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TAKE TWO INTERACTIVE SOFTWARE INC
Form 10-K/A
February 28, 2002

SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

FORM 10-K/A

Annual Report Pursuant to Section 13 or 15(d) of the Securities
Exchange Act of 1934 for the fiscal year ended October 31, 2001

OR

Transition Report Pursuant to Section 13 or 15(d) of the Securities
Exchange Act of 1934

0-29230
(Commission File No.)

TAKE-TWO INTERACTIVE SOFTWARE, INC.
(Exact name of Issuer as specified in its charter)

Delaware
(State or other jurisdiction
of incorporation)

51-0350842
(I.R.S. Employer
Identification No.)

575 Broadway, New York, New York 10012
(Address of principal executive offices including zip code)

Registrant's telephone number, including area code: (212) 334-6633

Securities registered pursuant to Section 12(b) of the Act: None

Securities registered pursuant to Section 12(g) of the Act:

Common Stock, \$.01 par value

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

Indicate by check mark if disclosure of delinquent filers pursuant to Item 405
of Regulation S-K is not contained herein, and will not be contained, to the
best of the Registrant's knowledge, in definitive proxy or information
statements in Part III of this Form 10-K or any amendment to this Form 10-K.

The aggregate market value of the Registrant's common stock held by
non-affiliates as of January 22, 2002 was approximately \$668,160,000. As of
January 22, 2002, there were 36,807,713 shares of the Registrant's common stock
outstanding.

Documents Incorporated by Reference:

None

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We are filing an amendment to this Report to include Part III information and information relating to a revision to the results of operations for the interim quarters of fiscal 2001 to reflect a mathematical miscalculation made in the course of the restatement discussed below, which had no effect on full fiscal 2001 results. See Part III and Note 20 of Notes to Consolidated Financial Statements.

PART I

Item 1. Business.

On December 17, 2001, Take-Two Interactive Software, Inc. announced its intention to restate its financial statements for the fiscal year ended October 31, 2000 and the interim quarters of fiscal 2001. All financial data in this Report reflects the effects of this restatement for fiscal 2000, each of the quarters in such year and the interim quarters of fiscal 2001. See Item 7. Management's Discussion and Analysis of Financial Condition and Results of Operations for details regarding the restatement, Item 3. Legal Proceedings for a discussion of a related investigation and Notes 2 and 20 of Notes to Consolidated Financial Statements.

General

We develop, publish and distribute interactive software games worldwide. Our software operates on personal computers and video game consoles manufactured by Sony, Nintendo and Microsoft. We develop software internally and engage third parties to develop games on our behalf. We publish our products under our Rockstar Games, Gathering of Developers, Talonsoft and Take-Two labels. We were ranked number three by NPDFunworld among all video game publishers in North America for 2001.

Our Rockstar Games subsidiary recently released Grand Theft Auto 3 for Sony's PlayStation(R)2. According to NPDFunworld, Grand Theft Auto 3 was ranked the number one selling video game across all platforms in North America for 2001. We also recently released Max Payne for Microsoft's Xbox and Sony's PlayStation(R)2, and we have a strong line-up of additional PlayStation 2 titles, including State of Emergency and a sequel to the popular Midnight Club. Our Gathering of Developers subsidiary also expects to bring several PC games to market, such as the highly anticipated Duke Nukem Forever.

Our Jack of All Games domestic distribution subsidiary sells our software as well as third-party software, hardware and accessories to retail outlets in the United States. Our customers in the United States include Wal-Mart, Gamestop, Best Buy, Circuit City, Electronics Boutique, Toys "R" Us and Blockbuster, as well as other leading national and regional drug store, supermarket and discount store chains and specialty retailers.

We also have sales, marketing and publishing operations in the United Kingdom, France, Germany, Austria, Denmark, Italy, Australia, Canada and Japan.

The Industry

A large and growing installed base of video game consoles and advanced PCs combined with expanding gameplayer demographics have driven demand for interactive entertainment software in recent years. The Interactive Digital

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Software Association (IDSA) estimates that 60% of all Americans, or approximately 145 million people, play video games on a regular basis. According to Euromonitor, worldwide sales of consoles, console games and games for the PC grew from \$17 billion in 1996 to \$27 billion in 2000.

Demand for interactive entertainment software is expected to increase due to the increased penetration of PC and console platforms, the increased installed base of next-generation platforms and broadening consumer demographics. The International Data Corporation (IDC) estimates that approximately 53% of all households in the United States will own a PC by 2002. According to IDC, the household penetration rate for video game consoles today is approximately 46%, and is expected to increase.

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Historically, the interactive entertainment software industry has experienced rapid and sustained periods of growth coinciding with the release of successive generations of game console platforms. The industry has recently transitioned to next-generation platforms, which began with the release of Sony's PlayStation 2 in 2000 and continued with the recent release of Nintendo's Game Boy Advance, Microsoft's Xbox and Nintendo's GameCube in 2001. Demand for these new platforms is expected to be significant due to their ability to offer one or more of the following features:

- o More powerful and realistic graphics and game play through 128-bit technology;
- o Backwards compatibility (the ability to play the platforms' previous generation of games); and
- o Broad entertainment capabilities, including Internet access and the ability to watch DVD movies and play compact discs.

Interactive entertainment software has increasingly become a mainstream entertainment choice for a maturing, technologically sophisticated audience. According to IDSA, 58% of Americans who play video games are over the age of 18, of which 43% are female. Additional catalysts for growth include mass market penetration of budget titles and the emergence of non-traditional retail channels such as drug stores and supermarkets.

Software Products

We publish titles with potential for broad consumer appeal. We plan to deliver game content for both PC and console markets, particularly for next-generation platforms with potential for significant market penetration, including the following titles:

Title	Platform	Genre	Description
State of Emergency	PS2	Action	Fight for freedom
Duke Nukem Forever	PC, Xbox, GBA	First-person shooter	The return of vid hero.

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Mafia	PC, Xbox	Third-person role playing	Chicago. The 1930 American underworld
Serious Sam: Second Encounter	PC, GameCube, GBA	First person shooter	Sequel to the Game
Austin Powers	GBA, PS2	Third-person action/adventure/comedy	The international yeah!
Age of Wonder 2	PC	Strategy	Sequel to the pop
Hidden & Dangerous 2	PC, PS2	Military	Tactics and intense behind-enemy-line
Midnight Club 2	PS2	Urban racing	Sequel to the hit
Grand Theft Auto 3	PC	Action	The global mega h
Smuggler's Run 2	GameCube	Adventure Racing	The off-road fran
MTV's Celebrity Deathmatch	PS2	Fighting	MTV's smash hit g
Austin Powers Pin Ball	PS	Arcade	Adventure with ev superstar.
Spec Ops: Airborne division	PS	Action	The number one mi
Family Feud	GameCube	Game Show	The popular game

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Arrangements with Major Platform Manufacturers

We have entered into license agreements with Sony, Nintendo and Microsoft to develop and publish software for the PlayStation, PlayStation 2, Nintendo 64, Color Gameboy, Gameboy Advance, Nintendo GameCube and Xbox in North America and Europe. We are not required to obtain any licenses to develop titles for the PC.

We entered into a Licensed Publisher Agreement with Sony Computer Entertainment America, Inc. in May 2000. Under the agreement, Sony granted us the right and license to develop, market, publish and distribute software titles for the PlayStation 2 in North America. The agreement requires us to submit products to Sony for its approval. The agreement provides for Sony to be the exclusive manufacturer of our products for the PlayStation 2 and for us to pay royalties to Sony based on the number of units manufactured.

The agreement with Sony expires in March 2003 and is automatically renewable for successive one-year terms, unless terminated by Sony in the event of a breach by us or our bankruptcy or insolvency. Sony may also terminate the agreement on a title-by-title basis. Upon expiration or termination of all of our publishing agreements with Sony (including those discussed below), we have certain rights to sell off existing inventories. We also entered into a similar three-year agreement with Sony in March 2000 for PlayStation 2 covering European

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territories.

We entered into a four-year Licensed Publisher Agreement with Sony in March 1999 under which Sony granted us the right and license to develop, market, publish and distribute software titles for the PlayStation in North America. We also entered into a similar agreement with Sony for Playstation in February 1999 covering European territories.

We entered into a Publisher License Agreement with Microsoft in December 2000. Under the agreement, Microsoft granted us the right and license to develop, market, publish and distribute software titles for Microsoft's Xbox in territories to be determined on a title-by-title basis. The agreement requires us to submit products to Microsoft for its approval and for us to make royalty payments to Microsoft based on the number of units manufactured. Products for the Xbox must be manufactured by pre-approved manufacturers. The agreement may be terminated by either party in the event of a material breach. Microsoft may also terminate the agreement on a title-by-title basis. Upon expiration or termination of the agreement, we have certain rights to sell-off existing inventories.

We entered into a three-year Confidential License Agreement with Nintendo in November 2001. Under the agreement, Nintendo granted us the right and license to develop, market, publish and distribute software for Nintendo's GameCube in the western hemisphere. The agreement requires us to submit products to Nintendo for its approval. The agreement also provides for Nintendo to be the exclusive manufacturer of our products and for us to make royalty payments to Nintendo based on the number of units manufactured. The agreement may be terminated by either party in the event of a breach and may be terminated by Nintendo in the event of our bankruptcy. Upon termination of all of our agreements with Nintendo (including those discussed below), we have certain rights to sell off existing inventories. We also entered into a similar three-year agreement with Nintendo in November 2001 for GameCube covering European territories.

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We entered into a three-year agreement with Nintendo in July 2001, granting us the right and license to develop software for Nintendo's GameBoy Advance in the Western Hemisphere. In October 2001, we entered into a similar three-year agreement with Nintendo for European territories. In addition, in March 1999 we entered into an agreement with Nintendo granting us the right and license to develop software for the Nintendo GameBoy, GameBoy Color and GameBoy Pocket handheld game systems. In February 1998, we entered into agreements with Nintendo granting us the right and license to develop software for Nintendo 64 in the United States and Europe.

Software Development and Licensing

We develop software titles through our internal development studios, Talonsoft, Rockstar Canada, DMA Design Limited, the developer of Grand Theft Auto 3, and PopTop Software, the developer of Railroad Tycoon 2 and Tropico. We also maintain a development studio focusing on games for the Nintendo GameBoy Color platform in the United Kingdom under the name Tarantula, as well as a recently acquired development studio in Austria under the name Neo. As of October 31, 2001, our internal development studios and product development department employed 214 personnel with the technical capabilities to develop and localize (translate into foreign languages) software titles for all major game platforms and territories.

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For the years ended October 31, 2001, 2000 and 1999, we incurred costs of \$6,190,000, \$5,668,000 and \$5,263,000 on research and development relating to our software titles. Additionally, for the years ended October 31, 2001, 2000 and 1999, we capitalized software development costs of \$6,490,000, \$8,837,000 and \$1,901,000.

Many of our software titles are developed by third parties. As a result of our acquisition of Gathering of Developers in fiscal 2000, we have established relationships with software developers, including Apogee Software a/k/a 3D Realms, the creator of the Duke Nukem' franchise, Ritual Entertainment, Terminal Reality, Epic MegaGames and Remedy Entertainment. We have entered into agreements with certain of these developers, as well as other developers such as Angel Studios and Illusions Software, to develop software products on our behalf.

Agreements with developers generally give us exclusive publishing and marketing rights and require us to make advance royalty payments, pay royalties based on product sales and satisfy other conditions. Royalty advances for software titles are recoupable only against royalties otherwise due to developers. Our agreements with developers generally provide us with the right to monitor development efforts and to cease making advance payments if specified development milestones are not satisfied. We monitor the level of advances in light of expected sales for the related titles and write off unrecoverable advances to cost of sales in the period in which we determine the advance will not be fully recouped.

In May 1998, we entered into an agreement with Apogee Software to develop two games based on the Max Payne character. The agreement grants us the exclusive worldwide right to publish Max Payne and a sequel on PC platforms. The agreement requires us to pay royalties and satisfy other conditions and grants Apogee approval rights with respect to products under development. The agreement may be terminated by either party in the event of a material breach or default.

