revenue deferred for specific titles, changes in the estimated service periods could materially impact the revenue recognition reported in a particular period.

During the quarter ended December 31, 2016, we deferred revenues and related cost of goods sold related to *Mafia III*, which released in October 2016, due to specified elements for which we do not have vendor specific objective evidence ("VSOE") of fair value being delivered at a later date.

Recently Issued Accounting Pronouncements

Accounting for Stock Compensation

In March 2016, the Financial Accounting Standards Board ("FASB") issued Accounting Standards Update ("ASU") 2016-09, Compensation Stock Compensation. This new guidance identifies areas for simplification involving several aspects of accounting for share-based payment transactions, including income tax consequences, classification of awards as either equity or liabilities, an option to recognize gross stock compensation expense with actual forfeitures recognized as they occur, as well as certain classifications on the statement of cash flows. This update is effective for annual periods beginning after December 15, 2016 (April 1, 2017 for the Company) and interim periods within those annual periods. Early adoption is permitted in any interim or annual period. We are currently evaluating the impact of adopting this update on our Consolidated Financial Statements.

Accounting for Leases

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

Table of Contents

TAKE-TWO INTERACTIVE SOFTWARE, INC.

Notes to Condensed Consolidated Financial Statements (Unaudited) (Continued)

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

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

statement purposes, the FASB retained a dual model, requiring leases to be classified as either operating or finance. Operating leases will result in straight-line expense (similar to current operating leases) while finance leases will result in a front-loaded expense pattern (similar to current capital leases). Classification will be based on criteria that are largely similar to those applied in current lease accounting. This update is effective for annual periods, and interim periods within those years, beginning after December 15, 2018 (April 1, 2019 for the Company). This new guidance must be adopted using a modified retrospective approach whereby lessees and lessors are required to recognize and measure leases at the beginning of the earliest period presented using a modified retrospective approach. Early adoption is permitted. We are currently evaluating the impact of adopting this update on our Consolidated Financial Statements, which will consist primarily of a balance sheet gross up of our operating leases, mostly for office space.

Revenue from Contracts with Customers

In May 2014, the FASB issued ASU 2014-09, Revenue from Contracts with Customers ("ASU 2014-09"), as a new Topic, Accounting Standards Codification Topic 606. The new revenue recognition standard provides a five-step analysis of transactions to determine when and how revenue is recognized. The core principle is that a company should recognize revenue to depict the transfer of promised goods or services to customers in an amount that reflects the consideration to which the entity expects to be entitled in exchange for those goods or services. In March 2016, the FASB amended ASU 2014-09 by issuing ASU 2016-08, Revenue from Contracts with Customers: Principal versus Agent Considerations (Reporting Revenue Gross versus Net), which clarifies the implementation guidance on principal versus agent considerations included in ASU 2014-09. The guidance includes indicators to assist an entity in determining whether it controls a specified good or service before it is transferred to customers. In April 2016, the FASB amended ASU 2014-09 by issuing ASU 2016-10, Revenue from Contracts with Customers: Identifying Performance Obligations and Licensing, which clarify the implementation guidance on licensing and identifying performance obligations. In May and December 2016, the FASB further amended ASU 2014-09 by issuing ASU 2016-12, Revenue from Contracts with Customers: Narrow-Scope Improvements and Practical Expedients and ASU 2016-20, Technical Corrections and Improvements to Topic 606, Revenue from Contracts with Customers, respectively, which do not change the core principles of the standard, but clarifies the guidance on assessing collectibility, presenting sales taxes, measuring noncash consideration, and certain transition matters. ASU 2014-09 and its amendments can be adopted retrospectively to each period presented or as a cumulative-effect adjustment as of the date of adoption. In July 2015, the FASB voted to defer the effective date by one year to annual and interim years beginning after December 15, 2017 (April 1, 2018 for the Company). Early adoption is permitted, but no earlier than the original effective date of annual and interim periods beginning after December 15, 2016 (April 1, 2017 for the Company). We anticipate this standard may have a material impact on our consolidated financial statements. While we are continuing to assess all potential impacts of the standard, we currently believe the most significant impact relates to our accounting for on-line enabled games that benefit from game related services (previously referred to as post customer support or "PCS".)

Table of Contents

TAKE-TWO INTERACTIVE SOFTWARE, INC.

Notes to Condensed Consolidated Financial Statements (Unaudited) (Continued)

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

2. MANAGEMENT AGREEMENT

In May 2011, we entered into an amended management services agreement, (the "2011 Management Agreement") with ZelnickMedia Corporation ("ZelnickMedia") pursuant to which ZelnickMedia provided us with certain management, consulting and executive level services. In March 2014, we entered into a new management agreement, (the "2014 Management Agreement"), with ZelnickMedia pursuant to which ZelnickMedia continues to provide financial and management consulting services to the Company through March 31, 2019. The 2014 Management Agreement became effective April 1, 2014 and supersedes and replaces the 2011 Management Agreement, except as otherwise contemplated by the 2014 Management Agreement. As part of the 2014 Management Agreement, Strauss Zelnick, the President of ZelnickMedia, continues to serve as Executive Chairman and Chief Executive Officer and Karl Slatoff, a partner of ZelnickMedia, continues to serve as President of the Company. The 2014 Management Agreement provides for an annual management fee of $2,970 over the term of the agreement and a maximum annual bonus opportunity of $4,752 over the term of the agreement, based on the Company achieving certain performance thresholds. In consideration for ZelnickMedia's services, we recorded consulting expense (a component of general and administrative expenses) of $2,440 and $1,931 during the three months ended December 31, 2016 and 2015, respectively, and $5,113 and $5,792 during the nine months ended December 31, 2016 and 2015, respectively. We recorded stock-based compensation expense for non-employee restricted stock units granted to ZelnickMedia, which is included in general and administrative expenses of $7,066 and $8,450 during the three months ended December 31, 2016 and 2015, respectively, and $17,862 and $16,737 during the nine months ended December 31, 2016 and 2015, respectively.

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

	Nine Months Ended December 31,	
	2016	**2015**
Time-based	**107,551**	151,575
Market-based(1)	**199,038**	280,512
Performance-based(1)		
New IP	**33,174**	46,752
Major IP	**33,172**	46,752
Total Performance-based	**66,346**	93,504
Total Restricted Stock Units	**372,935**	525,591

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

Time-based restricted stock units granted in 2016 will vest on April 1, 2018 and those granted in 2015 will vest on April 4, 2017, in each case provided that the 2014 Management Agreement has not been terminated prior to such vesting date.

Market-based restricted stock units granted in 2016 are eligible to vest on April 4, 2018 and those granted in 2015 are eligible to vest on April 4, 2017, in each case provided that the 2014 Management Agreement has not been terminated prior to such vesting date. Market-based restricted stock units are eligible to vest based on the Company's Total Shareholder Return (as defined in the relevant grant

Table of Contents

TAKE-TWO INTERACTIVE SOFTWARE, INC.

Notes to Condensed Consolidated Financial Statements (Unaudited) (Continued)

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

2. MANAGEMENT AGREEMENT (Continued)

agreement) relative to the Total Shareholder Return (as defined in the relevant grant agreement) of the companies that constitute the NASDAQ Composite Index as of the grant date measured over a two-year period. To earn the target number of market-based restricted stock units (which represents 50% of the number of the market-based restricted stock units set forth in the table above), the Company must perform at the 50th percentile, with the maximum number of market-based restricted stock units earned if the Company performs at the 75th percentile. Each reporting period we re-measure the fair value of the unvested shares of market-based restricted stock units granted to ZelnickMedia.

Performance-based restricted stock units granted in 2016 are eligible to vest on April 4, 2018 and those granted in 2015 are eligible to vest on April 4, 2017, in each case provided that the 2014 Management Agreement has not been terminated prior to such vesting date. Performance-based restricted stock units, of which 50% are tied to "New IP" and 50% to "Major IP" (as defined in the relevant grant agreement), are eligible to vest based on the Company's achievement of certain performance metrics (as defined in the relevant grant agreement) of individual product releases of "New IP" or "Major IP" measured over a two-year period. The target number of performance-based restricted stock units that may be earned pursuant to these grants is equal to 50% of the grant amounts set forth in the above table (the numbers in the table represent the maximum number of performance-based restricted stock units that may be earned). Each reporting period we assess the performance metric and upon achievement of certain thresholds record an expense for the unvested portion of the shares of performance-based restricted stock units. Certain performance metrics, based on unit sales, have been achieved as of December 31, 2016 for the "Major IP" performance-based restricted stock units granted in 2016 and 2015.

The unvested portion of time-based, market-based and performance-based restricted stock units held by ZelnickMedia were 898,526 and 1,145,081 as of December 31, 2016 and March 31, 2016, respectively. In addition to the restricted stock units granted to ZelnickMedia, 591,912 restricted stock units vested and 27,578 restricted stock units were forfeited during the nine months ended December 31, 2016.

3. FAIR VALUE MEASUREMENTS

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

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

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

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

Table of Contents

TAKE-TWO INTERACTIVE SOFTWARE, INC.

Notes to Condensed Consolidated Financial Statements (Unaudited) (Continued)

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

3. FAIR VALUE MEASUREMENTS (Continued)

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

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

	December 31, 2016	Quoted prices in active markets for identical assets (level 1)	Significant other observable inputs (level 2)	Significant unobservable inputs (level 3)	Balance Sheet Classification
Money market funds	$ 660,481	$ 660,481	$	$	Cash and cash equivalents
Bank-time deposits	55,630	55,630			Cash and cash equivalents
Corporate bonds	206,655		206,655		Short-term investments
Bank-time deposits	197,868	197,868			Short-term investments
Foreign currency forward contracts	162		162		Prepaid expenses and other
Foreign currency forward contracts	(21)		(21)		Accrued and other current liabilities
Total recurring fair value measurements, net	$ 1,120,775	$ 913,978	$ 206,796	$	

	March 31, 2016	Quoted prices in active markets for identical assets (level 1)	Significant other observable inputs (level 2)	Significant unobservable inputs (level 3)	Balance Sheet Classification
Money market funds	$ 562,726	$ 562,726	$	$	Cash and cash equivalents
Corporate bonds	205,250		205,250		Short-term investments
Bank-time deposits	265,570	265,570			Short-term investments
Foreign currency forward contracts	(137)		(137)		Accrued and other current liabilities
Total recurring fair value measurements, net	$ 1,033,409	$ 828,296	$ 205,113	$	

We did not have any transfers between Level 1 and Level 2 fair value measurements during the nine months ended December 31, 2016.

Debt

As of December 31, 2016, the estimated fair value of our 1.00% Convertible Notes due 2018 (the "1.00% Convertible Notes") was $640,198. The fair value was determined using Level 2 inputs, observable market data, for the 1.00% Convertible Notes and their embedded option feature. See Note 9 for additional information regarding our 1.00% Convertible Notes.

Table of Contents

TAKE-TWO INTERACTIVE SOFTWARE, INC.

Notes to Condensed Consolidated Financial Statements (Unaudited) (Continued)

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

4. SHORT-TERM INVESTMENTS

Our short-term investments consisted of the following:

	December 31, 2016			
	Cost or Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value
Short-term investments				
Bank time deposits	$ 197,868	$	$	$ 197,868
Available-for-sale securities:				
Corporate bonds	206,783	114	(242)	206,655
Total short-term investments	$ 404,651	$ 114	$ (242)	$ 404,523

	March 31, 2016			
	Cost or Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value
Short-term investments				
Bank time deposits	$ 265,570	$	$	$ 265,570
Available-for-sale securities:				
Corporate bonds	205,166	131	(47)	205,250
Total short-term investments	$ 470,736	$ 131	$ (47)	$ 470,820

We consider various factors in the review of investments with an unrealized loss, including 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 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. Based on our review, we did not consider these investments to be other-than-temporarily impaired as of December 31, 2016 or March 31, 2016.

The following table summarizes the contracted maturities of our short-term investments at December 31, 2016:

	December 31, 2016	
	Amortized Cost	Fair Value
Short-term investments		
Due in 1 year or less	$ 357,271	$ 357,292
Due in 1 - 2 years	47,380	47,231
Total short-term investments	$ 404,651	$ 404,523

Table of Contents

TAKE-TWO INTERACTIVE SOFTWARE, INC.

Notes to Condensed Consolidated Financial Statements (Unaudited) (Continued)

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

5. DERIVATIVE INSTRUMENTS AND HEDGING ACTIVITIES

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

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

	December 31, 2016	March 31, 2016
Forward contracts to sell foreign currencies	**$ 116,540**	$ 54,529
Forward contracts to purchase foreign currencies	**2,481**	2,409

For the three months ended December 31, 2016 and 2015, we recorded a gain of $11,158 and $1,230, respectively, and for the nine months ended December 31, 2016 and 2015, we recorded a gain of $11,731 and $908, respectively, related to foreign currency forward contracts in interest and other, net in our Condensed Consolidated Statements of Operations. Our derivative contracts are foreign currency exchange forward contracts that are not designated as hedging instruments under hedge accounting and are used to reduce the impact of foreign currency on certain balance sheet exposures and certain revenue and expense. These instruments are generally short term in nature, with typical maturities of less than one year, and are subject to fluctuations in foreign exchange rates.

6. INVENTORY

Inventory balances by category are as follows:

	December 31, 2016	March 31, 2016
Finished products	**$ 24,424**	$ 14,321
Parts and supplies	**2,241**	1,567
Inventory	**$ 26,665**	$ 15,888

Estimated product returns included in inventory at December 31, 2016 and March 31, 2016 were $2,790 and $527, respectively.

7. SOFTWARE DEVELOPMENT COSTS AND LICENSES

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

	December 31, 2016		March 31, 2016	
	Current	Non-current	Current	Non-current
Software development costs, internally developed	**$ 109,070**	**$ 263,689**	$ 131,378	$ 162,261
Software development costs, externally developed	**14,506**	**63,428**	46,888	45,703
Licenses	**2,609**		121	6,867
Software development costs and licenses	**$ 126,185**	**$ 327,117**	$ 178,387	$ 214,831

Table of Contents

TAKE-TWO INTERACTIVE SOFTWARE, INC.

Notes to Condensed Consolidated Financial Statements (Unaudited) (Continued)

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

7. SOFTWARE DEVELOPMENT COSTS AND LICENSES (Continued)

Software development costs and licenses as of December 31, 2016 and March 31, 2016 included $327,100 and $343,450, respectively, related to titles that have not been released. During the three months ended December 31, 2016 and 2015, we recorded $7,731 and $0, respectively, of software development impairment charges (a component of cost of goods sold). During the nine months ended December 31, 2016 and 2015, we recorded $19,325, and $2,133, respectively, of software development impairment charges (a component of cost of goods sold).

8. ACCRUED EXPENSES AND OTHER CURRENT LIABILITIES

Accrued expenses and other current liabilities consist of the following:

	December 31, 2016	March 31, 2016
Software development royalties	**432,327**	$ 414,492
Compensation and benefits	**68,026**	39,919
Business reorganization	**65,935**	66,323
Marketing and promotions	**63,491**	14,938
Licenses	**48,546**	31,825
Other	**57,851**	39,982
Accrued expenses and other current liabilities	**$ 736,176**	$ 607,479

9. DEBT

Credit Agreement

In April 2016, we entered into a Sixth Amendment to our Second Amended and Restated Credit Agreement (as amended, the "Credit Agreement"). The Credit Agreement provides for borrowings of up to $100,000 which may be increased by up to $100,000 pursuant to the terms of the Credit Agreement and which is secured by substantially all of our assets and the equity of our subsidiaries. The Credit Agreement expires on August 18, 2019. Revolving loans under the Credit Agreement bear interest at our election of (a) 0.25% to 0.75% above a certain base rate (3.75% at December 31, 2016) or (b) 1.25% to 1.75% above the LIBOR Rate (approximately 2.02% at December 31, 2016), with the margin rate subject to the achievement of certain average liquidity levels. We are also required to pay a monthly fee on the unused available balance, ranging from 0.25% to 0.375% based on availability. We had no outstanding borrowings at December 31, 2016 and March 31, 2016.

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

Table of Contents

TAKE-TWO INTERACTIVE SOFTWARE, INC.

Notes to Condensed Consolidated Financial Statements (Unaudited) (Continued)

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

9. DEBT (Continued)

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

	December 31, 2016	March 31, 2016
Available borrowings	**$ 98,336**	$ 98,335
Outstanding letters of credit	**1,664**	1,664

We recorded interest expense and fees related to the Credit Agreement of $111 for the three months ended December 31, 2016 and 2015 and $332 for the nine months ended December 31, 2016 and 2015. The Credit Agreement contains covenants that substantially limit us and our subsidiaries' ability to create, incur, assume or be liable for indebtedness; dispose of assets outside the ordinary course of business; acquire, merge or consolidate with or into another person or entity; create, incur or allow any lien on any of their respective properties; make investments; or pay dividends or make distributions (each subject to certain limitations); or optionally prepay any indebtedness (subject to certain exceptions, including an exception permitting the redemption of our unsecured convertible senior notes upon the meeting of certain minimum liquidity requirements). In addition, the Credit Agreement provides for certain events of default such as nonpayment of principal and interest, breaches of representations and warranties, noncompliance with covenants, acts of insolvency, default on indebtedness held by third parties and default on certain material contracts (subject to certain limitations and cure periods). The Credit Agreement also contains a requirement that we maintain an interest coverage ratio of more than one to one for the trailing twelve-month period, if certain average liquidity levels fall below $30,000.

1.75% Convertible Notes Due 2016

On November 16, 2011, we issued $250,000 aggregate principal amount of 1.75% Convertible Notes due 2016 (the "1.75% Convertible Notes"). The issuance of the 1.75% Convertible Notes included $30,000 related to the exercise of an over-allotment option by the underwriters. Interest on the 1.75% Convertible Notes was payable semi-annually in arrears on June 1st and December 1st of each year, commencing on June 1, 2012. The 1.75% Convertible Notes matured on December 1, 2016, unless earlier repurchased by the Company or converted. We did not have the right to redeem the 1.75% Convertible Notes prior to maturity.

The 1.75% Convertible Notes were convertible at an initial conversion rate of 52.3745 shares of our common stock per $1 principal amount of 1.75% Convertible Notes (representing an initial conversion price of approximately $19.093 per share of common stock for a total of approximately 13,094,000 underlying conversion shares) subject to adjustment in certain circumstances. As of June 1, 2016 until the close of business on the business day immediately preceding the maturity date, holders were eligible to convert their 1.75% Convertible Notes at any time. Prior to September 27, 2016, upon conversion, the 1.75% Convertible Notes were eligible to be settled, at our election, in cash, shares of our common stock, or a combination of cash and shares of our common stock. On September 27, 2016, we elected to settle our conversion obligations in connection with the 1.75% Convertible Notes solely in shares of our common stock and accordingly notified the Trustee. As such, we continued to classify these 1.75% Convertible Notes as long-term debt until their maturity.

Table of Contents

TAKE-TWO INTERACTIVE SOFTWARE, INC.

Notes to Condensed Consolidated Financial Statements (Unaudited) (Continued)

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

9. DEBT (Continued)

Prior to December 1, 2016, holders of the 1.75% Convertible Notes elected to convert such notes, and we settled all such notes during the period by converting them to shares of our common stock using the initial conversion rate. At maturity, the if-converted value exceeded the principal amount of $250,000 by $368,430.

We previously separately accounted for the liability and equity components of the 1.75% Convertible Notes in a manner that reflected our nonconvertible debt borrowing rate when interest expense is recognized in subsequent periods. We estimated the fair value of the 1.75% Convertible Notes to be $197,373, as of the date of issuance of our 1.75% Convertible Notes, assuming a 6.9% non-convertible borrowing rate. The carrying amount of the equity component was determined to be $52,627 by deducting the fair value of the liability component from the par value of the 1.75% Convertible Notes. The excess of the principal amount of the liability component over its carrying amount was amortized to interest and other, net over the term of the 1.75% Convertible Notes using the effective interest method. The equity component was not remeasured as it continued to meet the conditions for equity classification. In accounting for the $6,875 of banking, legal and accounting fees related to the issuance of the 1.75% Convertible Notes, we allocated $5,428 to the liability component and $1,447 to the equity component. Debt issuance costs attributable to the liability component were amortized to interest and other, net over the term of the 1.75% Convertible Notes, and issuance costs attributable to the equity component were netted with the equity component in additional paid-in capital.

The following table provides additional information related to our 1.75% Convertible Notes:

	December 31, 2016	March 31, 2016
Additional paid-in capital	**$**	$ 51,180
Principal amount of 1.75% Convertible Notes	**$**	$ 250,000
Unamortized discount of the liability component		8,014
Carrying amount of debt issuance costs		657
Net carrying amount of 1.75% Convertible Notes	**$**	$ 241,329

The following table provides the components of interest expense related to our 1.75% Convertible Notes:

	Three Months Ended December 31,		Nine Months Ended December 31,	
	2016	2015	2016	2015
Cash interest expense (coupon interest expense)	**$ 711**	$ 1,094	**$ 2,898**	$ 3,281
Non-cash amortization of discount on 1.75% Convertible Notes	**2,038**	2,867	**8,014**	8,458
Amortization of debt issuance costs	**171**	250	**657**	758
Total interest expense related to 1.75% Convertible Notes	**$ 2,920**	$ 4,211	**$ 11,569**	$ 12,497

Table of Contents

TAKE-TWO INTERACTIVE SOFTWARE, INC.

Notes to Condensed Consolidated Financial Statements (Unaudited) (Continued)

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

9. DEBT (Continued)

1.00% Convertible Notes Due 2018

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

The 1.00% Convertible Notes are convertible at an initial conversion rate of 46.4727 shares of our common stock per $1 principal amount of 1.00% Convertible Notes (representing an initial conversion price of approximately $21.52 per share of common stock for a total of approximately 13,361,000 underlying conversion shares) subject to adjustment in certain circumstances. Holders may convert the 1.00% Convertible Notes at their option prior to the close of business on the business day immediately preceding January 1, 2018 only under the following circumstances: (1) during any fiscal quarter commencing after September 30, 2013, if the last reported sale price of the common stock for at least 20 trading days (whether or not consecutive) during a period of 30 consecutive trading days ending on the last trading day of the preceding fiscal quarter is greater than or equal to 130% of the applicable conversion price on each applicable trading day; (2) during the five business day period after any 10 consecutive trading day period (the "measurement period") in which the trading price per $1 principal amount of 1.00% Convertible Notes for each day of that measurement period was less than 98% of the product of the last reported sale price of our common stock and the applicable conversion rate on each such day; or (3) upon the occurrence of specified corporate events. On and after January 1, 2018 until the close of business on the business day immediately preceding the maturity date, holders may convert their 1.00% Convertible Notes at any time, regardless of the foregoing circumstances. Upon conversion, the 1.00% Convertible Notes may be settled, at our election, in cash, shares of our common stock, or a combination of cash and shares of our common stock. Our common stock price exceeded 130% of the applicable conversion price per share for at least 20 trading days during the 30 consecutive trading days ended December 31, 2016. Accordingly, as of January 1, 2017, the 1.00% Convertible Notes may be converted at the holder's option through March 31, 2017. During the three months ended December 31, 2016, 1.00% Convertible Notes with an aggregate principal amount of $8,352 were settled and an additional 1.00% Convertible Notes with an aggregate principal amount of $10 were tendered for conversion, with January 2017 settlement dates. We elected to settle in shares of our common stock, and our intent and ability, given our option, would be to settle future conversions in shares of our common stock. As such, we have continued to classify these 1.00% Convertible Notes as long-term debt.