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In July 2001, we entered into a letter agreement with Apogee granting us the exclusive right to develop and publish Max Payne for video game console platforms. The agreement requires us to make recoupable royalty advances and pay royalties to Apogee. We internally developed and released Max Payne for Microsoft's Xbox and Sony's PlayStation 2 in December 2001.

We actively seek to acquire licenses for well-recognized properties. In December 2000, we acquired the exclusive worldwide publishing rights to the best-selling franchise of Duke Nukem' PC and video games, including the back catalog rights to six products, as well as PC, console and sequel rights to Duke Nukem' Forever, the sequel to the popular Duke Nukem' 3D developed by Apogee Software.

We also acquired the exclusive worldwide rights from New Line Productions to publish and distribute titles based on Austin Powers movies, the exclusive rights from MTV to develop titles based on MTV's properties and certain rights from Microsoft, including all of the rights to Oni and Myth and the right to develop two products utilizing the Halo game engine. Among our titles, we own all right, title and interest to all of the intellectual properties associated with the Grand Theft Auto product franchise, and we develop Grand Theft Auto products internally. We expect to launch another major addition to the Grand Theft Auto franchise in 2002.

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In 2000, we pursued an Internet strategy, which included our entry into online gaming markets through the acquisition of assets consisting of broadband, multiplayer and other online gaming technologies. We were unable to successfully implement this strategy, and we sold or wrote off certain of these assets. We are currently focusing on potential multiplayer opportunities for our publishing content.

Sales and Marketing

We sell software titles to retail outlets in the United States and Europe through direct relationships with large retail customers and third-party distributors. Our customers in the United States include Wal-Mart, Gamestop, BestBuy, Circuit City, Electronics Boutique, Toys "R" Us and Blockbuster as well as other leading mass merchandisers; video, electronic and toy stores; national and regional drug stores; supermarket and discount store chains; and specialty retailers. Our European customers include Dixons, Electronics Boutique and Karstadt. We have sales and marketing operations in the United Kingdom, France, Germany, Austria, Denmark, Italy, Australia, Canada and Japan.

Our marketing and promotional efforts are intended to maximize exposure and broaden distribution of our titles, promote brand name recognition, assist retailers and properly position, package and merchandise our titles. We market titles by implementing aggressive public relations campaigns, primarily using print and on-line advertising and to a lesser extent television and radio spots.

Our Rockstar Games subsidiary actively pursues relationships with participants in the music and entertainment industries. We believe that the shared demographics between various media and some of the software titles marketed by Rockstar Games provide excellent cross-promotional opportunities. We have been working with popular recording artists to create sophisticated game soundtracks, have entered into agreements to license high-profile names and likenesses, and have arrangements for co-branding opportunities. Our goal is to accelerate the acceptance of our titles, create brand awareness and develop a greater number of franchise titles.

We also employ various other marketing methods designed to promote consumer awareness, including in-store promotions and point-of-purchase displays, direct mail, cooperative advertising, as well as attendance at trade shows. As of October 31, 2001, we had a sales and marketing staff of 150 persons.

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Distribution

We distribute our own titles, as well as third-party titles and hardware through our subsidiaries. We distribute three major categories of third-party console products, consisting principally of hardware; newly released and popular software titles; and budget and catalog software titles. We seek to maintain a balance among these product categories in order to maximize sales and operating performance.

For the year ended October 31, 2001, the sale of third-party products accounted for approximately 46.1% of our total revenues, with sales to our five largest customers aggregating approximately 20.9% of our total revenues. No single customer accounted for more than 10% of our total revenues during this period.

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We procure products from suppliers using standard purchase orders based on our assessment of market demand, as well as pre-orders from retailers. We generally do not have any long-term agreements with our suppliers, and carry inventory quantities that we believe are necessary to provide rapid response time to retailer orders. We utilize electronic data interchange, or EDI, with many of our retailers to enhance the efficiency of placing and shipping orders.

Jack of All Games maintains warehouse facilities and sales offices in Ohio, Illinois and New York. Products arrive at our warehouses where products are picked, packed and shipped to customers. We generally ship products by common carrier.

Manufacturing

Sony and Nintendo are the sole manufacturers of software products sold for use on their respective hardware platforms. We begin the manufacturing process for our published titles by placing a purchase order for the manufacture of our products with Sony or Nintendo and opening either a letter of credit in favor of the manufacturer or utilizing our line of credit with the manufacturer. We then send software code and a prototype of the product to the manufacturer, together with related artwork, user instructions, warranty information, brochures and packaging designs for approval, defect testing and manufacture. Games manufactured by Sony and Nintendo are generally shipped within two weeks of receipt of our manufacturing order. Games for the Xbox must be manufactured by pre-approved manufacturers.

Production of PC software includes CD-ROM pressing, assembly of components, printing of packaging and user manuals and shipping of finished goods, which is performed by third-party vendors in accordance with our specifications. We believe that there are alternative sources for these services that could be implemented without delay. We send software code and a prototype of a title, together with related artwork, user instructions, warranty information, brochures and packaging designs to manufacturers. Games are generally shipped within two weeks of receipt of our manufacturing order.

To date, we have not experienced any material difficulties or delays in the manufacture of our titles or material delays due to manufacturing defects. Our software titles carry a 90-day limited warranty.

Competition

In our publishing business, we compete both for licenses to properties and the sale of interactive entertainment software with Sony, Nintendo, Microsoft and Sega, each of which is a large developer and marketer of software for its platforms. Sony and Nintendo currently dominate the industry and have the financial resources to withstand significant price competition and to implement extensive advertising campaigns, particularly for prime-time television spots. These companies may also increase their own software development efforts or focus on developing software products for third-party platforms.

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We also compete with domestic companies such as Electronic Arts, Activision, Acclaim Entertainment, THQ, Midway Games and international companies such as Sega, Vivendi, Ubisoft, Infogrames, Eidos, Capcom, Konami and Namco. In addition, we believe that large software companies and media companies are

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increasing their focus on the interactive entertainment software market. Certain of our competitors are developing on-line interactive games and interactive networks that may compete with our products for consumer dollars. Many of our competitors have far greater financial, technical, personnel and other resources than we do, and many are able to carry larger inventories, adopt more aggressive pricing policies and make higher offers to licensors and developers for commercially desirable properties than we can.

Retailers have limited shelf space and promotional resources, and competition is intense among an increasing number of newly introduced entertainment software titles and hardware for adequate levels of shelf space and promotional support. Competition for retail shelf space is expected to increase, which may require us to increase our marketing expenditures just to maintain current levels of sales of our titles. Competitors with more extensive lines and popular titles frequently have greater bargaining power with retailers. Accordingly, we may not be able to achieve the levels of support and shelf space that such competitors receive. Similarly, as competition for popular properties increases, our cost of acquiring licenses for such properties is likely to increase, possibly resulting in reduced margins. Prolonged price competition, increased licensing costs or reduced operating margins would cause our profits to decrease significantly.

Competition for our titles is influenced by the timing of competitive product releases and the similarity of such products to our titles and may result in loss of shelf space or a reduction in sell-through of our titles at retail stores. Our titles also compete with other forms of entertainment such as motion pictures, television and audio and video products featuring similar themes, on-line computer programs and other forms of entertainment which may be less expensive or provide other advantages to consumers.

In our distribution business, we compete with large national companies such as Ingram Entertainment, as well as smaller regional distributors. We also compete with the efforts of the major entertainment software companies that distribute directly to retailers or over the Internet. Some of our competitors have far greater financial, technical, personnel and other resources than we do, and many are able to carry larger inventories, adopt more aggressive pricing policies and provide more comprehensive product selection than we can.

Intellectual Property

We develop proprietary software titles and have obtained the rights to publish and distribute software titles developed by third parties. We attempt to protect our software and production techniques under copyright, trademark and trade secret laws as well as through contractual restrictions on disclosure, copying and distribution. Although we generally do not hold any patents or registered copyrights, we seek to obtain trademark registrations for our product names.

Interactive entertainment software is susceptible to unauthorized copying. Unauthorized third parties may be able to copy or to reverse engineer our titles to obtain and use programming or production techniques that we regard as proprietary. In addition, our competitors could independently develop technologies substantially equivalent or superior to our technologies.

As the amount of interactive entertainment software in the market increases and the functionality of this software further overlaps, we believe

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that interactive entertainment software will increasingly become the subject of claims that such software infringes the copyrights or patents of others. From time to time, we receive notices from third parties alleging infringement of their proprietary rights. Although we believe that our titles and the titles and technologies of third-party developers and publishers with whom we have contractual relationships do not and will not infringe or violate proprietary rights of others, it is possible that infringement of proprietary rights of others may occur. Any claims of infringement, with or without merit, could be time-consuming, costly and difficult to defend.

Employees

As of December 31, 2001, we had 662 full-time employees. None of our employees are subject to a collective bargaining agreement. We consider our relations with employees to be good.

Item 2. Properties.

Executive Offices

Our principal executive offices are located at 575 Broadway, New York, New York in approximately 13,300 square feet of space under a five-year lease with 575 Broadway Corporation, a company controlled by the father of Ryan A. Brant, our Chairman. The lease provides for an annual rent of approximately \$474,000 and expires in 2004. We believe that the terms of the lease are no less favorable than could have been obtained from an unaffiliated third-party.

International Operations

Take-Two Interactive Software Europe Limited leases 12,500 square feet of office space in Windsor, United Kingdom. The lease provides for a current annual rent of approximately \$400,000, plus taxes and utilities, and expires in 2011. Take-Two Interactive Software Europe Limited also leases office space in Lincoln, United Kingdom. The lease provides for a current annual rent of approximately \$17,000 and expires in 2007.

Subsidiaries of Take-Two Interactive Software Europe Limited lease office space at locations in Paris, France, Munich, Germany and Tokyo, Japan for current aggregate annual rent of approximately \$173,000. Directsoft leases office and warehouse space in Hornsby, Australia at an annual rent of approximately \$48,000. Joytech Europe Limited leases office space in Leighton Buzzard Beds, United Kingdom at an annual rent of approximately \$85,000. Funsoft Nordic A.S. and its subsidiaries lease office and warehouse space at locations in Oslo, Norway, Spanga, Sweden and Arthus, Denmark for current aggregate annual rent of approximately \$45,000. DMA Design Limited currently leases office space in Dundee and Edinburgh, Scotland, at an annual rental of approximately \$400,000. CD Verte Italia Spa currently leases office and warehouse space in Golarata, Italy at an annual rent of approximately \$79,000.

Development Facilities

Rockstar Canada leases approximately 3,600 square feet of space in Ontario, Canada at an annual rental of approximately \$26,000 plus taxes and insurance. Talonsoft leases approximately 10,800 square feet of office space in Baltimore, Maryland. Talonsoft currently pays \$162,000 per annum under the lease. PopTop Software leases approximately 3,300 square feet of office space in Fenton, Missouri and pays an annual rental of \$37,000. Neo leases approximately 3,000 square feet of office space in Vienna, Austria.

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North America Distribution Facilities

Jack of All Games leases approximately 13,000 square feet of office and warehouse space in College Point, New York. The lease provides for annual rent of \$237,000, plus increases in real estate taxes, and expires in October 2006. Jack of All Games also leases approximately 206,000 square feet of office and warehouse space in Cincinnati, Ohio. Jack of All Games pays \$750,000 per annum, plus taxes and insurance, under the lease, which expires in January 2006. Jack of All Games Canada, Inc. (formerly Triad Distributors) currently leases approximately 36,750 square feet of office and warehouse space in Ontario, Canada at an annual rate of approximately \$219,000 plus operating costs, under a lease that expires September 2004. VLM Entertainment Group leases approximately 3,000 square feet of space in Northbrook, Illinois at an annual rental of \$33,000. VLM also leases approximately 56,200 square feet of office and warehouse space in Ottawa, Illinois at an annual rent of \$288,000. VLM leases such space from its former stockholders and believes that the terms of the lease are no less favorable than could have been obtained from an unaffiliated third-party.