Upon the occurrence of certain fundamental changes involving the Company, holders of the 1.00% Convertible Notes may require us to purchase all or a portion of their 1.00% Convertible Notes for cash at a price equal to 100% of the principal amount of the notes to be purchased, plus accrued and

Table of Contents

TAKE-TWO INTERACTIVE SOFTWARE, INC.

Notes to Condensed Consolidated Financial Statements (Unaudited) (Continued)

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

9. DEBT (Continued)

unpaid interest (including additional interest, if any) to, but excluding, the fundamental change purchase date.

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

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

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

As of December 31, 2016 and March 31, 2016, the if-converted value of our 1.00% Convertible Notes exceeded the principal amount of $279,148 and $287,500, respectively by $360,284 and $215,809, respectively.

Table of Contents

TAKE-TWO INTERACTIVE SOFTWARE, INC.

Notes to Condensed Consolidated Financial Statements (Unaudited) (Continued)

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

9. DEBT (Continued)

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

	December 31, 2016	March 31, 2016
Additional paid-in capital	**$ 35,784**	$ 35,784
Principal amount of 1.00% Convertible Notes	**$ 279,148**	$ 287,500
Unamortized discount of the liability component	**19,683**	29,972
Carrying amount of debt issuance costs	**589**	922
Net carrying amount of 1.00% Convertible Notes	**$ 258,876**	$ 256,606

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

	Three Months Ended December 31,		Nine Months Ended December 31,	
	2016	2015	2016	2015
Cash interest expense (coupon interest expense)	**$ 698**	$ 719	**$ 2,115**	$ 2,156
Non-cash amortization of discount on 1.00% Convertible Notes	**3,285**	3,043	**10,289**	8,996
Amortization of debt issuance costs	**99**	110	**333**	334
Total interest expense related to 1.00% Convertible Notes	**$ 4,082**	$ 3,872	**$ 12,737**	$ 11,486

10. LOSS PER SHARE ("EPS")

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

	Three Months Ended December 31,		Nine Months Ended December 31,	
	2016	2015	2016	2015
Computation of Basic and Diluted Loss per Share:				
Net loss	**$ (29,842)**	$ (42,413)	**$ (31,977)**	$ (54,701)
Weighted average common shares outstanding basic and diluted	**90,428**	83,426	**86,796**	83,338
Basic and diluted loss per share	**$ (0.33)**	$ (0.51)	**$ (0.37)**	$ (0.66)

We incurred a net loss for the three and nine months ended December 31, 2016 and 2015; therefore, the basic and diluted weighted average shares outstanding exclude the effect of the unvested share-based awards that are considered participating securities and all common stock equivalents because their effect would be antidilutive. For the three and nine months ended December 31, 2016 and 2015, we had 4,912,000 and 7,255,000, respectively, of unvested share-based awards which are excluded from the EPS calculation due to the net loss for those periods.

19

Table of Contents

TAKE-TWO INTERACTIVE SOFTWARE, INC.

Notes to Condensed Consolidated Financial Statements (Unaudited) (Continued)

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

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

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

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

During the nine months ended December 31, 2016, 2,696,000 restricted stock awards vested, and we issued 1,275,000 of unvested restricted stock awards and canceled 72,000 of unvested restricted stock awards.

11. ACCUMULATED OTHER COMPREHENSIVE LOSS

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

	Nine Months Ended December 31, 2016			
	Foreign currency translation adjustments	Unrealized gain (loss) on derivative instruments	Unrealized gain (loss) on available-for-sales securities(1)	Total
Balance at March 31, 2016	$ (38,580)	$ 600	$ 84	$ (37,896)
Other comprehensive loss before reclassifications	(10,067)		(221)	(10,288)
Amounts reclassified from accumulated other comprehensive income (loss)			9	9
Balance at December 31, 2016	$ (48,647)	$ 600	$ (128)	$ (48,175)

(1) Amounts reclassified from Accumulated other comprehensive loss are included in Interest and other, net in our Condensed Consolidated Statement of Operations.

	Nine Months Ended December 31, 2015			
	Foreign currency translation adjustments	Unrealized gain (loss) on derivative instruments	Unrealized gain (loss) on available-for-sales securities	Total
Balance at March 31, 2015	$ (31,216)	$ 617	$ (25)	$ (30,624)
Other comprehensive income (loss) before reclassifications	(3,961)		(159)	(4,120)
Amounts reclassified from accumulated other comprehensive income (loss)		(17)	26	9

Balance at December 31, 2015	$ (35,177)	$ 600	$ (158)	$ (34,735)

Table of Contents

TAKE-TWO INTERACTIVE SOFTWARE, INC.

Notes to Condensed Consolidated Financial Statements (Unaudited) (Continued)

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

12. SEGMENT AND GEOGRAPHIC INFORMATION

We are a publisher of interactive software games designed for console systems and personal computers, including smart phones and tablets, which are delivered through physical retail, digital download, online platforms and cloud streaming services. Our business consists of our Rockstar Games and 2K labels, which represent a single operating segment, the "publishing segment." Our operations involve similar products and customers worldwide. Revenue earned from our publishing segment is primarily derived from the sale of internally developed software titles and software titles developed on our behalf by third-parties. Our operating segment is based upon our internal organizational structure, the manner in which our operations are managed and the criteria used by our Chief Executive Officer, our Chief Operating Decision Maker ("CODM"), to evaluate performance and allocate resources. We are centrally managed and the CODM primarily uses consolidated financial information supplemented by sales information by product category, major product title and platform to make operational decisions and assess financial performance.

We attribute net revenue to geographic regions based on product destination. Net revenue by geographic region was as follows:

	Three Months Ended December 31,		Nine Months Ended December 31,	
Net revenue by geographic region:	**2016**	**2015**	**2016**	**2015**
United States	**$ 257,504**	$ 218,386	**$ 703,088**	$ 546,926
Europe	**143,109**	142,326	**323,924**	362,059
Asia Pacific	**44,365**	28,429	**108,745**	68,913
Canada and Latin America	**31,495**	25,080	**72,435**	58,594
Total net revenue	**$ 476,473**	$ 414,221	**$ 1,208,192**	$ 1,036,492

Net revenue by product platform was as follows:

	Three Months Ended December 31,		Nine Months Ended December 31,	
Net revenue by product platform:	**2016**	**2015**	**2016**	**2015**
Console	**$ 354,220**	$ 355,235	**$ 961,285**	$ 878,838
PC and other	**122,253**	58,986	**246,907**	157,654
Total net revenue	**$ 476,473**	$ 414,221	**$ 1,208,192**	$ 1,036,492

Our products are delivered through physical retail and digital online services (digital download, online platforms and cloud streaming). Net revenue by distribution channel was as follows:

	Three Months Ended December 31,		Nine Months Ended December 31,	
Net revenue by distribution channel:	**2016**	**2015**	**2016**	**2015**
Digital online	**$ 240,213**	$ 146,449	**$ 643,051**	$ 502,860
Physical retail and other	**236,260**	267,772	**565,141**	533,632
Total net revenue	**$ 476,473**	$ 414,221	**$ 1,208,192**	$ 1,036,492

Table of Contents

TAKE-TWO INTERACTIVE SOFTWARE, INC.

Notes to Condensed Consolidated Financial Statements (Unaudited) (Continued)

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

13. COMMITMENTS AND CONTINGENCIES

We have entered into various agreements in the ordinary course of business that require substantial cash commitments over the next several years. Other than agreements entered into in the ordinary course of business and in addition to the agreements requiring known cash commitments as reported in Part II, Item 7 of our Annual Report on Form 10-K for the fiscal year ended March 31, 2016, we did not have any significant changes to our commitments since March 31, 2016.

Legal and Other Proceedings

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

On April 11, 2016, we filed a declaratory judgment action in the United States District Court for the Southern District of New York seeking, among other things, a judicial declaration that Leslie Benzies, the former president of one of our subsidiaries with whom we had been in ongoing discussions regarding his separation of employment, is not entitled to any minimum allocation or financial parity with any other person under the applicable royalty plan. We believe we will prevail in this matter, although there can be no assurance of the outcome. On April 12, 2016, Mr. Benzies filed a complaint in the Supreme Court of the State of New York, New York County against us, and certain of our subsidiaries and employees. We removed this case to the United States District Court for the Southern District of New York, but the case was subsequently remanded to state court. The complaint claims damages of at least $150,000 and contains allegations of breach of fiduciary duty; fraudulent inducement and fraudulent concealment; aiding and abetting breach of fiduciary duty; breach of various contracts; breach of implied duty of good faith and fair dealing; tortious interference with contract; unjust enrichment; reformation; constructive trust; declaration of rights; constructive discharge; defamation and fraud. Motion practice in both the federal and state actions is ongoing. While we believe that we have meritorious defenses to these claims, and we intend to vigorously defend against them and to pursue any counterclaims, we have accrued what we believe to be an adequate amount for this matter, which amounts are classified as Business reorganization within Accrued expenses and other current liabilities in our Condensed Consolidated Balance Sheet (see Note 8). We do not believe that the ultimate outcome of such litigation, even if in excess of our current accrual, will have a material adverse effect on our business, financial condition or results of operations.

14. SUBSEQUENT EVENT

On January 31, 2017, we acquired Social Point, S.L. ("Social Point), a leading mobile game developer, for consideration of $175,000 in cash and the issuance of 1,480,168 shares of Take-Two Common Stock. Certain of the shares that were issued to continuing employees are subject to transferability restrictions and forfeiture provisions requiring their continued employment subject to certain exceptions over the three-year period following the closing. Additional contingent consideration of up to an aggregate of $25,900 may become due based on Social Point achieving certain performance measures over the 12 and 24 month periods following the closing. It is not practicable to disclose the preliminary purchase price allocation or consolidated pro forma information for this transaction given the short period of time between the acquisition date and the issuance of this report.

Table of Contents

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

CAUTIONARY NOTE ABOUT FORWARD-LOOKING STATEMENTS

The statements contained herein which are not historical facts are considered forward-looking statements under federal securities laws and may be identified by words such as "anticipates," "believes," "estimates," "expects," "intends," "plans," "potential," "predicts," "projects," "seeks," "should" "will," or words of similar meaning and include, but are not limited to, statements regarding the outlook for the Company's future business and financial performance. Such forward-looking statements are based on the current beliefs of our management as well as assumptions made by and information currently available to them, which are subject to inherent uncertainties, risks and changes in circumstances that are difficult to predict. Actual outcomes and results may vary materially from these forward-looking statements based on a variety of risks and uncertainties including those contained herein, in the Company's Annual Report on Form 10-K for the fiscal year ended March 31, 2016, in the section entitled "Risk Factors," and the Company's other periodic filings with the Securities and Exchange Commission. All forward-looking statements are qualified by these cautionary statements and speak only as of the date they are made. The Company undertakes no obligation to update any forward-looking statement, whether as a result of new information, future events or otherwise.

Our Management's Discussion and Analysis of Financial Condition and Results of Operations ("MD&A") is provided in addition to the accompanying Condensed Consolidated Financial Statements and notes to assist readers in understanding our results of operations, financial condition and cash flows. The following discussion should be read in conjunction with the MD&A and our annual consolidated financial statements and the notes thereto, included in our Annual Report on Form 10-K for the fiscal year ended March 31, 2016.

Overview

Our Business

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

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

Table of Contents

programs and global distribution on platforms and through channels that are relevant to our target audience.

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

Software titles published by our Rockstar Games label are primarily internally developed. We expect Rockstar Games, our wholly-owned publisher of the *Grand Theft Auto*, *Max Payne*, *Midnight Club*, *Red Dead* and other popular franchises, to continue to be a leader in the action / adventure product category and to create groundbreaking entertainment by leveraging our existing titles as well as by developing new brands. We believe that Rockstar has established a uniquely original, popular cultural phenomenon with its *Grand Theft Auto* series, which is the interactive entertainment industry's most iconic and critically acclaimed brand and has sold-in over 250 million units. The latest installment, *Grand Theft Auto V*, was released on Sony's PS3 and Microsoft's Xbox 360 in September 2013, on Sony's PS4 and Microsoft's Xbox One in November 2014, and on PC in April 2015. *Grand Theft Auto V* includes access to *Grand Theft Auto Online*, which initially launched in October 2013. Rockstar Games is also well known for developing brands in other genres, including the *L.A. Noire*, *Bully* and *Manhunt* franchises. Rockstar Games continues to expand on our established franchises by developing sequels, offering downloadable episodes, content and virtual currency, and releasing titles for smartphones and tablets. In October 2016, Rockstar Games announced that *Red Dead Redemption 2* is in development and planned for worldwide release in Fall 2017 for Sony's PS4 and Microsoft's Xbox One.

Our 2K label has published a variety of popular entertainment properties across all key platforms and across a range of genres including shooter, action, role-playing, strategy, sports and family/casual entertainment. We expect 2K to continue to develop new, successful franchises in the future. 2K's internally owned and developed franchises include the critically acclaimed, multi-million unit selling *BioShock*, *Mafia*, *Sid Meier's Civilization* and *XCOM* series. In May 2016, 2K launched *Battleborn*, a new brand created by Gearbox Software, the makers of *Borderlands*. 2K also publishes externally developed franchises, such as *Borderlands* and *Evolve*. 2K's realistic sports simulation titles include our flagship *NBA 2K* series, which continues to be the top-ranked NBA basketball video game, and the *WWE 2K* professional wrestling series.

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

Trends and Factors Affecting our Business

Product Release Schedule. Our financial results are affected by the timing of our product releases and the commercial success of those titles. Our *Grand Theft Auto* products in particular have historically accounted for a significant portion of our revenue. Sales of *Grand Theft Auto* products generated 38.7% of our net revenue for the nine months ended December 31, 2016. The timing of our *Grand Theft Auto* product releases may affect our financial performance on a quarterly and annual basis.

Economic Environment and Retailer Performance. We continue to monitor economic conditions that may unfavorably affect our businesses, such as deteriorating consumer demand, pricing pressure on

Table of Contents

our products, credit quality of our receivables, and foreign currency exchange rates. Our business is dependent upon a limited number of customers that account for a significant portion of our revenue. Our five largest customers accounted for 65.8% and 65.3% of net revenue during the nine months ended December 31, 2016 and 2015, respectively. As of December 31, 2016 and March 31, 2016, our five largest customers comprised 69.0% and 73.9% of our gross accounts receivable, respectively, with our significant customers (those that individually comprised more than 10% of our gross accounts receivable balance) accounting for 47.9% and 64.1% of such balance at December 31, 2016 and March 31, 2016, respectively. We had two customers who accounted for 33.5% and 14.4% of our gross accounts receivable as of December 31, 2016 and three customers who accounted for 35.2%, 16.8% and 12.1% of our gross accounts receivable as of March 31, 2016. The economic environment has affected our customers in the past, and may do so in the future. Bankruptcies or consolidations of our large retail customers could seriously hurt our business, due to uncollectible accounts receivables and the concentration of purchasing power among the remaining large retailers. Certain of our large customers sell used copies of our games, which may negatively affect our business by reducing demand for new copies of our games. While the downloadable content that we now offer for certain of our titles may serve to reduce used game sales, we expect used game sales to continue to adversely affect our business.

Hardware Platforms. We derive most of our revenue from the sale of products made for video game consoles manufactured by third-parties, such as Sony's PS4 and PS3 and Microsoft's Xbox One and Xbox 360, which comprised 79.6% of our net revenue by product platform for the nine months ended December 31, 2016. The success of our business is dependent upon the consumer acceptance of these consoles and continued growth in their installed base. When new hardware platforms are introduced, demand for software used on older platforms typically declines, which may negatively affect our business during the market transition to the new consoles. We continually monitor console hardware sales. We manage our product delivery on each current and future platform in a manner we believe to be most effective to maximize our revenue opportunities and achieve the desired return on our investments in product development. Accordingly, our strategy is to focus our development efforts on a select number of the highest quality titles for these platforms, while also expanding our offerings for emerging platforms such as tablets, smartphones and online games.

Online Content and Digital Distribution. The interactive entertainment software industry is delivering a growing amount of content through digital online delivery methods. We provide a variety of online delivered products and offerings. Most of our titles that are available through retailers as packaged goods products are also available through direct digital download (from websites we own and others owned by third-parties). In addition, we aim to drive ongoing engagement and incremental revenue from recurrent consumer spending on our titles after their initial purchase through downloadable offerings, including add-on content, microtransactions and online play. We also publish an expanding variety of titles for tablets and smartphones, which are delivered to consumers through digital download via the Internet. Note 12 to our Condensed Consolidated Financial Statements, "Segment and Geographic Information," discloses that net revenue from digital online channels comprised 53.2% of our net revenue by distribution channel for the nine months ended December 31, 2016. We expect online delivery of games and game offerings to continue to grow and to become an increasing part of our business over the long-term.

Table of Contents

Product Releases

We released the following key titles during the nine months ended December 31, 2016.

Title	Publishing Label	Internal or External Development	Platform(s)	Date Released
Battleborn	2K	External	Xbox One, PS4, PC	May 3, 2016
BioShock: The Collection	2K	Internal/External	Xbox One, PS4, PC (digital download only)	September 13, 2016
NBA 2K17	2K	Internal	Xbox 360, Xbox One, PS3, PS4, PC	September 20, 2016
XCOM 2	2K	Internal	Xbox One, PS4	September 27, 2016
Mafia III	2K	Internal	Xbox One, PS4, PC	October 7, 2016
WWE 2K17	2K	Internal/External	Xbox 360, Xbox One, PS3, PS4	October 11, 2016
Sid Meier's Civilization VI	2K	Internal	PC	October 21, 2016

Product Pipeline

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

Title	Publishing Label	Internal or External Development	Platform(s)	Expected Release Date
Red Dead Redemption 2	Rockstar Games	Internal	PS4, Xbox One	Fall 2017
WWE 2K17	2K	Internal/External	PC	February 7, 2017
NBA 2K18	2K	Internal	Xbox One, Xbox 360, PS3, PS4, iOS and Android	Fall 2017

Critical Accounting Policies and Estimates

Our most critical accounting policies, which are those that require significant judgment, include: revenue recognition; price protection and allowances for returns; capitalization and recognition of software development costs and licenses; fair value estimates including inventory obsolescence, and valuation of goodwill, intangible assets and long-lived assets; valuation and recognition of stock-based compensation; and income taxes. In-depth descriptions of these can be found in our Annual Report on Form 10-K for the fiscal year ended March 31, 2016.

The following is an update to our Critical Accounting Policies and Estimates disclosed in our Annual Report on Form 10-K for the fiscal year ended March 31, 2016.

Revenue Recognition

Because the service period for our online-enabled games with significant post-contract customer support ("PCS") is not an explicitly defined period, we must make an estimate of the service offering period for purposes of recognizing revenue. As our franchise offerings with significant PCS are relatively new offerings, we have limited historical data to assess end-user game playing patterns. Therefore, the estimated service period for current deferred title offerings is based on our estimate of the economic game life of the respective title. Determining the estimated service period (or economic game life) is inherently subjective and is subject to regular revision based on numerous factors and considerations. The factors that we primarily consider as part of our process of initially determining

Table of Contents

and subsequently reassessing estimated service periods for our *Grand Theft Auto* and other franchise titles include:

- the period of time over which the substantial majority of a respective title's estimated lifetime game sales and in-game virtual currency sales are expected to occur;
- the period of time over which we plan to provide free unspecified add-on content updates, maintenance or other remaining material online support services associated with our online-enabled games;
- the time over which we plan to dedicate internal resources to support the online functionality of a title;
- known and expected online gameplay trends;
- the results from prior analyses;
- the nature of the game (e.g., annual title, genre, period of time between franchise title releases, etc.); and
- the disclosed service periods for competitors' games.

To the extent we have recorded significant amounts of revenue deferred for specific titles, changes in the estimated service periods could materially impact the revenue recognition reported in a particular period.

Recently Issued Accounting Pronouncements

Accounting for Stock Compensation

In March 2016, the Financial Accounting Standards Board ("FASB") issued Accounting Standards Update ("ASU") 2016-09, Compensation Stock Compensation. This new guidance identifies areas for simplification involving several aspects of accounting for share-based payment transactions, including income tax consequences, classification of awards as either equity or liabilities, an option to recognize gross stock compensation expense with actual forfeitures recognized as they occur, as well as certain classifications on the statement of cash flows. This update is effective for annual periods beginning after December 15, 2016 (April 1, 2017 for the Company) and interim periods within those annual periods. Early adoption is permitted in any interim or annual period. We are currently evaluating the impact of adopting this update on our Consolidated Financial Statements

Accounting for Leases

In February 2016, the FASB issued ASU 2016-02, "Leases." This new guidance requires lessees to recognize a right-of-use asset and a lease liability for virtually all leases (other than leases that meet the definition of a short-term lease). The liability will be equal to the present value of lease payments. The asset will be based on the liability, subject to adjustment, such as for initial direct costs. For income statement purposes, the FASB retained a dual model, requiring leases to be classified as either operating or finance. Operating leases will result in straight-line expense (similar to current operating leases) while finance leases will result in a front-loaded expense pattern (similar to current capital leases). Classification will be based on criteria that are largely similar to those applied in current lease accounting. This update is effective for annual periods, and interim periods within those years, beginning after December 15, 2018 (April 1, 2019 for the Company). This new guidance must be adopted using a modified retrospective approach whereby lessees and lessors are required to recognize and measure leases at the beginning of the earliest period presented using a modified retrospective approach. Early adoption is permitted. We are currently evaluating the impact of adopting this update

Table of Contents

on our Consolidated Financial Statements, which will consist primarily of a balance sheet gross up of our operating leases, mostly for offices space.

Revenue from Contracts with Customers

In May 2014, the FASB issued ASU 2014-09, Revenue from Contracts with Customers ("ASU 2014-09"), as a new Topic, Accounting Standards Codification Topic 606. The new revenue recognition standard provides a five-step analysis of transactions to determine when and how revenue is recognized. The core principle is that a company should recognize revenue to depict the transfer of promised goods or services to customers in an amount that reflects the consideration to which the entity expects to be entitled in exchange for those goods or services. In March 2016, the FASB amended ASU 2014-09 by issuing ASU 2016-08, Revenue from Contracts with Customers: Principal versus Agent Considerations (Reporting Revenue Gross versus Net), which clarifies the implementation guidance on principal versus agent considerations included in ASU 2014-09. The guidance includes indicators to assist an entity in determining whether it controls a specified good or service before it is transferred to customers. In April 2016, the FASB amended ASU 2014-09 by issuing ASU 2016-10, Revenue from Contracts with Customers: Identifying Performance Obligations and Licensing, which clarifies the implementation guidance on licensing and identifying performance obligations. In May 2016, the FASB further amended ASU 2014-09 by issuing ASU 2016-12, Revenue from Contracts with Customers: Narrow-Scope Improvements and Practical Expedients, which does not change the core principles of the standard, but clarifies the guidance on assessing collectibility, presenting sales taxes, measuring noncash consideration, and certain transition matters. In December 2016, the FASB further amended ASU 2014-09 by issuing ASU 2016-20, Technical Corrections and Improvements to Topic 606, Revenue from Contracts with Customers, which does not change the core principles of the standard represent changes to make minor corrections or minor improvements to the Codification that are not expected to have a significant effect on current accounting practice or create a significant administrative cost to most entities. ASU 2014-09 and its amendments can be adopted retrospectively to each period presented or as a cumulative-effect adjustment as of the date of adoption. In July 2015, the FASB voted to defer the effective date by one year to annual and interim years beginning after December 15, 2017 (April 1, 2018 for the Company). Early adoption is permitted, but no earlier than the original effective date of annual and interim periods beginning after December 15, 2016 (April 1, 2017 for the Company). We anticipate this standard may have a material impact on our consolidated financial statements. While we are continuing to assess all potential impacts of the standard, we currently believe the most significant impact relates to our accounting for on-line enabled games that benefit from game related services (previously referred to as post customer support or "PCS".)