Item 3. Legal Proceedings.

In December 2001 and January 2002, six purported class action lawsuits were filed in the United States District Court for the Southern District of New York by Peter Fischbein; Drimal Ltd.; Corado Petruzzelli; Michael Lucas; Israel M. Zacks; and Eliot Gertsen against Take-Two Interactive Software, Inc. and certain of its officers or directors asserting damages on behalf of all persons or entities who purchased or otherwise acquired Take-Two common stock in the open market during the period commencing on February 24, 2000 through December 17, 2001. These complaints allege violations of Section 10 (b) of the Securities Exchange Act of 1934 and Rule 10b-5 promulgated thereunder by Take-Two and the individual defendants and violations of Section 20 (a) of the Exchange Act by the individual defendants.

In the foregoing complaints, the plaintiffs allege that, among other things, because Take-Two's financial statements issued during the class period were not prepared in conformity with generally accepted accounting principles, the defendants concealed adverse material information and made or participated in the making of untrue statements of material facts and omitted to state material facts concerning the business, financial condition, operations and future prospects of Take-Two. The plaintiffs, in each of the complaints, seek compensatory damages, including interest, against all of the defendants, recovery of their reasonable litigation costs, and expenses. Take-Two intends to defend vigorously the claims against it. Although we cannot predict the ultimate outcome of these actions, an unfavorable resolution could have a material adverse effect on our financial condition, cash flows and results of operations.

In connection with an informal and voluntary request from the SEC to provide documents, we engaged the law firm of Blank Rome Tenzer Greenblatt LLP, as counsel, to conduct an investigation into our accounting treatment of certain transactions in fiscal 2000 and 2001. Blank Rome retained advisors to conduct a forensic accounting investigation. In addition, our Board of Directors authorized the Audit Committee (consisting of three independent members of the Board), together with Morrison Foerster LLP, as independent counsel, to oversee the investigation and advise the Audit Committee with respect to the investigation. In February 2002, Blank Rome reported the results of the investigation to the Audit Committee and the Board of Directors, which included among other things, that we implement certain remedial procedures, controls and systems.

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As a result of the investigation and other reviews we performed, we restated our previously issued consolidated financial statements for fiscal 2000, each of the quarters in such year, and the first three quarters of 2001. The effect of the restatement is presented in Item 7. Management's Discussion and Analysis of Financial Condition and Results of Operations and in Notes 2 and 20 of the Notes to the Consolidated Financial Statements.

The Securities and Exchange Commission has issued a formal order of investigation into, among other things, certain accounting matters relating to our financial statements, periodic reporting and internal accounting control provisions of the federal securities laws.

We are involved in routine litigation in the ordinary course of our business, which in management's opinion will not have a material adverse effect on our financial condition, cash flows or results of operations.

Item 4. Submission of Matters to a Vote of Security Holders.

Not Applicable.

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PART II

Item 5. Market for Registrant's Common Equity and Related Stockholder Matters.

Market Information. Our common stock has traded since September 23, 1998 on the NASDAQ National Market under the symbol "TTWO." From April 14, 1997 to September 22, 1998, our common stock traded on the NASDAQ SmallCap Market. On January 22, 2002, trading in our common stock was halted by NASDAQ pending our furnishing certain information relating to a restatement of our financial statements. The following table sets forth, for the periods indicated, the range of the high ask and low bid prices for the common stock as reported by NASDAQ. Such prices reflect inter-dealer quotations, without retail mark-up, mark-down or commission and may not necessarily represent actual transactions.

	High	Low
Fiscal Year Ended October 31, 2000 -----		
First Quarter	17.50	10.00
Second Quarter	18.94	8.00
Third Quarter	13.50	8.88
Fourth Quarter	16.50	9.00

Fiscal Year Ended October 31, 2001

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First Quarter	13.44	8.41
Second Quarter	14.63	10.44
Third Quarter	24.50	14.06
Fourth Quarter	21.62	6.44

Fiscal Year Ending October 31, 2002

First Quarter (through January 22, 2002)	19.50	9.30
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The last reported sale price for our common stock on January 22, 2002 was \$18.56. The number of record holders of our common stock was approximately 157 as of January 22, 2002. We believe that there are in excess of 1,000 beneficial owners of our common stock.

Dividend Policy. To date, we have not declared or paid any cash dividends. The payment of dividends, if any, in the future is within the discretion of the board of directors and will depend upon future earnings, capital requirements and other relevant factors. The payment of cash dividends is restricted by the terms of our loan agreement. We presently intend to retain all earnings to finance continued growth and development of our business and we do not expect to declare or pay any cash dividends in the foreseeable future.

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Item 6. Selected Financial Data.

Our consolidated financial statements for the fiscal year ended October 31, 2000, the related Management's Discussion and Analysis of Financial Condition and Results of Operations for such year, each of the quarters in such year and the interim quarters of fiscal 2001 have been restated. See Management's Discussion and Analysis of Financial Condition and Results of Operations and Consolidated Financial Statements contained elsewhere in this Report.

(in thousands, except per share data)

Statement of Operations Data:

	Fiscal Year Ended October		
	2001 (1)	2000 (2)	1999
Net sales.....	\$451,056	\$364,001	\$304,714
Income (loss) from operations.....	25,841	33,309	27,381
Income (loss) before extraordinary item and cumulative effect of change in accounting principle.....	(1,295)	6,417	16,332
Net income (loss).....	(8,580)	6,417	16,332
Net income (loss) per share			
Basic.....	\$ (.25)	\$.23	\$.79
Diluted.....	(.25)	.23	.76

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Net income (loss) per share attributable to common stockholders - Diluted (4).....	(.25)	.23	.76
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Balance Sheet Data:

	2001	2000 (2)	1999
	-----	-----	-----
Cash and cash equivalents.....	\$6,056	\$5,245	\$10,374
Working capital.....	88,229	69,025	41,439
Total assets.....	354,997	330,257	231,712
Total debt.....	54,073	96,873	56,137
Total liabilities.....	134,936	160,065	146,609
Stockholders' equity.....	220,061	170,192	85,103

- (1) Includes approximately \$27 million of net sales and \$5.3 million of income, net of taxes of \$3.6 million, representing the effect of the adoption of Staff Accounting Bulletin 101 "Revenue Recognition" (SAB 101) in the first quarter of fiscal 2001. There was no impact on net income. See Note 3 of Notes to Consolidated Financial Statements.
- (2) As restated. See "Management's Discussion and Analysis of Financial Condition and Results of Operations - Restatement of Historical Financial Statements."
- (3) Net income in 1998 and 1997 includes acquired S corporation net income of \$1,233,000 and \$1,347,000, respectively.
- (4) Gives effect to distributions of \$673,000 and \$931,000 to S corporation shareholders prior to acquisitions in 1998 and 1997, respectively.

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Item 7. Management's Discussion and Analysis of Financial Condition and Results of Operations.

Restatement of Historical Financial Statements

In connection with an informal and voluntary request from the SEC to provide documents, we engaged counsel to conduct an investigation into our accounting treatment of certain transactions in fiscal 2000 and 2001. Counsel retained advisors to perform a forensic accounting investigation. As a result of the investigation, we restated our previously issued consolidated financial statements for fiscal 2000 to eliminate \$15,367,000 of net sales made to certain independent third-party distributors and related cost of sales of \$8,702,000, which were improperly recognized as revenue and later returned or repurchased by us.

In addition, we reviewed our revenue recognition policy, reserve policies and our accounting for certain other transactions. As a result of this review, we restated our previously issued consolidated financial statements for fiscal 2000 for the following transactions:

- o The elimination of \$3,780,000 of net sales and related cost of sales of \$2,236,000 that were previously recognized for products that had not been shipped within the period;

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- o A charge of \$19,206,000 to record our portion of the losses incurred by an affiliate accounted for under the equity method in accordance with the provisions of EITF Issue No. 99-10, and a net reduction for post acquisition amortization of \$710,000 after we acquired the remaining 80% interest in this entity. See Note 5 of Notes to Consolidated Financial Statements; and
- o The elimination of \$2,563,000 of license revenue in connection with a business combination.

Our financial statements for fiscal 2000 have been restated as follows (and are presented in thousands, except per share data):

	Year ended October 31, 2000	
	As Reported	As Restated
Statement of Operations Data:		
Net sales (1).....	\$387,006	\$364,001
Cost of sales (1).....	247,796	235,978
Depreciation and amortization	9,805	8,680
Income from operations	45,061	33,309
Equity in loss of affiliate	763	19,969
Income before provision for income taxes	38,229	8,961
Provision for income taxes	13,266	2,544
Net income	24,963	6,417
Basic income per share	0.91	0.23
Diluted income per share	0.88	0.23

- (1) Restated amounts give effect to reclassification of certain amounts to conform to current year presentation, including the reduction in net sales and costs of sales by approximately \$1.3 million.

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	October 31, 2000	
	As Reported	As Restated
Balance Sheet Data:		
Accounts receivable*	\$134,877	\$110,783
Inventories*	44,922	53,798
Prepaid royalties - current	19,721	24,093
Deferred tax assets	666	9,243
Intangible assets	90,505	66,562
Other assets, net	1,565	2,558
Total assets	351,641	330,257
Accounts payable	47,972	46,566
Accrued expenses and other current liabilities*	19,357	16,189
Total liabilities	164,639	160,065
Retained earnings	43,365	24,819
Total liabilities and stockholders' equity ...	351,641	330,257

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* Restated amounts reflect a reclassification relating to the presentation of allowance for returns.

We also restated the unaudited results of operations for each of the quarters in fiscal 2000 for the matters described above.

Our unaudited results of operations for each of the three quarters in the period ended July 31, 2001 were restated for the matters discussed above and for the following:

- o The cumulative effect in the first quarter of the change in accounting related to the adoption of SAB 101. See Note 3 of Notes to Consolidated Financial Statements;
- o The recognition in the first quarter of net sales of \$3,780,000 and related cost of sales of \$2,237,000 for transactions that did not qualify for revenue recognition in the fourth quarter of fiscal 2000;
- o An additional charge of \$438,000, net of taxes of \$292,000, in the third quarter for an extraordinary loss on the early extinguishment of debt; and
- o An adjustment in the first two quarters for income related to the reversal of revenue of \$721,000 in the first quarter and \$951,000 in the second quarter, net of expense reductions, and a corresponding adjustment to the purchase price related to a business acquired during the year.

	Nine months ended July 31, 2001	
	As Reported	As Restated(1)
Statement of Operations Data:		
Net sales	\$ 309,048	\$ 327,797
Cost of sales	201,609	211,268
Income from operations	23,610	34,513
Net income (loss)	(3,765)	(3,900)
Basic income per share	(.11)	(.12)
Diluted income per share	(.11)	(.12)

(1) The results of operations for the third quarter of fiscal 2001, as restated, has been revised to correct mathematical miscalculations made in the course of preparing the restatement. The revisions do not involve the application of any accounting principle or have any impact on the results of operations for fiscal 2001. See Note 20 of Notes to Consolidated Financial Statements for financial information relating to the restatement of the fiscal 2000 and fiscal 2001 quarters.

Significant Accounting Policies

Financial Reporting Release No. 60, which was recently released by the Securities and Exchange Commission, requires all companies to include a discussion of critical accounting policies or methods used in the preparation of financial statements. Note 3 of the Notes to the Consolidated Financial Statements includes a summary of the significant accounting policies and methods used in the preparation of our Consolidated Financial Statements. The following is a brief discussion of the more significant accounting policies and methods used by us.

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In addition, Financial Reporting Release No. 61 was recently released by the SEC to require all companies to include a discussion to address, among other things, liquidity, off-balance sheet arrangements, contractual obligations and commercial commitments.