Table of Contents

Results of Operations

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

	Three Months Ended December 31,				Nine Months Ended December 31,			
	2016		2015		2016		2015	
Net revenue	$ 476,473	100.0%	$ 414,221	100.0%	$ 1,208,192	100.0%	$ 1,036,492	100.0%
Cost of goods sold	311,074	65.3%	257,861	62.3%	708,059	58.6%	604,416	58.3%
Gross profit	165,399	34.7%	156,360	37.7%	500,133	41.4%	432,076	41.7%
Selling and marketing	95,820	20.1%	59,846	14.5%	247,141	20.5%	160,289	15.4%
General and administrative	52,939	11.1%	49,061	11.8%	149,367	12.4%	148,057	14.3%
Research and development	37,589	7.9%	27,944	6.7%	101,494	8.4%	86,499	8.3%
Depreciation and amortization	7,460	1.6%	7,534	1.8%	22,329	1.8%	21,462	2.1%
Total operating expenses	193,808	40.7%	215,557	52.0%	520,331	43.1%	487,479	47.0%
Loss from operations	(28,409)	(6.0)%	(59,197)	(14.3)%	(20,198)	(1.7)%	(55,403)	(5.3)%
Interest and other, net	(3,715)	(0.8)%	(8,018)	(1.9)%	(15,298)	(1.3)%	(23,948)	(2.3)%
Gain on long-term investments, net		0.0%		0.0%	1,350	0.1%		0.0%
Loss before income taxes	(32,124)	(6.7)%	(67,215)	(16.2)%	(34,146)	(2.8)%	(79,351)	(7.7)%
Benefit from income taxes	(2,282)	(0.5)%	(24,802)	(6.0)%	(2,169)	(0.2)%	(24,650)	(2.4)%
Net loss	$ (29,842)	(6.3)%	$ (42,413)	(10.2)%	$ (31,977)	(2.6)%	$ (54,701)	(5.3)%

	Three Months Ended December 31,				Nine Months Ended December 31,			
	2016		2015		2016		2015	
Net revenue by geographic region:								
United States	$ 257,504	54.0%	$ 218,386	52.7%	$ 703,088	58.2%	$ 546,926	52.8%
International	218,969	46.0%	195,835	47.3%	505,104	41.8%	489,566	47.2%
Net revenue by platform:								
Console	$ 354,220	74.3%	$ 355,235	85.8%	$ 961,285	79.6%	$ 878,838	84.8%
PC and other	122,253	25.7%	58,986	14.2%	246,907	20.4%	157,654	15.2%
Net revenue by distribution channel:								
Digital online	$ 240,213	50.4%	$ 146,449	35.4%	$ 643,051	53.2%	$ 502,860	48.5%
Physical retail and other	236,260	49.6%	267,772	64.6%	565,141	46.8%	533,632	51.5%

Table of Contents

Three Months Ended December 31, 2016 Compared to December 31, 2015

(thousands of dollars)	2016	%	2015	%	Increase/ (decrease)	% Increase/ (decrease)
Net revenue	**$ 476,473**	**100.0%**	$ 414,221	100.0%	$ 62,252	15.0%
Software development costs and royalties(1)	**109,900**	**23.1%**	61,652	14.9%	48,248	78.3%
Internal royalties	**103,613**	**21.7%**	95,311	23.0%	8,302	8.7%
Product costs	**70,089**	**14.7%**	74,935	18.1%	(4,846)	(6.5)%
Licenses	**27,472**	**5.8%**	25,963	6.3%	1,509	5.8%
Cost of goods sold	**311,074**	**65.3%**	257,861	62.3%	53,213	20.6%
Gross profit	**$ 165,399**	**34.7%**	$ 156,360	37.7%	$ 9,039	5.8%

(1) Includes $6,022 and $4,131 of stock-based compensation expense in 2016 and 2015, respectively, in software development costs and royalties.

For the three months ended December 31, 2016, net revenue increased by $62.3 million as compared to the prior year. This increase was due primarily to (i) an aggregate increase of $55.0 million from our *Civilization* franchise due to *Civilization VI*, which released in October 2016; (ii) an increase of $22.7 million from our *NBA 2K* franchise; and (iii) an increase of $7.7 million from *Battleborn,* which released in May 2016. This increase was partially offset by a decrease of $24.9 million in net revenue from *Evolve.*

Net revenue from console games decreased by $1.0 million, and accounted for 74.3% of our total net revenue for the three months ended December 31, 2016, as compared to 85.8% for the same period in the prior year. The decrease in net revenue from console games was due primarily to lower net revenues from *Evolve* partially offset by higher net revenues from our *NBA 2K* franchise. Net revenue from PC and other increased by $63.3 million and accounted for 25.7% of our total net revenue for the three months ended December 31, 2016, as compared to 14.2% for the prior year's period. The increase in net revenue from PC and other was due primarily to higher net revenues from *Civilization VI, Grand Theft Auto V, and Grand Theft Auto Online,* partially offset by lower net revenues from *Evolve*.

Net revenue from digital online channels increased by $93.8 million and accounted for 50.4% of our total net revenue for the three months ended December 31, 2016, as compared to 35.4% for the same period in the prior year. The increase in net revenue from digital online channels was due to higher net revenue from *Civilization VI,* our *NBA 2K* franchise and *Grand Theft Auto V* and *Grand Theft Auto Online*, partially offset by lower net revenues from *Evolve*. Recurrent consumer spending (including add-on content, microtransactions and virtual currency) increased by $34.5 million and accounted for 39.0% of net revenue from digital online channels for the three months ended December 31, 2016, as compared to 40.3% of net revenue from digital online channels for the three months ended December 31, 2015. The increase in recurrent consumer spending was primarily due to higher net revenues from *Grand Theft Auto Online* and our *NBA 2K* franchise partially offset by lower net revenues from *Evolve*. Net revenue from physical retail and other channels decreased by $31.5 million and accounted for 49.6% of our total net revenues for the three months ended December 31, 2016, as compared to 64.6% for the same period in the prior year. The decrease in net revenue from physical retail and other channels was due primarily to lower net revenues from*, Grand Theft Auto V* and *Evolve* partially offset by higher net revenues from *Civilization VI*.

Gross profit as a percentage of net revenue for the three months ended December 31, 2016 was 34.7%, as compared to 37.7% for the prior year period. The decrease was due primarily to higher software development costs and royalties as a percentage of net revenue due to higher amortization

Table of Contents

and impairment of capitalized software costs on our recently released titles and the timing of when internal royalties are earned.

Net revenue earned outside of the United States increased by $23.1 million, and accounted for 46.0% of our total net revenue for the three months ended December 31, 2016, as compared to 47.3% in the prior year. The increase in net revenue outside of the United States was due primarily to net revenues from the release of *Civilization VI* and our *NBA* franchise, which was partially offset by a decrease in net revenues from *Evolve*. Changes in foreign currency exchange rates decreased net revenue by $6.8 million and decreased gross profit by $3.7 million for the three months ended December 31, 2016 as compared to the prior year.

Operating Expenses

(thousands of dollars)	2016	% of net revenue	2015	% of net revenue	Increase/ (decrease)	% Increase/ (decrease)
Selling and marketing	**$ 95,820**	**20.1%**	$ 59,846	14.5%	$ 35,974	60.1%
General and administrative	**52,939**	**11.1%**	49,061	11.8%	3,878	7.9%
Research and development	**37,589**	**7.9%**	27,944	6.7%	9,645	34.5%
Business reorganization		**0.0%**	71,172	17.2%	(71,172)	N/A
Depreciation and amortization	**7,460**	**1.6%**	7,534	1.8%	(74)	(1.0)%
Total operating expenses(1)	**$ 193,808**	**40.7%**	$ 215,557	52.0%	$ (21,749)	(10.1)%

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

	2016	2015
Selling and marketing	**$ 2,441**	$ 2,364
General and administrative	**$ 10,382**	$ 11,761
Research and development	**$ 3,243**	$ 482

Changes in foreign currency exchange rates decreased total operating expenses by $5.0 million for the three months ended December 31, 2016, as compared to the prior year.

Selling and marketing

Selling and marketing expenses increased by $36.0 million for the three months ended December 31, 2016, as compared to the prior year, due primarily to $31.7 million in higher advertising expenses. Advertising expenses were higher in the current year period due primarily to the releases of *Mafia III* and *Civilization VI* in October 2016, and the October 2016 announcement of *Red Dead Redemption 2's* fall 2017 release, as well as the timing of spend.

General and administrative

General and administrative expenses increased by $3.9 million for the three months ended December 31, 2016, as compared to the prior year, due primarily to increases in legal fees and incentive compensation accruals, which were mostly offset by lower expenses associated with severance.

General and administrative expenses for the three months ended December 31, 2016 and 2015 included occupancy expense (primarily rent, utilities and office expenses) of $4.2 million and $3.8 million, respectively, related to our development studios.

Table of Contents

Research and development

Research and development expenses increased by $9.6 million for the three months ended December 31, 2016, as compared to the prior year, due primarily to higher production expenses for new titles in development that have not reached technological feasibility.

Business reorganization

Business reorganization expense decreased by $71.2 million for the three months ended December 31, 2016 as compared to the prior year. During the three months ended December 31, 2015, the Company incurred business reorganization expenses of $71.2 million due primarily to employee separation costs in connection with reorganizing one development studio and closing two development studios.

Depreciation and Amortization

Depreciation and amortization expenses increased by $0.1 million for the three months ended December 31, 2016, as compared to the prior year, due primarily to information technology infrastructure costs.

Interest and other, net

Interest and other, net was an expense of $3.7 million for the three months ended December 31, 2016, as compared to $8.0 million for the three months ended December 31, 2015. The decrease was due primarily to higher foreign exchange transaction gains and higher interest income related to our short-term investments.

Benefit from Income Taxes

The benefit from income taxes was $2.3 million for the three months ended December 31, 2016, as compared to $24.8 million for the three months ended December 31, 2015. The decrease in tax benefit is due to the recognition of a discrete tax benefit of approximately $26.4 million recorded in the same period in the prior year relating to a tax deduction.

Our effective tax rate differed from the federal statutory rate due primarily to changes in valuation allowances related to tax loss and tax credit carryforwards anticipated to be utilized. As disclosed in our Annual Report on Form 10-K for the fiscal year ended March 31, 2016, we recognized an income tax benefit based on becoming eligible to claim certain tax deductions in the UK on applicable video games. It is possible that we will become eligible to claim tax deductions on additional video games in future periods, which could result in tax benefits that could have a material impact on our effective tax rate.

We are regularly audited by domestic and foreign taxing authorities. Audits may result in tax assessments in excess of amounts claimed and the payment of additional taxes. We believe that our tax positions comply with applicable tax law, and that we have adequately provided for reasonably foreseeable tax assessments.