General

The preparation of financial statements in conformity with generally accepted accounting principles requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and the disclosure of contingent assets and liabilities at the dates of the financial statements and the reported amounts of revenues and expenses during the reporting periods. The most significant estimates and assumptions relate to the recoverability of prepaid royalties, capitalized software development costs and other intangibles, inventories, realization of deferred income taxes and the adequacy of allowances for returns, price protection and doubtful accounts. Actual amounts could differ significantly from these estimates.

Revenue Recognition

Our principal sources of revenues are derived from publishing and distribution operations. Publishing revenues are derived from the sale of internally developed software titles or software titles licensed from third parties. Distribution revenues are derived from the sale of third-party software titles, accessories and hardware. Publishing activities generally generate significantly higher margins than distribution activities, with sales of PC software titles resulting in higher margins than sales of CDs or cartridges designed for video game consoles. Effective November 1, 2000, we recognize revenue net of allowances for returns and price protection when title and risk of loss pass to customers (generally, upon receipt of products by customers). Prior to that date, we recognized revenue upon shipment. In accordance with Statement of Position 97-2 "Software Revenue Recognition" we recognize revenue when the price is fixed and determinable, upon persuasive evidence of an agreement, our fulfillment of our obligations under any such agreement and a determination that collection is probable. Our payment arrangements with customers provide primarily 60 day terms and to a limited extent with certain customers 30, 90 or 120 day terms. We may not have a reliable basis to estimate returns and allowances for certain customers or we may be unable to determine that collection of receivables is probable. In such circumstances, we defer revenues at the time of sale and recognize revenues when collection of the related receivable becomes probable or cash is collected.

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Returns and Reserves

Our arrangements with customers for published titles generally require us to accept returns and provide price protection. We establish a reserve for future returns of published titles and price protection based primarily on historical return rates, return policies and price protection, and recognize revenues net of allowances for returns and price protection. Our distribution arrangements with customers generally do not give them the right to return titles or to cancel firm orders. However, we sometimes accept returns for stock balancing and negotiate accommodations to customers, which includes price discounts, credits and returns, when demand for specific titles fall below expectations. The historical product return rate for our distribution business has been substantially less than for our publishing business. If future returns

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significantly exceed our reserves, our operating results would be adversely affected.

Prepaid Royalties

Our agreements with licensors and developers generally require us to make advance royalty payments and pay royalties based on product sales. Prepaid royalties are capitalized when technological feasibility of the related software title is established, which generally occurs early in the development cycle. Prepaid royalties are amortized as cost of sales based on the greater of the proportion of current year sales to total of current and estimated future sales on a product-by-product basis for that title or the contractual royalty rate based on actual net product sales. We continually evaluate recoverability of prepaid royalties on a product-by-product basis and we charge to cost of sales any amount that management deems unlikely to be recoverable in the future.

Prepaid royalties are classified as current and non-current assets based on estimated net product sales within the next year. Unrecoverable prepaid royalties written down amounted to \$975,000, \$501,000 and \$1,308,000 for the years ended October 31, 2001, 2000 and 1999. Amortization of prepaid royalties amounted to \$17,598,000, \$16,849,000 and \$12,144,000 for the years ended October 31, 2001, 2000 and 1999.

Capitalized Software Development Costs

We capitalize internal software development costs subsequent to establishing technological feasibility of a title. Amortization of such costs as cost of sales is done on a product-by-product basis based on the greater of the proportion of current year sales to total of current and estimated future sales for that title or the straight-line method over the remaining estimated useful life of the title. We continually evaluate the recoverability of capitalized costs. Capitalized software costs were written down by \$389,000 and \$698,000 for the years ended October 31, 2001 and 1999. No capitalized software costs were written down for the year ended October 31, 2000. Amortization of capitalized software costs amounted to \$3,780,000, \$1,451,000 and \$1,136,000 for the years ended October 31, 2001, 2000 and 1999.

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Income Taxes

Income tax assets and liabilities are determined by taxable jurisdiction. We do not provide taxes in undistributed earnings of our subsidiaries. The total amount of undistributed earnings of foreign subsidiaries for income tax purposes was approximately \$36 million and \$10 million for the years ended October 31, 2001 and 2000, respectively. It is our intention to reinvest undistributed earnings of our foreign subsidiaries and thereby indefinitely postpone their remittance. Accordingly, no provision has been made for foreign withholding taxes or United States income taxes which may become payable if undistributed earnings of foreign subsidiaries are paid as dividends to us.

Results of Operations

The following table sets forth for the periods indicated the percentage of net sales represented by certain items reflected in our statement of operations, and sets forth net sales by territory, platform and principal product:

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	Years Ended October 31,		
	2001	2000	1999
	(as restated)		
OPERATING DATA:			
Net sales	100.0%	100.0%	100.0%
Cost of sales	67.9	64.8	70.2
Selling and marketing	12.2	11.8	9.9
General and administrative ...	9.9	10.0	8.3
Research and development	1.4	1.6	1.7
Depreciation and amortization	2.8	2.4	0.9
Interest expenses	1.9	1.7	1.0
Provision (benefit) for income taxes	(0.5)	0.7	2.7
Net income (loss)	(1.9)	1.8	5.4
NET SALES BY TERRITORY:			
North America	76.4%	71.6%	67.0%
International	23.6	28.4	33.0
PLATFORM MIX (publishing):			
Console	57.5%	50.6%	47.4%
PC	35.7	36.9	41.7
Hand-held	1.9	7.3	5.7
Accessories	4.9	5.2	5.2
PRINCIPAL PRODUCT SALES (2001)			
Grand Theft Auto 3, PS2.....	7.4%	--	--
Max Payne, PC.....	5.2	--	--
Midnight Club, PS2.....	4.1	2.7	--
Smugglers Run, PS2.....	3.0	3.3	--
Ten largest titles.....	31.3%	16.4%	33.5%

Business Acquisitions and Dispositions

In April 2000, we acquired the remaining 80.1% of the stock of Gathering of Developers, Inc. that we did not already own for 1,060,000 shares of common stock. Prior to the acquisition, we had a distribution and publishing arrangement with Gathering under which we were entitled to receive a distribution fee of 20% of net receipts derived from sales of PC products. Products sold under this arrangement accounted for approximately 6.3% of our net sales and 18.0% of our net income for the year ended October 31, 1999, and approximately 9.7% of our net sales and 9.3% of our net income during fiscal 2000.

We also acquired PopTop Software, Inc., an independent software developer, in July 2000 for 559,100 shares of common stock. PopTop's operations did not contribute to our revenues and its loss did not significantly affect our net income during fiscal 2000.

We purchased Toga Holdings BV, the parent of Pixel Broadband Studios Ltd. in March 2000 as part of our Internet strategy for \$4.5 million in cash and 2,561,000 shares of common stock. Pixel had developed leading-edge software technology, which enables broadband carriers to deliver persistent online gameplay via satellite, cable and wireless communications devices. We intended to combine Pixel's business with the gaming content of our Rockstar video game publishing subsidiary with a view toward obtaining financing to operate this business independently. Due to unfavorable market conditions, we abandoned a proposed financing in July 2000. We incurred a charge of \$1,103,000 consisting primarily of professional fees related to the abandoned offering.

We sold Toga to Gameplay.com plc in October 2000. During fiscal 2000, Toga's operations did not contribute to our revenues and accounted for an operating loss of approximately \$1.5 million. We incurred a loss of \$286,000 in connection with the sale of Toga. In connection with the sale of Toga, we entered into a Joint Exploitation Agreement with Gameplay pursuant to which we acquired Neo Software Productions GMBH, a software developer based in Austria. Neo developed Max Payne for Microsoft's Xbox.

In February 2000, we sold Falcon Ventures d/b/a DVDWave.com, an online provider of music CDs, to eUniverse, Inc. and recorded a gain of \$1,976,000. Falcon Ventures accounted for an insignificant portion of our revenues and accounted for an operating loss of approximately \$1.1 million during fiscal 2000.

In November 2000, we acquired all of the capital stock of VLM Entertainment Group Inc., a third-party video game distributor, for \$2 million in cash and 875,000 shares of common stock and assumed liabilities of approximately \$10.6 million. VLM accounted for 14.4% of our distribution revenues in fiscal 2001.

In July 2001, we acquired all of the outstanding capital stock of Techcorp Limited, a Hong Kong based design and engineering firm specializing in video game accessories, for 30,000 shares of restricted common stock, \$100,000 in cash and assumed liabilities of \$2.9 million. The acquisition of Techcorp did not have a significant effect on our 2001 operating results.

In July 2001, we sold all of the outstanding capital stock of Jack of All Games UK, a video game distributor, to Jay Two Limited, an unaffiliated third-party controlled by Freightmasters Ltd., for approximately \$215,000. In

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connection with the sale, the purchaser assumed net liabilities of \$436,000. We recorded a gain on this sale of \$651,000. The sale of Jack of All Games UK is not expected to have a significant effect on our future operating results.

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Fiscal Year Ended October 31, 2001 and 2000

Net Sales. Net sales increased by \$87,055,000, or 23.9%, to \$451,056,000 for fiscal 2001 from \$364,001,000 for fiscal 2000. The increase was attributable to growth in both publishing and distribution operations and acquisitions. The adoption of SAB 101 effective November 2000 to recognize revenue when both title and all risks of loss pass to customers resulted in an increase in net sales of \$27 million. Fiscal 2000 sales that were previously recognized upon product shipment were effectively reversed with the adoption of SAB 101 and reported upon receipt by the customer as sales in the first quarter of fiscal 2001. In fiscal 2001, we implemented changes to our practices to significantly reduce shipment time near quarter and year end. Accordingly, the adoption of SAB 101 did not have a significant impact on previously reported interim results for the first three quarters of fiscal 2001.

Publishing revenues increased by \$56,795,000 or 30.5%, to \$242,913,000 for fiscal 2001 from \$186,118,000 for fiscal 2000. The increase was primarily attributable to the release of Grand Theft Auto 3 for PlayStation 2 and Max Payne for the PC, and included \$21 million resulting from the adoption of SAB 101. Publishing activities accounted for approximately 53.9% of net sales in fiscal 2001.

In fiscal 2001, software titles designed for PC platforms accounted for approximately 35.7% of publishing revenues as compared to 36.9% in the prior year. Software titles designed for video game console platforms accounted for 57.5% of publishing revenues as compared to 50.6% in the prior year. We expect that sales of video game console titles will continue to account for an increasing portion of our publishing revenues.

Distribution revenues increased by \$30,260,000, or 17.0%, to \$208,143,000 for fiscal 2001 from \$177,883,000 for fiscal 2000. The increase was attributable to the continued rollout of Sony's PlayStation 2, and included \$6 million relating to the adoption of SAB 101. VLM Entertainment Group, which was acquired in November 2000, accounted for 14.4% of our distribution revenues in fiscal 2001. In fiscal 2001, distribution activities accounted for approximately 46.1% of net sales, with video game hardware and peripherals accounting for 16.0% of net sales.

International operations accounted for approximately \$106,564,000 or 23.6% of net sales in fiscal 2001 compared to \$103,315,000 or 28.4% in fiscal 2000. The percentage decrease was attributable to the growth in our North American operations. In recent periods, we placed increasing emphasis on expanding publishing activities in Europe, and we sold our Jack of All Games UK distribution subsidiary in July 2001. We expect that international sales will continue to account for a significant portion of our future revenues.

Cost of Sales. Cost of sales increased by \$70,286,000 or 29.8%, to \$306,264,000 for fiscal 2001 from \$235,978,000 for fiscal 2000. The increase was commensurate with increased net sales and included \$18 million resulting from the adoption of SAB 101. Cost of sales primarily represents royalties paid to our manufacturers, amortization of prepaid royalties to third-party developers, amortization of capitalized software related to internally developed titles and

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the cost of third-party products for our distribution business. Included in cost of sales is a non-cash impairment charge of \$3,786,000 taken in the quarter ended April 30, 2001 relating to a reduction in the value of certain Internet gaming assets. Cost of sales as a percentage of net sales increased to 67.9% for fiscal 2001 from 64.8% for fiscal 2000 as a result of higher production costs associated with the development of next-generation software titles and the aforementioned impairment charge. We estimate that cost of sales as a percentage of net sales in our publishing business is generally 60%, while cost of sales as a percentage of net sales in our distribution business is generally 90%.