Net loss and loss per share

For the three months ended December 31, 2016, our net loss was $29.8 million, as compared to $42.4 million in the prior year period. For the three months ended December 31, 2016, basic and diluted loss per share was $0.33 as compared to $0.51 in the prior year's period. Basic weighted average shares of 90.4 million were 7.0 million shares higher as compared to the prior year, due primarily to the vesting of restricted stock awards as well as the settlement of our 1.75% Convertible Notes by

Table of Contents

converting those notes to shares of our common stock using the stated conversion rate. See Note 10 to our Condensed Consolidated Financial Statements for additional information regarding loss per share.

Nine Months Ended December 31, 2016 Compared to December 31, 2015

(thousands of dollars)	2016	%	2015	%	Increase/ (decrease)	% Increase/ (decrease)
Net revenue	**$ 1,208,192**	**100.0%**	$ 1,036,492	100.0%	$ 171,700	16.6%
Software development costs and royalties(1)	**218,753**	**18.1%**	152,160	14.7%	66,593	43.8%
Internal royalties	**240,711**	**19.9%**	256,058	24.7%	(15,347)	(6.0)%
Product costs	**170,127**	**14.1%**	153,652	14.8%	16,475	10.7%
Licenses	**78,468**	**6.5%**	42,546	4.1%	35,922	84.4%
Cost of goods sold	**708,059**	**58.6%**	**604,416**	58.3%	103,643	17.1%
Gross profit	**$ 500,133**	**41.4%**	**$ 432,076**	41.7%	$ 68,057	15.8%

(1) Includes $15,974 and $12,935 of stock-based compensation expense in 2016 and 2015, respectively, in software development costs and royalties.

For the nine months ended December 31, 2016, net revenue increased by $171.7 million as compared to the prior year. This increase was due primarily to (i) an increase of $238.2 million in revenues from our *NBA 2K* franchise; (ii) an increase of $60.3 million in net revenues from *Civilization VI,* which released in October 2016; and (iii) an increase of $34.7 million in net revenues from *BioShock: The Collection* which released in September 2016. The increase was partially offset by (i) a decrease of $116.4 million in net revenue from our *Grand Theft Auto* franchise, due primarily to lower net revenues from *Grand Theft Auto V* and (ii) a decrease of $69.0 million in net revenues from *Evolve*.

Net revenue from console games increased by $82.4 million and accounted for 79.6% of our total net revenue for the nine months ended December 31, 2016, as compared to 84.8% for the same period in the prior year. The increase in net revenue from console games was due primarily to higher net revenues from our *NBA 2K* franchise, partially offset by lower net revenues from *Grand Theft Auto V*. Net revenue from PC and other increased by $89.3 million and accounted for 20.4% of our total net revenue for the nine months ended December 31, 2016, as compared to 15.2% for the prior year's period. The increase in net revenue from PC and other was due primarily to higher net revenues from *Civilization VI, Grand Theft Auto V* and *Grand Theft Auto Online*, our *NBA 2K* franchise, *WWE Supercard,* and *XCOM:2,* which released on the PC in February 2016, partially offset by lower net revenues from *Evolve*.

Net revenue from digital online channels increased by $140.2 million and accounted for 53.2% of our total net revenue for the nine months ended December 31, 2016, as compared to 48.5% for the same period in the prior year. The increase in net revenue from digital online channels was due to higher net revenue from *NBA 2K16* and *Civilization VI,* partially offset by lower net revenues from *Evolve*. Recurrent consumer spending (including add-on content, microtransactions and virtual currency) increased by $43.4 million and accounted for 49.8% of net revenue from digital online channels for the nine months ended December 31, 2016, as compared to 55.1% for the nine months ended December 31, 2015. The increase in recurrent consumer spending was primarily due to higher net revenues from our *NBA 2K* franchise . Net revenue from physical retail and other channels increased by $31.5 million and accounted for 46.8% of our total net revenues for the nine months ended December 31, 2016, as compared to 51.5% for the same period in the prior year. The increase

Table of Contents

in net revenue from physical retail and other channels was due primarily to higher net revenues from *NBA 2K*, which was partially offset by lower net revenues from *Grand Theft Auto V*.

Gross profit as a percentage of net revenue for the nine months ended December 31, 2016 was 41.4% as compared to 41.7% for the prior year period. The decrease was due primarily to higher internal royalties as a percentage of net revenues due to having a larger release schedule when compared to the prior year and due to the timing of when internal royalties are earned.

Net revenue earned outside of the United States increased by $15.5 million and accounted for 41.8% of our total net revenue for the nine months ended December 31, 2016, as compared to 47.2% in the prior year. The increase in net revenue was due primarily to an increase in net revenues from *NBA 2K* and *Civilization VI* outside of the United States, which was partially offset by lower net revenues from our *Grand Theft Auto* franchise. Changes in foreign currency exchange rates decreased net revenue by $10.0 million and increased gross profit by $0.3 million for the nine months ended December 31, 2016 as compared to the prior year.

Operating Expenses

(thousands of dollars)	2016	% of net revenue	2015	% of net revenue	Increase/ (decrease)	% Increase/ (decrease)
Selling and marketing	**$ 247,141**	**20.5%**	$ 160,289	15.4%	$ 86,852	54.2%
General and administrative	**149,367**	**12.4%**	148,057	14.3%	1,310	0.9%
Research and development	**101,494**	**8.4%**	86,499	8.3%	14,995	17.3%
Business reorganization		**0.0%**	71,172	6.9%	(71,172)	N/A
Depreciation and amortization	**22,329**	**1.8%**	21,462	2.1%	867	4.0%
Total operating expenses(1)	**$ 520,331**	**43.1%**	$ 487,479	47.0%	$ 32,852	6.7%

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

	2016	2015
Selling and marketing	**$ 7,269**	$ 6,859
General and administrative	**$ 26,861**	$ 31,324
Research and development	**$ 5,317**	$ 3,026

Changes in foreign currency exchange rates decreased total operating expenses by $9.3 million for the nine months ended December 31, 2016 as compared to the prior year.

Selling and marketing

Selling and marketing expenses increased by $86.9 million for the nine months ended December 31 2016, as compared to the prior year, due primarily to $83.4 million in higher advertising expenses. Advertising expenses were higher in the current year period due primarily to the recent release of *Mafia III* in October 2016, the releases of *Battleborn* in May 2016, *Civilization VI* in October 2016 and *BioShock: The Collection* in September 2016. These were slightly offset by a decrease in advertising expense for *Grand Theft Auto V* and *Grand Theft Auto Online.*

General and administrative

General and administrative expenses increased by $1.3 million for the nine months ended December 31, 2016, as compared to the prior year, due primarily to an increase in expenses associated with unclaimed property and higher allowances for bad debt. Partially offsetting this increase were lower expenses associated with severance related to the closing of two of our studios during the prior year.

34

Table of Contents

General and administrative expenses for the nine months ended December 31, 2016 and 2015 included occupancy expense (primarily rent, utilities and office expenses) of $11.8 million and $12.9 million, respectively, related to our development studios.

Research and development

Research and development expenses increased by $15.0 million for the nine months ended December 31, 2016 as compared to the prior year due to higher production expenses for new titles in development that have not reached technological feasibility, which were slightly offset by lower IT expenses.

Business reorganization

Business reorganization expense decreased by $71.2 million for the nine months ended December 31, 2016 as compared to the prior year. During the nine months ended December 31, 2015, the Company incurred business reorganization expenses of $71.2 million due primarily to employee separation costs in connection with reorganizing one development studio and closing two development studios.

Depreciation and Amortization

Depreciation and amortization expenses increased by $0.9 million for the nine months ended December 31, 2016, as compared to the prior year, due primarily to higher purchases of fixed assets for studios and information technology infrastructure build-outs.

Interest and other, net

Interest and other, net was an expense of $15.3 million for the nine months ended December 31, 2016, as compared to $23.9 million for the nine months ended December 31, 2015. The decrease was due primarily to higher foreign exchange transaction gains and higher interest income related to our short-term investments.

Benefit from Income Taxes

The benefit from income taxes was $2.2 million for the nine months ended December 31, 2016, as compared to $24.7 million for the nine months ended December 31, 2015. The decrease in tax benefit is due to the recognition of a discrete tax benefit of approximately $26.4 million recorded in the same period in the prior year relating to a tax deduction.

Our effective tax rate differed from the federal statutory rate due primarily to changes in valuation allowances related to tax loss and tax credit carryforwards anticipated to be utilized. As disclosed in our Annual Report on Form 10-K for the fiscal year ended March 31, 2016, we recognized an income tax benefit based on becoming eligible to claim certain tax deductions in the UK on applicable video games. It is possible that we will become eligible to claim tax deductions in the UK on additional video games in future periods, which could result in tax benefits that could have a material impact on our effective tax rate.

We are regularly audited by domestic and foreign taxing authorities. Audits may result in tax assessments in excess of amounts claimed and the payment of additional taxes. We believe that our tax positions comply with applicable tax law, and that we have adequately provided for reasonably foreseeable tax assessments.

Table of Contents

Net loss and loss per share

For the nine months ended December 31, 2016, our net loss was $32.0 million as compared to $54.7 million in the prior year's period. For the nine months ended December 31, 2016, basic and diluted loss per share was $0.37 as compared to $0.66 in the prior year's period. Basic and diluted weighted average shares of 86.8 million were 3.5 million shares higher as compared to the prior year, due primarily to the vesting of restricted stock awards as well as the settlement of our 1.75% Convertible Notes by converting those notes to shares of our common stock using the stated conversion rate. See Note 10 to our Condensed Consolidated Financial Statements for additional information regarding loss per share.

Liquidity and Capital Resources

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

Short-term Investments

As of December 31, 2016, we had $404.5 million of short-term investments, which are highly liquid in nature and represent an investment of cash that is available for current operations. From time to time, we may purchase additional short-term investments depending on future market conditions and liquidity needs.

Credit Agreement

In April 2016, we entered into a Sixth Amendment to our Second Amended and Restated Credit Agreement (as amended, the "Credit Agreement"). The Credit Agreement provides for borrowings of up to $100.0 million which may be increased by up to $100.0 million pursuant to the terms of the Credit Agreement, and is secured by substantially all of our assets and the equity of our subsidiaries. The Credit Agreement expires on August 18, 2019. Revolving loans under the Credit Agreement bear interest at our election of (a) 0.25% to 0.75% above a certain base rate (3.75% at December 31, 2016), or (b) 1.25% to 1.75% above the LIBOR Rate (approximately 2.02% at December 31, 2016), with the margin rate subject to the achievement of certain average liquidity levels. We are also required to pay a monthly fee on the unused available balance, ranging from 0.25% to 0.375% based on availability.

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

As of December 31, 2016, there was $98.3 million available to borrow under the Credit Agreement and we had $1.7 million of letters of credit outstanding. At December 31, 2016, we had no outstanding borrowings under the Credit Agreement.

The Credit Agreement contains covenants that substantially limit us and our subsidiaries' ability to: create, incur, assume or be liable for indebtedness; dispose of assets outside the ordinary course of business; acquire, merge or consolidate with or into another person or entity; create, incur or allow any lien on any of their respective properties; make investments; or pay dividends or make distributions (each subject to certain limitations); or optionally prepay any indebtedness (subject to certain exceptions, including an exception permitting the redemption of our unsecured convertible senior notes upon the meeting of certain minimum liquidity requirements). In addition, the Credit Agreement

Table of Contents

provides for certain events of default such as nonpayment of principal and interest, breaches of representations and warranties, noncompliance with covenants, acts of insolvency, default on indebtedness held by third parties and default on certain material contracts (subject to certain limitations and cure periods). The Credit Agreement also contains a requirement that we maintain an interest coverage ratio of more than one to one for the trailing twelve-month period, if certain average liquidity levels fall below $30.0 million.