Selling and Marketing. Selling and marketing expenses increased by \$12,399,000, or 28.9%, to \$55,253,000 for fiscal 2001 from \$42,854,000 for fiscal 2000. The increase was primarily attributable to increased advertising activities relating to our new releases in 2001. Selling and marketing expenses as a percentage of net sales remained relatively constant from year to year.

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General and Administrative. General and administrative expenses increased by \$8,458,000, or 23.2%, to \$44,867,000 for fiscal 2001 from \$36,409,000 for fiscal 2000. General and administrative expenses as a percentage of net sales remained relatively constant from year to year at 10.0%. The increase in absolute dollars was attributable to increased salaries and rent necessary to support our expanded operations and increased bad debt expenses.

Research and Development. Research and development costs increased by \$522,000, or 9.2%, to \$6,190,000 for fiscal 2001 from \$5,668,000 for fiscal 2000. Research and development costs as a percentage of net sales remained relatively constant from year to year. Once software development projects reach technological feasibility, a substantial portion of our research and development costs are capitalized and subsequently amortized as cost of goods sold. These capitalized software development costs relate to our internally developed publishing titles.

Depreciation and Amortization. Depreciation and amortization expense increased by \$3,961,000, or 45.6%, to \$12,641,000 for fiscal 2001 from \$8,680,000 for fiscal 2000. Depreciation and amortization expense as a percentage of net sales increased to 2.8% for fiscal 2001 from 2.4% for fiscal 2000. The increases were attributable to amortization of intangible assets as a result of business acquisitions offset by the impact of sales of businesses made in fiscal 2000 and fiscal 2001.

Income from Operations. Income from operations decreased by \$7,468,000, or 22.4%, to \$25,841,000 for fiscal 2001 from \$33,309,000 for fiscal 2000 primarily due to the increase in our cost of sales discussed above.

Interest Expenses. Interest expenses increased by \$2,441,000, or 40.2% to \$8,510,000 for fiscal 2001 from \$6,069,000 for fiscal 2000. The increase was attributable to higher levels of borrowings during 2001. Interest expenses as a percentage of net sales remained constant.

Gain on Sale of Subsidiary. We sold Jack of All Games UK in July 2001 and recorded a gain on sale of \$651,000.

Loss on Available-For-Sale Internet Securities. We incurred non-cash impairment charges of \$21,477,000 during fiscal 2001 relating to our Internet related investments to reflect other than temporary declines in the value of such investments.

Income Taxes. Income tax expenses decreased by \$4,744,000 for fiscal

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2001 from fiscal 2000. The decrease was attributable to tax losses in fiscal 2001 compared to taxable income in fiscal 2000. We recorded an income tax benefit of \$2,200,000 for fiscal 2001 compared to an income tax provision of \$2,544,000 for fiscal 2000. The effective tax rate in 2001 and 2000 of (62.9%) and 28.4%, respectively, are the result of state and foreign tax rate differentials partially offset by non deductible items. We believe that it is more likely than not that we will generate sufficient levels of taxable income in the future to realize \$21,765,000 of reported net deferred tax assets, approximately \$7 million of which is a capital loss carryforward. The amount of the deferred tax asset considered realizable, however, could be reduced in the near term if estimates of future taxable income during the carryforward period are reduced. Failure to achieve sufficient levels of taxable income from capital transactions might affect the ultimate realization of the capital loss carryforwards. If this were to occur, management is committed to implementing tax planning strategies, such as the sale of net appreciated assets to the extent required (if any) to generate sufficient taxable income prior to the expiration of the capital loss carryforwards.

Extraordinary Item. We incurred an extraordinary charge of \$1,948,000, net of taxes of \$1,217,000, upon the early extinguishment of debt of \$15,000,000 in July 2001.

Cumulative Effect of Change in Accounting Principle. In connection with our adoption of SAB 101, we recognized a cumulative effect of \$5.3 million, net of taxes of \$3,558,000.

Net (loss) Income. As a result of the foregoing, for fiscal 2001, we incurred a net loss of \$8,580,000 as compared to net income of \$6,417,000 for fiscal 2000.

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Fiscal Years Ended October 31, 2000 and 1999

Net Sales. Net sales increased by \$59,287,000, or 19.5%, to \$364,001,000 for fiscal 2000 from \$304,714,000 for fiscal 1999. Substantially all of the increase in net sales in fiscal 2000 was attributable to internal growth of our publishing and distribution operations.

Publishing revenues increased by \$27,001,000, or 17.0%, to \$186,118,000 for fiscal 2000 from \$159,117,000 for fiscal 1999. The increase was primarily attributable to the release of Midnight Club and Smuggler's Run at the launch of PlayStation 2. In fiscal 2000, publishing activities accounted for approximately 51.1% of our net sales.

In fiscal 2000, software products designed for PC platforms accounted for approximately 36.9% of our publishing revenues as compared to 41.7% in fiscal 1999. The decrease was primarily attributable to our emphasis on developing and releasing titles for next-generation video game console platforms. Software titles developed for video game console platforms accounted for 50.6% of publishing revenues compared to 47.4% in the prior year. The increase was primarily attributable to the release of several new products with the launch of PlayStation 2 in October 2000.

Distribution revenues increased by \$32,286,000, or 22.2%, to \$177,883,000 for fiscal 2000 from \$145,597,000 for fiscal 1999. The increase was primarily attributable to continued strong sales of PlayStation hardware and

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software, and the launch of PlayStation 2. In fiscal 2000, distribution activities accounted for approximately 48.9% of our net sales, with video game hardware and peripherals accounting for 20.4% of net sales.

International operations accounted for approximately \$103,315,000 or 28.4% of our net sales for fiscal 2000 compared to \$100,520,000 or 33.0% for fiscal 1999. The percentage decrease was primarily attributable to the growth in our North American operations.

Cost of Sales. Cost of sales increased by \$22,074,000, or 10.3%, to \$235,978,000 for fiscal 2000 from \$213,904,000 for fiscal 1999. The increase was primarily a result of the expanded scope of our operations and was consistent with revenue growth. Cost of sales as a percentage of net sales decreased to 64.8% for fiscal 2000 from 70.2% for fiscal 1999. This decrease was primarily due to an increase in our higher margin publishing activities.

Selling and Marketing. Selling and marketing expenses increased by \$12,746,000, or 42.3%, to \$42,854,000 for fiscal 2000 from \$30,108,000 for fiscal 1999. Selling and marketing expenses as a percentage of net sales increased to 11.8% for fiscal 2000 from 9.9% for fiscal 1999. The increases were due to increased marketing costs associated with establishing our publishing programs and brand names.

General and Administrative. General and administrative expenses increased by \$11,173,000 or 44.3%, to \$36,409,000 for fiscal 2000 from \$25,236,000 for fiscal 1999. General and administrative expenses as a percentage of net sales increased to 10.0% for fiscal 2000 from 8.3% for fiscal 1999. The increases were due to additional salaries, rent, insurance premiums and professional fees in connection with our expanded operations and from our acquisitions offset by our dispositions.

Research and Development. Research and development costs increased by \$405,000, or 7.7%, to \$5,668,000 for fiscal 2000 from \$5,263,000 for fiscal 1999. Research and development costs as a percentage of sales decreased to 1.6% for fiscal 2000 from 1.7% for fiscal 1999.

Depreciation and Amortization. Depreciation and amortization expense increased by \$5,858,000 to \$8,680,000 for fiscal 2000 from \$2,822,000 for fiscal 1999. Depreciation and amortization expense as a percentage of net sales increased to 2.4% for fiscal 2000 from 0.9% for fiscal 1999. The increases were attributable to the amortization of goodwill associated with the acquisitions of Toga Holdings, Gathering of Developers and DMA Design Limited. We sold Toga Holdings in October 2000.

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Abandoned Offering Costs. We incurred a charge of \$1,103,000 relating to an abandoned offering in fiscal 2000.

Income from Operations. Income from operations increased by \$5,928,000, or 21.7%, to \$33,309,000 for fiscal 2000 from \$27,381,000 for fiscal 1999. The increase was commensurate with our growth in net sales offset by the changes referred to above.

Interest Expenses. Interest expenses increased by \$3,159,000, or 108.6%, to \$6,069,000 for fiscal 2000 from \$2,910,000 for fiscal 1999. The increase was primarily a result of increased borrowings and the amortized portion of the expenses relating to a subordinated loan.

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Gain on Sale of Subsidiary - Net. Includes a gain on sale of \$1,976,000 relating to the sale of Falcon Ventures and offset by a loss of \$286,000 relating to the sale of Toga Holdings.

Equity in Loss of Affiliate. In fiscal 2000, in accordance with EITF 99-10, we incurred a charge of \$19,969,000 for our share of losses incurred by Gathering of Developers prior to our acquisition of the then remaining interest in Gathering of Developers. The increase over fiscal 1999 is the result of increased losses at Gathering of Developers coupled with the implementation of EITF 99-10.

Income Taxes. Income taxes decreased by \$5,550,000 or 68.6% to \$2,554,000 as a result of a reduced taxable income for fiscal 2000 as compared to a tax provision of \$8,094,000 for fiscal 1999. The reduction in the effective tax rate of 28.4% in fiscal 2000 from 33.1% in fiscal 1999 is primarily attributable to the foreign tax rate differential.

Net Income. As a result of the foregoing, we recorded net income of \$6,417,000 in fiscal 2000, as compared to net income of \$16,332,000 in fiscal 1999.

Liquidity and Capital Resources

Our primary cash requirements have been and will continue to be to fund developing, publishing and distributing our products. We have historically financed our operations through cash flows from operations, the issuance of debt and equity securities and bank borrowings. At October 31, 2001, we had working capital of \$88,229,000 as compared to working capital of \$69,025,000 at October 31, 2000. At October 31, 2001, we had cash and cash equivalents of \$6,056,000.

Net cash provided by operating activities for fiscal 2001 was \$27,319,000 as compared to net cash used in operating activities of \$54,230,000 for fiscal 2000 and \$16,023,000 for fiscal 1999. The increase in 2001 was primarily attributable to our increased focus on working capital management. In fiscal 2000 and 1999, we invested substantial funds in our next-generation entertainment software publishing subsidiaries. We believe that such investments will continue to be reflected in future cash flow from operations. Fiscal 1999 cash flows were also impacted by an increase in accounts receivable offset in part by an increase in accounts payable.

Net cash used in investing activities for fiscal 2001 was \$13,479,000 as compared to \$12,906,000 for fiscal 2000 and \$21,540,000 for fiscal 1999. Net cash used in investing activities in 2001 related primarily to the purchase of fixed assets and to a lesser extent acquisitions. Net cash used in investing activities in 2000 and 1999 related primarily to acquisitions.

Net cash used in financing activities for fiscal 2001 was \$11,790,000 as compared to net cash provided by financing activities of \$70,535,000 for fiscal 2000 and \$46,055,000 for fiscal 1999. Net cash used in fiscal 2001 related primarily to the repayment of indebtedness offset by proceeds from equity offerings and the exercise of stock options and warrants. Net cash provided by operations in fiscal 2000 and 1999 was primarily due to proceeds from borrowings and equity offerings.

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lenders led by Bank of America, N.A., as agent. The agreement was amended in February 2002 to provide for borrowings of up to \$15,000,000 through February 20, 2002; \$22,500,000 through February 28, 2002; \$30,000,000 through April 13, 2002; and \$50,000,000 through the remaining term of the agreement. Generally, advances under the line of credit are based on a borrowing formula equal to the lesser of (1) the borrowing limit or (2) 70% of eligible accounts receivable, plus 25% of eligible inventory. Interest accrues on such advances at the bank's prime rate plus 0.5%, or at LIBOR plus 2.5%. Borrowings under the line of credit are collateralized by our accounts receivable, inventory, equipment, general intangibles, securities and other personal property, including the capital stock of our domestic subsidiaries. The loan agreement contains certain financial and other covenants, which were amended retroactively. Accordingly, as of October 31, 2001, we were in compliance with such covenants, as amended. The loan agreement limits or prohibits us from declaring or paying cash dividends, merging or consolidating with another corporation, selling assets (other than in the ordinary course of business), creating liens and incurring additional indebtedness. The line of credit expires on December 7, 2002. As of October 31, 2001, \$48,701,000 was outstanding under the line of credit.

In January 2001, our United Kingdom subsidiary entered into a credit facility agreement, as amended, with Lloyds TSB Bank plc under which Lloyds agreed to make available borrowings of up to \$19,000,000. Advances under the credit facility bear interest at the rate of 1.25% per annum over the bank's base rate, and are guaranteed by us. The credit facility expires in March 2002. As of October 31, 2001, \$5,372,000 was outstanding under the credit facility.

During the year ended October 31, 2001, we received proceeds of \$22,614,000 from the exercise of stock options and warrants.

In July 2001, we sold 1,300,000 shares of common stock in a private placement and received net proceeds of approximately \$20.9 million. We used the proceeds to repay in full the subordinated indebtedness described below, and other indebtedness.

In July 2000, we entered into a subordinated loan agreement with Finova Mezzanine Capital under which we borrowed \$15,000,000 evidenced by a five-year promissory note bearing interest at the rate of 12.5% per annum, payable monthly. In connection with the loan, we issued to Finova warrants to purchase 451,747 shares of common stock at an exercise price of \$11.875 per share. We incurred an extraordinary charge of \$1,948,000, net of taxes, upon the early repayment of this indebtedness.

In connection with our acquisition of the franchise of Duke Nukem' PC and video games in December 2000, we are obligated to pay \$6 million in cash upon delivery of the final PC version of Duke Nukem' Forever.

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Our accounts receivable, less an allowance for doubtful accounts, returns and price protection and other discounts at October 31, 2001 were \$94,950,000. Of such receivables, approximately \$11,033,000 or 11.7% was due from one customer. Most of our receivables are covered by insurance and generally have been collected in the ordinary course of business. Our sales are typically made on credit, with terms that vary depending upon the customer and the demand for the particular title being sold. We do not hold any collateral to secure payment by our customers. As a result, we are subject to credit risks, particularly in the event that any of our receivables represent sales to a limited number of retailers or are concentrated in foreign markets. If we are unable to collect our accounts receivable as they become due and such accounts are not covered by insurance, our liquidity and working capital position would

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be adversely affected. We had accounts receivable days outstanding of 69 at October 31, 2001, as compared to 92 days at October 31, 2000.

Our offices and warehouse facilities are occupied under noncancelable operating leases expiring at various times from July 2001 to October 2011. Additionally, we have leased certain furniture, equipment and automobiles under noncancelable operating leases expiring through July 2005. Our future minimum rental payments for the year ending October 31, 2002 are \$3,879,000, and aggregate minimum rental payments through applicable lease expirations is \$16,756,000.

We have no material commitments for capital expenditures. We anticipate incurring significant additional legal, accounting and other professional expenses in connection with pending litigation and regulatory matters.

Recently Issued Accounting Pronouncements

In July 2001, the FASB issued Statement of Financial Accounting Standard No. 141, "Business Combinations" ("SFAS 141") and Statement of Financial Accounting Standard No. 142, "Goodwill and Other Intangible Assets" ("SFAS 142").

SFAS 141 establishes accounting and reporting for business combinations by requiring that all business combinations be accounted for under the purchase method. Use of the pooling-of-interests method is no longer permitted. SFAS 141 also provides guidance on purchase accounting related to the recognition of intangible assets and accounting for negative goodwill. SFAS 141 requires that the purchase method be used for business combinations initiated after June 30, 2001. SFAS 142 changes the accounting for goodwill from an amortization method to an impairment-only approach. Upon adoption of SFAS 142, amortization of goodwill recorded for business combinations consummated prior to July 1, 2001 will cease, and intangible assets acquired prior to July 1, 2001 that do not meet the criteria for recognition under SFAS 141 will be reclassified to goodwill. Goodwill will be subject to an annual impairment test, including a transitional impairment test required upon adoption of SFAS 142, which companies have six months to complete.

The provisions of SFAS 142 will be effective for fiscal years beginning after December 15, 2001; however, early adoption is permitted. We anticipate the early adoption of SFAS 142 as of the beginning of fiscal 2002. We are still in the process of reallocating previously identifiable intangibles that do not meet the criteria of SFAS 141 into goodwill and evaluating the useful lives of our remaining identifiable intangibles. However, we currently estimate that unaudited pro forma income before extraordinary item and cumulative effect of change in accounting principle and the respective diluted EPS would have been approximately \$2.9 million and \$0.08, respectively for the year ended October 31, 2001 had the provisions of the new standards been applied in that year. We are in the process of completing the step one transitional assessment of goodwill. We do not currently anticipate having to record a transition impairment of goodwill or other intangible assets as a cumulative effect as a result of these new standards.

In August 2001, the FASB issued Statement of Financial Accounting Standard No. 143, "Accounting for Obligations Associated with the Retirement of Long-Lived Assets" ("SFAS 143"). The objective of SFAS 143 is to provide accounting guidance for legal obligations associated with the retirement of long-lived assets. The retirement obligations included within the scope of this project are those that an entity cannot avoid as a result of either the acquisition, construction or normal operation of a long-lived asset. Components of larger systems also fall under this project, as well as tangible long-lived assets with indeterminable lives. The provisions of SFAS 143 are effective for financial statements issued for fiscal years beginning after June 15, 2002. We

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are currently evaluating the expected impact of the adoption of SFAS 143 on our financial condition, cash flows and results of operations and will adopt SFAS 143 in fiscal 2003.

In October 2001, the FASB issued Statement of Financial Accounting Standard No.144, "Accounting for the Impairment or Disposal of Long-Lived Assets" ("SFAS 144"). The objectives of SFAS 144 are to address significant issues relating to the implementation of SFAS 121 and to develop a single accounting model, based on the framework established in SFAS 121, for long-lived assets to be disposed of by sale, whether previously held and used or newly acquired. The provisions of SFAS 144 are effective for financial statements issued for fiscal years beginning after December 15, 2001. We are currently evaluating the expected impact of the adoption of SFAS 144 on our financial condition and results of operations and will be adopting SFAS 144 in the first quarter of fiscal 2003.

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Cautionary Statement and Risk Factors

Safe Harbor Statement under the Securities Litigation Reform Act of 1995: We make statements in this report that are considered forward-looking statements under federal securities laws. Such forward-looking statements are based on the beliefs of management as well as assumptions made by and information currently available to them. The words "expect," "anticipate," "believe," "may," "estimate," "intend" and similar expressions are intended to identify such forward looking statements. Forward- looking statements involve risks, uncertainties and assumptions including, but not limited to, the following:

The market for interactive entertainment software titles is characterized by short product life cycles. The interactive entertainment software market is characterized by short product life cycles and frequent introduction of new products. New products introduced by us may not achieve significant market acceptance or achieve sufficient sales to permit us to recover development, manufacturing and associated costs. Historically, few interactive entertainment software products have achieved sustained market acceptance. Even the most successful titles remain popular for only limited periods of time, often less than six months. The life cycle of a game generally consists of a relatively high level of sales during the first few months after introduction followed by a decline in sales. Because revenues associated with the initial shipments of a new product generally constitute a high percentage of the total revenues associated with the life of a product, any delay in the introduction of one or more new products could harm our operating results. Additionally, because we introduce a relatively limited number of new products in a given period, the failure of one or more of our products to achieve market acceptance could result in losses.

A significant portion of our revenues are derived from a limited number of titles. Our ten best selling titles accounted for approximately 31.3% of our revenues for the year ended October 31, 2001. For this period, Grand Theft Auto 3 for the PlayStation 2 accounted for 7.4% of our revenues; Midnight Club for the PlayStation 2 accounted for 4.1% of our revenues; Smuggler's Run for the PlayStation 2 accounted for 3.0% of our revenues; and Max Payne for the PC accounted for 5.2% of our revenues, with each of the next three titles accounting for between 1.9% and 3.0% of our revenues. Our ten best selling titles accounted for 16.4% of our revenues for the year ended October 31, 2000. Each of Grand Theft Auto and the Smuggler's Run titles accounted for approximately 3.0% of our revenues for the year ended October 31, 2000, with each of the next four titles accounting for between 1.2% and 2.3% of our

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revenues. For the year ended October 31, 1999, our ten best selling titles accounted for approximately 33.5% of our revenues, with Grand Theft Auto products accounting for approximately 18.7% of our revenues. Our future titles may not be commercially viable. We also may not be able to release new titles within scheduled release times or at all. If we fail to continue to develop and sell new, commercially successful titles, our revenues and profits may decrease substantially and we may incur losses.

Our quarterly operating results may vary significantly, which could cause our stock price to decline. We have experienced and may continue to experience wide fluctuations in quarterly operating results. The interactive entertainment industry is highly seasonal, with sales typically higher during the fourth and first calendar quarters, due primarily to the increased demand for games during and immediately following the holiday buying season. Our failure or inability to introduce products on a timely basis to meet seasonal fluctuations in demand will harm our business and operating results. These fluctuations could also cause our stock price to decline. Other factors that cause fluctuations include delays in the introduction of new titles; the size and timing of product and corporate acquisitions; variations in sales of titles designed to operate on particular platforms; development and promotional expenses relating to the introduction of new titles, sequels or enhancements of existing titles; availability of hardware platforms; the timing and success of title introductions by our competitors; product returns; the accuracy of retailers' forecasts of consumer demand; and the timing of orders from major customers.

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Our expense levels are based, in part, on our expectations regarding future sales and therefore our operating results would be harmed by a decrease in sales or a failure to meet our sales expectations. The uncertainties associated with interactive entertainment software development, lengthy manufacturing lead times, production delays and the approval process for products by hardware manufacturers and other licensors make it difficult to predict the quarter in which our products will ship and therefore may cause us to fail to meet financial expectations. In future quarters our operating results may fall below the expectations of securities analysts and investors. In this event, the trading price of our common stock could significantly decline.

The interactive entertainment software industry is cyclical, and we may fail to anticipate changing consumer preferences. Our business is subject to all of the risks generally associated with the interactive entertainment software industry, which has been cyclical in nature and has been characterized by periods of significant growth followed by rapid declines. Our future operating results will depend on numerous factors beyond our control, including the popularity, price and timing of new software and hardware platforms being released and distributed by us and our competitors; international, national and regional economic conditions, particularly economic conditions adversely affecting discretionary consumer spending; changes in consumer demographics; the availability of other forms of entertainment; and critical reviews and public tastes and preferences, all of which change rapidly and cannot be predicted. In order to plan for acquisition and promotional activities, we must anticipate and respond to rapid changes in consumer tastes and preferences. A decline in the popularity of interactive entertainment software or particular platforms could cause sales of our titles to decline dramatically. The period of time necessary to develop new game titles, obtain approvals of manufacturers and produce CD-ROMs or game cartridges is unpredictable. During this period, consumer appeal of a particular title may decrease, causing sales to decline.

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Rapidly changing technology and platform shifts could hurt our operating results. The interactive entertainment industry in general is associated with rapidly changing technology, which often leads to software and platform obsolescence and significant price erosion over the life of a product. The introduction of new platforms and technologies can render existing software titles obsolete or unmarketable. We expect that as more advanced platforms achieve market acceptance, consumer demand for software for older platforms will decline. Obsolescence of software or platforms could leave us with increased inventories of unsold titles and limited amounts of new titles to sell to consumers, which would have a material adverse effect on our operating results. A number of software publishers who compete with us have developed or are currently developing software for use by consumers over the Internet. Future increases in the availability of such software or technological advances in such software or the Internet could result in a decline in platform-based software and impact our sales. Direct sales of software by major manufacturers over the Internet would materially adversely affect our distribution business.