1.75% Convertible Notes Due 2016

On November 16, 2011, we issued $250.0 million aggregate principal amount of 1.75% Convertible Notes due 2016 (the "1.75% Convertible Notes"). Interest on the 1.75% Convertible Notes was payable semi-annually in arrears on June 1st and December 1st of each year, commencing on June 1, 2012. The 1.75% Convertible Notes matured on December 1, 2016, unless earlier repurchased by us or converted. We did not have the right to redeem the 1.75% Convertible Notes prior to maturity.

The 1.75% Convertible Notes were convertible at an initial conversion rate of 52.3745 shares of our common stock per $1,000 principal amount of 1.75% Convertible Notes (representing an initial conversion price of approximately $19.093 per share of common stock for a total of approximately 13,094,000 underlying conversion shares) subject to adjustment in certain circumstances. As of June 1, 2016 until the close of business on the business day immediately preceding the maturity date, holders could have converted their 1.75% Convertible Notes at any time. Prior to September 27, 2016, upon conversion, the 1.75% Convertible Notes were eligible to be settled, at our election, in cash, shares of our common stock, or a combination of cash and shares of our common stock. On September 27, 2016, we elected to settle our conversion obligations in connection with the 1.75% Convertible Notes solely in shares of our common stock and accordingly notified the Trustee. As such, we continued to classify these 1.75% Convertible Notes as long-term debt until their maturity on December 1, 2016.

Prior to December 1, 2016, holders 1.75% Convertible Notes elected to convert such notes, and we settled all such notes during the period by converting them to shares of our common stock using the initial conversion rate.

1.00% Convertible Notes Due 2018

On June 18, 2013, we issued $250.0 million aggregate principal amount of 1.00% Convertible Notes due 2018 (the "1.00% Convertible Notes" and together with the 1.75% Convertible Notes, the "Convertible Notes"). The 1.00% Convertible Notes were issued at 98.5% of par value for proceeds of $246.3 million. Interest on the 1.00% Convertible Notes is payable semi-annually in arrears on July 1st and January 1st of each year, commencing on January 1, 2014. The 1.00% Convertible Notes mature on July 1, 2018, unless earlier repurchased by us or converted. We do not have the right to redeem the 1.00% Convertible Notes prior to maturity. We also granted the underwriters a 30-day option to purchase up to an additional $37.5 million principal amount of 1.00% Convertible Notes to cover overallotments, if any. On July 17, 2013, we closed our public offering of $37.5 million principal amount of our 1.00% Convertible Notes as a result of the underwriters exercising their overallotment option in full on July 12, 2013, bringing the proceeds to $283.2 million.

The 1.00% Convertible Notes are convertible at an initial conversion rate of 46.4727 shares of our common stock per $1,000 principal amount of 1.00% Convertible Notes (representing an initial conversion price of approximately $21.52 per share of common stock for a total of approximately 13,361,000 underlying conversion shares) subject to adjustment in certain circumstances. Holders may convert the 1.00% Convertible Notes at their option prior to the close of business on the business day immediately preceding January 1, 2018 only under the following circumstances: (1) during any fiscal quarter commencing after September 30, 2013, if the last reported sale price of the common stock for at least 20 trading days (whether or not consecutive) during a period of 30 consecutive trading days

Table of Contents

ending on the last trading day of the preceding fiscal quarter is greater than or equal to 130% of the applicable conversion price on each applicable trading day; (2) during the five business day period after any 10 consecutive trading day period (the "measurement period") in which the trading price per $1,000 principal amount of 1.00% Convertible Notes for each day of that measurement period was less than 98% of the product of the last reported sale price of our common stock and the applicable conversion rate on each such day; or (3) upon the occurrence of specified corporate events. On and after January 1, 2018 until the close of business on the business day immediately preceding the maturity date, holders may convert their 1.00% Convertible Notes at any time, regardless of the foregoing circumstances. Upon conversion, the 1.00% Convertible Notes may be settled, at our election, in cash, shares of our common stock, or a combination of cash and shares of our common stock. Our common stock price exceeded 130% of the applicable conversion price per share for at least 20 trading days during the 30 consecutive trading days ended December 31, 2016. Accordingly, as of January 1, 2017 the 1.00% Convertible Notes may be converted at the holder's option through March 31, 2017. During the three months ended December 31, 2016, 1.00% Convertible Notes with an aggregate principal amount of $8.4 million were converted and settled in shares of our common stock, and our intent and ability, given our option, would be to settle future conversions in shares of our common stock. As such, we have continued to classify these 1.00% Convertible Notes as long-term debt.

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

Financial Condition

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

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

A majority of our trade receivables are derived from sales to major retailers and distributors. Our five largest customers accounted for 65.8% and 65.3% of net revenue during the nine months ended December 31, 2016 and 2015, respectively. As of December 31, 2016 and March 31, 2016, five customers accounted for 69.0% and 73.9% of our gross accounts receivable, respectively. Customers that individually accounted for more than 10% of our gross accounts receivable balance comprised 47.9% and 64.1% of such balances at December 31, 2016 and March 31, 2016, respectively. We had two customers who accounted for 33.5% and 14.4% of our gross accounts receivable as of December 31, 2016 and three customers who accounted for 35.2%, 16.8% and 12.1% of our gross accounts receivable as of March 31, 2016. Based upon performing ongoing credit evaluations, maintaining trade credit insurance on a majority of our customers and our past collection experience, we believe that the receivable balances from these largest customers do not represent a significant credit risk, although we actively monitor each customer's credit worthiness and economic conditions that may affect our customers' business and access to capital. We are monitoring the current global economic conditions, including credit markets and other factors as it relates to our customers in order to manage the risk of uncollectible accounts receivable.

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

Table of Contents

As of December 31, 2016, the amount of cash and cash equivalents held outside of the U.S. by our foreign subsidiaries was $358.3 million. These balances are dispersed across various locations around the world. We believe that such dispersion meets the business and liquidity needs of our foreign affiliates. In addition, we expect in the foreseeable future to have the ability to generate sufficient cash domestically to support ongoing operations. Consequently, it is our intention to indefinitely reinvest undistributed earnings of its foreign subsidiaries. In the event we needed to repatriate funds outside of the U.S., such repatriation may be subject to local laws and tax consequences including foreign withholding taxes or U.S. income taxes. It is not practicable to estimate the tax liability and we would try to minimize the tax effect to the extent possible. However, any repatriation may not result in significant cash payments as the taxable event would likely be offset by the utilization of the then available tax credits.

Our Board of Directors has authorized the repurchase of up to 14,217,683 shares of our common stock. We did not repurchase any shares under this program during the nine months ended December 31, 2016. As of December 31, 2016, we have repurchased a total of 5,171,330 shares of our common stock and have remaining availability of 9,046,353 shares under our share repurchase authorization. We are authorized to purchase shares from time to time through a variety of methods, including in the open market or through privately negotiated transactions, in accordance with applicable securities laws. Repurchases are subject to the availability of stock, prevailing market conditions, the trading price of the stock, our financial performance and other conditions. The program may be suspended or discontinued at any time for any reason.

Our changes in cash flows were as follows:

	Nine Months Ended December 31,	
(thousands of dollars)	**2016**	**2015**
Net cash provided by operating activities	**$ 239,602**	$ 188,823
Net cash provided by (used in) investing activities	**48,187**	(224,897)
Net cash used in financing activities	**(35,235)**	(39,549)
Effects of foreign currency exchange rates on cash and cash equivalents	**(11,866)**	(256)
Net increase (decrease) in cash and cash equivalents	**$ 240,688**	$ (75,879)

At December 31, 2016, we had $1,039.4 million of cash and cash equivalents, compared to $798.7 million at March 31, 2016. The increase in cash and cash equivalents was due primarily to cash provided by operating and investing activities offset by cash used in financing activities. Net cash provided by operations was due primarily to cash generated from sales of *NBA 2K17, Grand Theft Auto V*, Mafia III, *WWE 2K17* and virtual currency, partially offset by investments in software development and licenses, and the funding of internal royalty payments. Net cash used in financing activities was primarily related to net share settlements of our stock-based awards. These decreases to cash and cash equivalents were partially offset by net cash provided by investing activities due primarily to the maturity of bank time deposits.

Contractual Obligations and Commitments

We have entered into various agreements in the ordinary course of business that require substantial cash commitments over the next several years. Other than agreements entered into in the ordinary course of business and in addition to the agreements requiring known cash commitments as reported in Part II, Item 7 of our Annual Report on Form 10-K for the fiscal year ended March 31, 2016, we did not have any significant changes to our commitments since March 31, 2016.

Table of Contents

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

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

Off-Balance Sheet Arrangements

As of December 31, 2016 and March 31, 2016, we did not have any material relationships with unconsolidated entities or financial parties, such as entities often referred to as structured finance or variable interest entities, which would have been established for the purpose of facilitating off-balance sheet arrangements or other contractually narrow or limited purposes. As such, we are not exposed to any financing, liquidity, market or credit risk that could arise if we had engaged in such relationships.

International Operations

Net revenue earned outside of the United States is principally generated by our operations in Europe, Asia, Australia, Canada and Latin America. For the three months ended December 31, 2016 and 2015, 46.0% and 47.3%, respectively, and for the nine months ended December 31, 2016 and 2015, 41.8% and 47.2%, respectively, of our net revenue was earned outside of the United States. We are subject to risks inherent in foreign trade, including increased credit risks, tariffs and duties, fluctuations in foreign currency exchange rates, shipping delays and international political, regulatory and economic developments, all of which can have a significant effect on our operating results.

Fluctuations in Quarterly Operating Results and Seasonality

We have experienced fluctuations in quarterly and annual operating results as a result of the timing of the introduction of new titles; variations in sales of titles developed for particular platforms; market acceptance of our titles; development and promotional expenses relating to the introduction of new titles; sequels or enhancements of existing titles; projected and actual changes in platforms; the timing and success of title introductions by our competitors; product returns; changes in pricing policies by us and our competitors; the accuracy of retailers' forecasts of consumer demand; the size and timing of acquisitions; the timing of orders from major customers; and order cancellations and delays in product shipment. Sales of our products are also seasonal, with peak shipments typically occurring in the fourth calendar quarter as a result of increased demand for products during the holiday season. For

Table of Contents

certain of our software products with multiple element revenue arrangements where we do not have VSOE for each element and the deliverables are deemed more-than-inconsequential, we defer the recognition of our net revenues over an estimated service period which generally ranges from 12 to 36 months. As a result, the quarter in which we generate the highest net sales volume may be different from the quarter in which we recognize the highest amount of net revenues. Quarterly comparisons of operating results are not necessarily indicative of future operating results.

Item 3. Quantitative and Qualitative Disclosures About Market Risk

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

Interest Rate Risk

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

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

As of December 31, 2016, we had $404.5 million of short-term investments which included $206.7 million of available-for-sale securities. The available-for-sale securities were recorded at fair market value with unrealized gains or losses resulting from changes in fair value reported as a separate component of accumulated other comprehensive income (loss), net of tax, in stockholders' equity. We also had $1,039.4 million of cash and cash equivalents that are comprised primarily of money market funds and bank-time deposits. We determined that, based on the composition of our investment portfolio, there was no material interest rate risk exposure to our Consolidated Financial Statements or liquidity as of December 31, 2016.

Historically, fluctuations in interest rates have not had a significant effect on our operating results. Under our Credit Agreement, outstanding balances bear interest at our election of (a) 0.25% to 0.75% above a certain base rate (3.75% at December 31, 2016), or (b) 1.25% to 1.75% above the LIBOR rate (approximately 2.02% at December 31, 2016), with the margin rate subject to the achievement of certain average liquidity levels. Changes in market rates may affect our future interest expense if there is an outstanding balance on our line of credit. At December 31, 2016, there were no outstanding borrowings under our Credit Agreement. The 1.00% Convertible Notes pay interest semi-annually at a fixed rate of 1.00per annum, and we expect that there will be no fluctuation related to the 1.00% Convertible Notes affecting our cash component of interest expense. For additional details on our Convertible Notes see Note 9 to our Condensed Consolidated Financial Statements.