Next-generation hardware platforms on which we have based our business strategy may not achieve significant market acceptance. Our software development efforts with respect to new hardware platforms may not lead to marketable titles or titles that generate sufficient revenues to recover their development, manufacturing and marketing costs, especially if a new hardware platform does not reach a significant level of market acceptance. This risk may increase in the future, as continuing increases in development costs require corresponding increases in revenues in order to maintain profitability.

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We have devoted and will continue to devote significant development and marketing resources on products designed for next-generation video game systems that have not yet achieved large installed bases. We released several titles for the PlayStation 2 and have additional titles under development for this platform. If PlayStation 2 does not continue to achieve wide acceptance by consumers or Sony is unable to ship a significant number of PlayStation 2 units in a timely fashion, or if the sale of our titles fails to meet our expectations, we will have spent substantial amounts for developing products for this platform without corresponding revenues, which could result in losses. We are also devoting development resources on products designed for Microsoft's Xbox and Nintendo's GameCube. If fewer than expected units of a new hardware platform are produced or shipped, or if such platforms do not achieve commercial success, we may experience lower than expected sales or losses for these platforms.

Our business is dependent on licensing and publishing arrangements with third parties. Our success depends on our ability to identify and develop new titles on a timely basis. We have entered into agreements with third parties to acquire the rights to publish and distribute interactive entertainment software. These agreements typically require us to make advance payments, pay royalties and satisfy other conditions. Our advance payments may not be sufficient to permit developers to develop new software successfully. In addition, software development costs, promotion and marketing expenses and royalties payable to software developers have increased significantly in recent years and reduce the potential profits derived from sales of our software. Future sales of our titles may not be sufficient to recover advances to software developers, and we may not have adequate financial and other resources to satisfy our contractual commitments. If we fail to satisfy our obligations under these license agreements, the agreements may be terminated or modified in ways that may be

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burdensome to us.

Returns of our published titles and markdown allowances may adversely affect our operating results. We are exposed to the risk of product returns and markdown allowances with respect to our customers. Although our distribution arrangements with retailers generally do not give them the right to return titles to us or to cancel firm orders, our arrangements with retailers for published titles require us to accept returns. We sometimes negotiate accommodations to retailers, including price discounts, credits and returns, when demand for specific titles falls below expectations. We establish a reserve for future returns and markdown allowances for published titles at the time of sales, based primarily on these return policies and historical return rates, and we report our revenues net of returns.

Decreased demand for products compatible with older hardware platforms may result in a higher level of markdown allowances. In addition, if new platforms or products do not achieve market acceptance, we may be required to grant markdown allowances to maintain our relationships with retailers and access to distribution channels. If return rates and markdown allowances for our published titles significantly exceed our reserves, our revenues will decline and we could incur losses.

The interactive entertainment software industry is highly competitive. We compete for both licenses to properties and the sale of interactive entertainment software with Sony, Nintendo, Microsoft and Sega, each of which is a large developer and marketer of software for its platforms. Sony and Nintendo currently dominate the industry and have the financial resources to withstand significant price competition and to implement extensive advertising campaigns, particularly for prime-time television spots. These companies may also increase their own software development efforts or focus on developing software products for third-party platforms.

We compete with domestic and international companies, large software companies and media companies. Many of our competitors have far greater financial, technical, personnel and other resources than we do, and many are able to carry larger inventories, adopt more aggressive pricing policies and make higher offers to licensors and developers for commercially desirable properties than we can. Competition in the entertainment software industry is based on product quality and features; brand name recognition; access to distribution channels; effectiveness of marketing; and price. Our titles also compete with other forms of entertainment such as motion pictures, television and audio and video cassettes featuring similar themes, online computer programs and forms of entertainment which may be less expensive or provide other advantages to consumers.

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Increased competition for limited shelf space and promotional support from retailers could affect the success of our business and require us to incur greater expenses to market our titles. Retailers have limited shelf space and promotional resources, and competition is intense among an increasing number of newly introduced interactive entertainment software titles for adequate levels of shelf space and promotional support. Competition for retail shelf space is expected to increase, which may require us to increase our marketing expenditures just to maintain current levels of sales of our titles. Competitors with more extensive lines and popular titles frequently have greater bargaining power with retailers. Accordingly, we may not be able to achieve the levels of promotional support and shelf space that such competitors receive.

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Rating systems for interactive entertainment software, potential legislation and consumer opposition could inhibit sales of our products. Trade organizations within the video game industry require interactive entertainment software publishers to provide consumers with information relating to graphic violence, profanity or sexually explicit material contained in software titles. Certain countries have also established similar rating systems as prerequisites for sales of interactive entertainment software in such countries. In some instances, we may be required to modify our products to comply with the requirements of such governmental entities, which could delay the release of those products in such countries. We recently discontinued making sales of Grand Theft Auto 3 in Australia for several weeks while we made certain content changes to this title to comply with applicable rating systems. We believe that we comply with such rating systems and display the ratings received for our titles.

Historically, our software titles received a rating of "G" (all ages) or "T" (age 13 and over), although most of our newer titles (including Grand Theft Auto 3, Max Payne and State of Emergency) have received a rating of "M" (age 18 and over). Certain retailers may decline to sell interactive entertainment software containing graphic violence or sexually explicit material, which may limit the potential market for our "M" rated products.

Several proposals have been made for federal legislation to regulate the interactive entertainment software, motion picture and recording industries, including a proposal to adopt a common rating system for interactive entertainment software, television and music containing violence and sexually explicit material and the Federal Trade Commission has adopted rules with respect to the marketing of such material to minors. Consumer advocacy groups have also opposed sales of interactive entertainment software containing graphic violence and sexually explicit material by pressing for legislation in these areas and by engaging in public demonstrations and media campaigns. If any groups were to target our "M" rated titles, we might be required to significantly change or discontinue a particular title, which in the case of our best selling titles could hurt our business. Additionally, in light of the events in September 2001, we revised content in certain of our products that we deemed inappropriate. Delays in the release of products as a result of inappropriate content could result in lost revenues.

We cannot publish our console titles without the approval of hardware manufacturers. We are required to obtain a license to develop and publish titles for each hardware console platform for which we develop and publish titles. Our existing hardware console platform licenses require that we obtain approval for the publication of new titles on a title-by-title basis. As a result, the number of titles we are able to publish for these hardware platforms, along with our ability to time the release of these titles and, accordingly, our revenues from titles for these hardware platforms, may be limited. If any manufacturer chooses not to renew or extend our license agreement at the end of its current term, or if the manufacturer were to terminate our license for any reason, we would be unable to publish additional titles for that manufacturer's hardware platform.

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License agreements relating to these rights generally extend for a term of three years. The agreements are terminable upon the occurrence of a number of factors, including: (1) breach of the agreement by us; (2) our bankruptcy or insolvency; or (3) our entry into a relationship with, or acquisition by, a competitor of the manufacturer. We cannot assure you that we will be able to

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obtain new or maintain existing licenses on acceptable terms, or at all.

We are dependent upon a license agreement with Sony to publish titles for PlayStation 2. The term of the license agreement expires in March 2003 and is automatically extended, unless terminated by one of the parties, for additional successive one-year terms. Termination of such agreement would seriously hurt our business.

Sony and Nintendo are the sole manufacturers of the titles we publish under license from them. Games for the Xbox must be manufactured by pre-approved manufacturers. Each platform license provides that the manufacturer may raise prices for the titles at any time and grants the manufacturer substantial control over the release of new titles. Each of these manufacturers also publishes software for its own platforms and manufactures titles for all of its other licensees and may choose to give priority to its own titles or those of other publishers if it has insufficient manufacturing capacity or if there is increased demand.

In addition, these manufacturers may not have sufficient production capacity to satisfy our scheduling requirements during any period of sustained demand. If manufacturers do not supply us with finished titles on favorable terms without delays, our operations would be materially interrupted, and we would be unable to obtain sufficient amounts of our product to sell to our customers. If we cannot obtain sufficient product amounts, our revenues will decline and we could incur losses.

We may not be able to protect our proprietary rights or avoid claims that we infringe on the proprietary rights of others. We develop proprietary software and have obtained the rights to publish and distribute software developed by third parties. We attempt to protect our software and production techniques under copyright, trademark and trade secret laws as well as through contractual restrictions on disclosure, copying and distribution. Interactive entertainment software is susceptible to unauthorized copying. Unauthorized third parties may be able to copy or to reverse engineer our software to obtain and use programming or production techniques that we regard as proprietary.

As the amount of interactive entertainment software titles in the market increases and the functionality of this software further overlaps, we believe that interactive entertainment software will increasingly become the subject of claims that such software infringes the copyrights or patents of others. From time to time, we receive notices from third parties alleging infringement of their proprietary rights. Although we believe that our software and technologies and the software and technologies of third-party developers and publishers with whom we have contractual relations do not and will not infringe or violate proprietary rights of others, it is possible that infringement of proprietary rights of others has or may occur. Any claims of infringement, with or without merit, could be time-consuming, costly and difficult to defend.

We are dependent on third-party software developers to complete many of our titles. We rely on third-party software developers for the development of a significant number of our titles. Quality third-party developers are continually in high demand. Software developers who have developed titles for us in the past may not be available to develop software for us in the future. Due to the limited number of third-party software developers and the limited control that we exercise over them, these developers may not be able to complete titles for us on a timely basis or within acceptable quality standards, if at all.

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We depend on third-party software developers and our internal development studios to develop new interactive entertainment software within anticipated release schedules and cost projections. In addition, the development cycle for new titles is long, typically ranging from twelve to twenty-four months. After development of a product, it may take between six to twelve additional months to develop the product for other hardware platforms. If developers experience financial difficulties, additional costs or unanticipated development delays, we will not be able to release titles according to our schedule.

Our software is susceptible to errors, which can harm our financial results and reputation. The technological advancements of new hardware platforms allow more complex software products. As software products become more complex, the risk of undetected errors in products when first introduced increases. If, despite testing, errors are found in new products or releases after shipments have been made, we could experience a loss of or delay in timely market acceptance, product returns, loss of revenues and damage to our reputation.

The costs of developing and marketing products for new interactive entertainment hardware platforms may be substantial and could harm our operating results. We anticipate that it will be more costly to develop titles for new hardware platforms and believe the costs of developing and publishing titles for these hardware platforms will require greater financial and technical resources than prior development and publishing efforts. Additionally, during periods of new technology and platform introductions, forecasting our revenues and earnings is more difficult than in more stable or rising product markets.

Our distribution business is subject to intense competition. Our distribution business operates in a highly competitive environment. The intense competition that characterizes our industry is based primarily on breadth, availability and quality of product lines; price; terms and conditions of sale; credit terms and availability; speed and accuracy of delivery; and effectiveness of sales and marketing programs. Our competitors include regional, national and international distributors, as well as hardware manufacturers and software publishers. We may lose market share or be forced in the future to reduce our prices in response to the actions of our competitors, and thereby experience a reduction in our gross margins.

Gross margins relating to our distribution business have been historically narrow which increases the impact of variations in costs on our operating results. As a result of intense price competition in the console hardware and software distribution industry, our gross margins in our distribution business have historically been narrow and we expect them to continue to be narrow in the future. We receive purchase discounts from suppliers based on various factors, including volume purchases. These purchase discounts directly affect our gross margins. It may become more difficult for us to achieve the percentage growth in sales required to continue to receive volume purchase discounts.

A significant percentage of our revenues relates to products sold to us by relatively few manufacturers or publishers. They each have the ability to make rapid and significantly adverse changes in their sales terms and conditions, such as reducing the amount of price protection and return rights as well as reducing the level of purchase discounts they make available to us. Our inability to pass through to our customers the impact of these changes could have a negative impact on our gross margins. A decline in gross margins could have a material adverse effect on our business and could result in losses.