Foreign Currency Exchange Rate Risk

We transact business in foreign currencies and are exposed to risks resulting from fluctuations in foreign currency exchange rates. Accounts relating to foreign operations are translated into United States dollars using prevailing exchange rates at the relevant period end. Translation adjustments are included as a separate component of stockholders' equity. For the nine months ended December 31, 2016 and 2015, our foreign currency translation adjustment was a loss of $10.0 million and $4.0 million, respectively. For the three months ended December 31, 2016 and 2015, we recognized a foreign

Table of Contents

currency exchange transaction gain of $1.1 million and a foreign currency exchange transaction loss of $0.7 million respectively, and for the nine months ended December 31, 2016 and 2015, we recognized a foreign currency exchange transaction gain of $3.6 million and a foreign currency exchange transaction loss of $1.8 million respectively, included in interest and other, net in our Condensed Consolidated Statements of Operations.

Balance Sheet Hedging Activities

We use foreign currency forward contracts to mitigate foreign currency exchange rate risk associated with non-functional currency denominated cash balances and inter-company funding loans, non-functional currency denominated accounts receivable and non-functional currency denominated accounts payable. These transactions are not designated as hedging instruments and are accounted for as derivatives whereby the fair value of the contracts is reported as either assets or liabilities on our Condensed Consolidated Balance Sheets, and gains and losses resulting from changes in the fair value are reported in interest and other, net, in our Condensed Consolidated Statements of Operations. We do not enter into derivative financial contracts for speculative or trading purposes. At December 31, 2016, we had $116.5 million of forward contracts outstanding to sell foreign currencies in exchange for U.S. dollars and $2.5 million of forward contracts outstanding to buy foreign currencies in exchange for U.S. dollars, all of which have maturities of less than one year. At March 31, 2016, we had $54.5 million of forward contracts outstanding to sell foreign currencies in exchange for U.S. dollars and $2.4 million of forward contracts outstanding to buy foreign currencies in exchange for U.S. dollars, all of which have maturities of less than one year. For the three months ended December 31, 2016 and 2015, we recorded a gain of $11.2 million and $1.2 million, respectively, and for the nine months ended December 31, 2016 and 2015, we recorded a gain of $11.7 million and of $0.9 million, respectively, related to foreign currency forward contracts in interest and other, net on our Condensed Consolidated Statements of Operations. As of December 31, 2016 the fair value of these contracts was immaterial and as of March 31, 2016 the fair value of these outstanding forward contracts was $0.1 million and was included in accrued and other current liabilities. The fair value of these outstanding forward contracts is estimated based on the prevailing exchange rates of the various hedged currencies as of the end of the period.

Our hedging programs are designed to reduce, but do not entirely eliminate, the effect of currency exchange rate movements. We believe the counterparties to these foreign currency forward contracts are creditworthy multinational commercial banks and that the risk of counterparty nonperformance is not material. Notwithstanding our efforts to mitigate some foreign currency exchange rate risks, there can be no assurance that our hedging activities will adequately protect us against the risks associated with foreign currency fluctuations. For the nine months ended December 31, 2016, 41.8% of our revenue was generated outside the United States. Using sensitivity analysis, a hypothetical 10% increase in the value of the U.S. dollar against all currencies would decrease revenues by 4.2%, while a hypothetical 10% decrease in the value of the U.S. dollar against all currencies would increase revenues by 4.2%. In the opinion of management, a substantial portion of this fluctuation would be offset by cost of goods sold and operating expenses incurred in local currency.

Item 4. Controls and Procedures

Evaluation of Disclosure Controls and Procedures

Based on an evaluation under the supervision and with the participation of management, our principal executive officer and principal financial officer have concluded that our disclosure controls and procedures as defined in rules 13a-15(e) and 15d-15(e) under the Securities Exchange Act of 1934, as amended ("Exchange Act") were effective as of the end of the period covered by this report to ensure that information required to be disclosed by us in reports that we file or submit under the Exchange Act is (i) recorded, processed, summarized and reported within the time periods specified in

Table of Contents

the Securities and Exchange Commission rules and forms and (ii) accumulated and communicated to our management, including our principal executive officer and principal financial officer, as appropriate to allow timely decisions regarding required disclosure.

Changes in Internal Control Over Financial Reporting

There were no changes in our internal control over financial reporting during the quarter ended December 31, 2016, which were identified in connection with management's evaluation required by paragraph (d) of Rules 13a-15 and 15d-15 under the Exchange Act, that have materially affected, or are reasonably likely to materially affect, our internal control over financial reporting.

Table of Contents

PART II. OTHER INFORMATION

Item 1. Legal Proceedings

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

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

Item 1A. Risk Factors

There have been no material changes to the Risk Factors disclosed in Item 1A of our Annual Report on Form 10-K for the fiscal year ended March 31, 2016.

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

Issuer Purchases of Equity Securities

Share Repurchase Program In January 2013, our Board of Directors authorized the repurchase of up to 7,500,000 shares of our common stock. On May 13, 2015, our Board of Directors approved an increase of 6,717,683 shares to our share repurchase program, increasing the total number of shares that we are permitted to repurchase to 14,217,683 shares of our common stock. The authorizations permit us to purchase shares from time to time through a variety of methods, including in the open market or through privately negotiated transactions, in accordance with applicable securities laws. Repurchases are subject to the availability of stock, prevailing market conditions, the trading price of the stock, our financial performance and other conditions. The program may be suspended or discontinued at any time for any reason. As of December 31, 2016, we have repurchased a total of 5,171,330 shares of our common stock under this program and 9,046,353 shares of common stock remain available for repurchase under the Company's share repurchase program. We did not repurchase any shares of our common stock under this program during the nine months ended

Table of Contents

December 31, 2016. The table below details the share repurchases that were made by us during the three months ended December 31, 2016:

Period	Shares purchased(1)	Average price per share	Total number of shares purchased as part of publicly announced plans or programs	Maximum number of shares that may yet be purchased under the repurchase program
October 1 - 31, 2016		$		9,046,353
November 1 - 30, 2016	1,047	$ 48.30		9,046,353
December 1 - 31, 2016		$		9,046,353

(1) All of the shares purchased during this period were purchased in connection with our obligation to holders of restricted stock awards to withhold the number of shares required to satisfy the holders' tax liabilities in connection with the vesting of such shares. None of the shares repurchased during the three months ended December 31, 2016 were part of the publicly announced share repurchase program.

Item 6. Exhibits

Exhibits:

10.1 Lease Agreement, dated as of December 12, 2016, by and between Take-Two Interactive Software, Inc. and DOLP 1133 Properties II LLC for a premises with entrances at 1133 Avenue of the Americas and 110 West 44th Street, New York, New York 10036

10.2 Amendment No. 4 to the Xbox One Publisher License Agreement, by and between Microsoft Corporation and Take-Two Interactive Software, Inc.*

10.3 Amendment to Amended and Restated Restricted Unit Agreement Pursuant to the Take-Two Interactive Software, Inc. 2009 Incentive Stock Plan, dated as of February 7, 2017.

10.4 Share Sale and Purchase Agreement, dated January 31, 2017, by and among Take-Two Interactive Software, Inc., Take-Two Invest Espana, S.L., Andres Bou Ortiz, Horacio Martos Borja, Marc Canaleta Caupena, Voladuras Hinojo, S.L., Nauta Tech Invest III, S.C.R., S.A., Bilbao Vizcaya Holding, S.A., La Banque Postale Innovation 11 FCPI, Capital Croissance 4, Objectif Innovation Patrimoine 4 FCPI, Strategie PME 2011 FCPI, Idinvest Patrimoine FCPI, Allianz Eco Innovation 3 FCPI, Objectif Innovation 5 FCPI, Idinvest Crossance FCPI, SG Innovation 2011 FCPI, Allianz Eco Innovation 2 FCPI, Objectif Innovation 4 FCPI, Idinvest Flexible 2016 FCPI, Capital Croissance 5 FCPI, Objectif Innovation Patrimoine 5 FCPI, Idinvest Patrimoine 2 FCPI, Objectif Innovation Patrimoine 6 FCPI, Idinvest Patrimoine 3 FCPI, Greylock Israel Investment Vehicle in Social Point, LTD, and HCPESP, S.a.r.l. (incorporated by reference to the Company's Current Report on Form 8-K filed with the Securities and Exchange Commission on February 3, 2017)

Table of Contents

Exhibits:

10.5	Registration Rights Agreement, dated January 31, 2017, by and among Take-Two Interactive Software, Inc, Andres Bou Ortiz, Horacio Martos Borja, Marc Canaleta Caupena, Voladuras Hinojo, S.L., Nauta Tech Invest III, S.C.R., S.A., Bilbao Vizcaya Holding, S.A., La Banque Postale Innovation 11 FCPI, Capital Croissance 4, Objectif Innovation Patrimoine 4 FCPI, Strategie PME 2011 FCPI, Idinvest Patrimoine FCPI, Allianz Eco Innovation 3 FCPI, Objectif Innovation 5 FCPI, Idinvest Crossance FCPI, SG Innovation 2011 FCPI, Allianz Eco Innovation 2 FCPI, Objectif Innovation 4 FCPI, Idinvest Flexible 2016 FCPI, Capital Croissance 5 FCPI, Objectif Innovation Patrimoine 5 FCPI, Idinvest Patrimoine 2 FCPI, Objectif Innovation Patrimoine 6 FCPI, Idinvest Patrimoine 3 FCPI, Greylock Israel Investment Vehicle in Social Point, LTD, and HCPESP, S.a.r.l. (incorporated by reference to the Company's Current Report on Form 8-K filed with the Securities and Exchange Commission on February 3, 2017).
31.1	Chief Executive Officer Certification Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.
31.2	Chief Financial Officer Certification Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.
32.1	Chief Executive Officer Certification pursuant to 18 U.S.C. Section 1350, as adopted Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.
32.2	Chief Financial Officer Certification pursuant to 18 U.S.C. Section 1350, as adopted Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.
101.INS	XBRL Instance Document.
101.SCH	XBRL Taxonomy Extension Schema Document.
101.CAL	XBRL Taxonomy Calculation Linkbase Document.
101.LAB	XBRL Taxonomy Label Linkbase Document.
101.PRE	XBRL Taxonomy Presentation Linkbase Document.
101.DEF	XBRL Taxonomy Extension Definition Document.

*

Portions hereof have been omitted and filed separately with the Securities and Exchange Commission pursuant to a request for confidential treatment in accordance with Exchange Act Rule 24b-2.

Attached as Exhibit 101 to this report are the following formatted in XBRL (Extensible Business Reporting Language): (i) Condensed Consolidated Balance Sheets at December 31, 2016 and March 31, 2016, (ii) Condensed Consolidated Statements of Operations for the three and nine months ended December 31, 2016 and 2015, (iii) Condensed Consolidated Statements of Comprehensive Income (Loss) for the three and nine months ended December 31, 2016 and 2015, (iv) Condensed Consolidated Statements of Cash Flows for the nine months ended December 31, 2016 and 2015; and (v) Notes to Condensed Consolidated Financial Statements (Unaudited).

Table of Contents

SIGNATURES

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

TAKE-TWO INTERACTIVE SOFTWARE, INC.
(Registrant)

Date: February 7, 2017 By: /s/ STRAUSS ZELNICK

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

Date: February 7, 2017 By: /s/ LAINIE GOLDSTEIN

Lainie Goldstein
Chief Financial Officer
(Principal Financial Officer)