We may not be able to adequately adjust our cost structure in a timely fashion in response to a sudden decrease in demand. A significant portion of our selling and general and administrative expense is comprised of personnel,

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facilities and costs of invested capital. In the event of a significant decline in revenues, we may not be able to exit facilities, reduce personnel, or make other significant changes to our cost structure without significant disruption to our operations or without significant termination and exit costs. Management may not be able to implement such actions, if at all, in a timely manner to offset an immediate shortfall in revenues and gross profit.

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Our distribution business is dependent on suppliers to maintain an adequate supply of products to fulfill customer orders on a timely basis. Our ability to obtain particular products in required quantities and to fulfill customer orders on a timely basis is critical to our success. In most cases, we have no guaranteed price or delivery agreements with suppliers. In certain product categories, limited price protection or return rights offered by manufacturers may have a bearing on the amount of product we may be willing to purchase. The console hardware industry experiences significant product supply shortages from time to time due to the inability of certain manufacturers to supply certain products on a timely basis. As a result, we have experienced, and may in the future continue to experience, short-term hardware inventory shortages. In addition, manufacturers who currently distribute their products through us may decide to distribute, or to substantially increase their existing distribution, through other distributors, or directly to retailers. In the case of software, alternative means of distribution have emerged, such as electronic distribution. We cannot assure you that suppliers will be able to maintain an adequate supply of products to fulfill our customer orders on a timely basis or that we will be able to obtain particular products or that products currently offered by suppliers will continue to be available.

We are subject to the risk that our inventory values may decline and protective terms under supplier arrangements may not adequately cover the decline in values. The interactive entertainment software and hardware industry is subject to rapid technological change, new and enhanced generations of products, and evolving industry standards. These changes may cause inventory to decline substantially in value or to become obsolete. We are also exposed to inventory risk to the extent that supplier price protections are not available on all products or quantities and are subject to time restrictions. In addition, suppliers may become insolvent and unable to fulfill price protection obligations.

We rely on arrangements with independent shipping companies for the delivery of our products. The termination of our arrangements with one or more of these independent shipping companies, or the failure or inability of one or more of these independent shipping companies to deliver products from suppliers to us or products from us to our customers on a timely basis could adversely affect our results of operations.

Our rapid expansion and acquisitions may strain our operations. We have expanded through internal growth and acquisitions, which have placed and may continue to place a significant strain on our management, administrative, operational, financial and other resources. We have released a significant number of titles on new platforms, expanded our publishing and distribution operations, increased our advances to developers and payments to manufacturers, enlarged our work force and expanded our presence in international markets. To successfully manage this growth, we must continue to implement and improve our operating systems as well as hire, train and manage a substantial and increasing number of management, technical, marketing, administrative and other personnel. We may be unable to effectively manage expanded operations that are

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geographically dispersed.

A limited number of customers may account for a significant portion of our sales. Sales to our five largest customers accounted for approximately, 20.9% of our revenues for the year ended October 31, 2001, 22.7% of our revenues for the year ended October 31, 2000 and 24.6% of our revenues for the year ended October 31, 1999. Our customers may terminate their relationship with us at any time. The loss of our relationships with principal customers or a decline in sales to principal customers could harm our operating results. Bankruptcies or consolidations of certain large retail customers could also hurt our business.

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We have significant debt obligations. We have historically incurred substantial indebtedness in order to finance our operations. As of October 31, 2001, \$48,701,000 was outstanding under a line of credit agreement entered into with a group of lenders led by Bank of America, N.A., as agent. This line of credit was recently amended to provide for borrowings of up to \$15,000,000 through February 20, 2002; \$22,500,000 through February 28, 2002; \$30,000,000 through April 13, 2002; and \$50,000,000 through December 7, 2002. Borrowings under the line of credit are collateralized by our accounts receivable, inventory, equipment, general intangibles, securities and other personal property, including the capital stock of our domestic subsidiaries. The loan agreement contains certain financial and other covenants, which were retroactively amended. Accordingly, we are in compliance with such covenants as amended. The loan agreement limits or prohibits us, subject to certain exceptions, from declaring or paying cash dividends, merging or consolidating with another corporation, selling assets (other than in the ordinary course of business), creating liens and incurring additional indebtedness. If we default on our obligations, the banks could elect to declare our indebtedness to be due and payable and foreclose on our assets. Our UK subsidiary also had outstanding indebtedness of \$5,372,000 at October 31, 2001.

We are subject to credit and collection risks. Our sales are typically made on credit, with terms that vary depending upon the customer and the demand for the particular title being sold. We do not hold any collateral to secure payment by our customers. As a result, we are subject to credit risks, particularly in the event that any of our receivables represent sales to a limited number of retailers or are concentrated in foreign markets. If we are unable to collect on accounts receivable as they become due and such accounts are not covered by insurance, it could adversely affect our financial condition. Our accounts receivable, less an allowance for doubtful accounts and product returns, at October 31, 2001 were \$94,950,000.

We are subject to risks and uncertainties of international trade. Sales in international markets, primarily in the United Kingdom and other countries in Europe and the Pacific Rim, have accounted for a significant portion of our revenues. Sales in international markets accounted for approximately 23.6% of our revenues for the year ended October 31, 2001, 28.4% of our revenues for the year ended October 31, 2000 and 33.0% of our revenues for the year ended October 31, 1999. 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 impact on our operating results. All of our international sales are made in local currencies. For the year ended October 31, 2001, our foreign currency translation adjustment loss was \$767,000. We purchase currency forward contracts to a limited extent to seek to minimize our exposure to fluctuations in foreign currency exchange rates.

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Litigation. Several class action lawsuits have been filed against us. These lawsuits can be costly to defend and can distract management's time from our operations. An unfavorable resolution of these actions could have a material adverse effect on our financial condition and results of operations.

Item 7A. Quantitative and Qualitative Disclosures About Market Risk

We are subject to market risks in the ordinary course of our business, primarily risks associated with interest rate and foreign currency fluctuations. Historically, fluctuations in interest rates have not had a significant impact on our operating results. At October 31, 2001, we had \$54,073,000 in outstanding variable rate indebtedness. A hypothetical 1% increase in the interest rate of our variable rate debt would increase annual interest expense by approximately \$541,000 as of October 31, 2001.

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We transact business in foreign currencies and are exposed to risk 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 fiscal quarter or year end. Translation adjustments are included within accumulated other comprehensive income as a separate component of stockholders' equity. For the year ended October 31, 2001, our foreign currency translation loss was \$767,000. A hypothetical 10% change in applicable currency exchange rates at October 31, 2001 would result in a material translation adjustment. We purchase currency forward contracts to a limited extent to seek to minimize our exposure to fluctuations in foreign currency exchange rates. We had no outstanding contracts as of October 31, 2001.

In addition, we may be exposed to risk of loss associated with fluctuations in the value of our investments. Our investments are stated at fair value, with net unrealized appreciation and loss included within accumulated other comprehensive income as a separate component of stockholders' equity. We regularly review the carrying values of our investments to identify and record impairment losses when events or circumstances indicate that such investments may be other than temporarily impaired.

In fiscal 2001, we recorded a loss of \$19,171,000 to reflect an other than temporary impairment of our investment relating to Gameplay. At October 31, 2001, we held 6,869,000 shares of common stock of Gameplay.com plc with a fair value of approximately \$75,000 which was recorded as non-current.

In fiscal 2001, we recorded a loss of \$2,000,000 to reflect an other than temporary impairment of our investment relating to eUniverse Inc. At October 31, 2001, we held 2,269,333 shares of eUniverse with fair value of approximately \$6,241,000, all of which was recorded as current. We recorded an unrealized gain of \$157,000, net of tax of \$96,000, within accumulated other comprehensive income (loss) as a separate component of stockholders' equity.

Item 8. Financial Statements.

The financial statements appear in a separate section of this report following Part III.

Item 9. Changes in and Disagreements with Accountants on Accounting and

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Financial Disclosure.

Not applicable.

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PART III

Item 10. Directors and Executive Officers of the Registrant.

Ryan A. Brant, age 30, has been our Chairman since 1993. Mr. Brant served as our Chief Executive Officer from 1993 until February 2001. Mr. Brant received a B.S. degree in Economics from the University of Pennsylvania's Wharton School of Business.

Kelly Sumner, age 40, has been our Chief Executive Officer since February 2001 and a director since December 1997. Mr. Sumner was President of Take-Two Interactive Software Europe Limited, our subsidiary, from July 1997 until February 2001. From April 1993 to July 1997, Mr. Sumner was President and Chief Operating Officer of Gametek, Inc. From June 1979 to April 1993, Mr. Sumner held various positions, most recently as Managing Director, of the UK subsidiary of Commodore Business Machines.

Paul Eibeler, age 46, has been our President since July 2000 and a director since December 2000. Prior to joining us, Mr. Eibeler was a consultant to Microsoft's Xbox launch team, as well as W-Trade, Inc., an online financial services provider, and Essential Realities, Inc. From 1998 to 1999, Mr. Eibeler served as Acclaim Entertainment's Executive Vice-President and General Manager. During the seven years prior to that, Mr. Eibeler held various executive positions with Impact, Inc., a leading supplier of licensed toys and school supplies. Mr. Eibeler received a B.A. degree from Loyola College in 1978.

Don Leeds, age 51, has been our Executive Vice President/Special Projects since February 2002 and a director since October 2000. Mr. Leeds has been President and Chief Executive Officer of Ultimate Health Media, LLC, a private health products and services company, from May 2000 to February 2002. From June 1996 to January 2000, Mr. Leeds was President and director of Youth Stream Media Networks, Inc., a company engaged in providing college-based media and marketing services. Prior to this, from February 1989 to May 1996, Mr. Leeds was a Managing Director of Veronis, Suhler & Associates, Inc., an investment bank focused on media, marketing and publishing companies.

Oliver R. Grace, Jr., age 47, has been a director since April 1997. Mr. Grace, a private investor, has been the Chairman of the Board of Andersen Group, Inc., a dental products and video broadcasting equipment manufacturing company, since 1990. Mr. Grace has also been a director of Republic Automotive Parts, Inc., a distributor of replacement parts for the automotive aftermarket, since 1982. Mr. Grace is a general partner of Anglo American Security Fund, L.P., a private investment fund.

Robert Flug, age 53, has been a director since February 1998. Mr. Flug has been the President and Chief Operating Officer of S.L. Danielle, a women's apparel company, since September 1987. Mr. Flug received a B.S. in Business Administration from New York University.

Mark Lewis, age 51, has been a director since May 2001. For the past fifteen years and until February 2001, Mr. Lewis held various positions with Electronic Arts, most recently as Senior Vice President of International Operations. Mr. Lewis has been a director of Muse Communications Corp., a

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broadband technology company, since November 1997.

Todd Emmel, age 39, has been a director and the Chairman of our Audit Committee since February 2002. Since November 1999, Mr. Emmel has been a First Vice President at Ambac Assurance Corporation, a financial insurance company. From May 1999 to November 1999, Mr. Emmel was Chief Credit Officer at Structured Credit Partners, a private credit arbitrage firm. From March 1998 to May 1999, Mr. Emmel was a Managing Director of DVI Private Capital Group, a private equity fund. From April 1990 to March 1998, Mr. Emmel held various positions at Union Bank of Switzerland, most recently as a Managing Director. Prior to this, Mr. Emmel was an Associate at both Drexel Burnham Lambert, from June 1988 to February 1990, and at E.F. Hutton from July 1987 to February 1988. Mr. Emmel received an M.B.A. from Carnegie Mellon University and a B.S. in accounting from Miami University.

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Karl H. Winters, age 43, has been our Chief Financial Officer since February 2002. From April 2000 to June 2001, Mr. Winters was the Chief Financial Officer of ModelWire, Inc., a company engaged in marketing imaging database products. From September 1993 to December 1999, Mr. Winters served in various positions, most recently as Vice President of Trace International Holdings, Inc., a private holding company that held significant interests in United Auto Group, Inc., a consolidator of new car dealerships, and Foamex International Inc., a manufacturer of polyurethane products. From 1993 to 1999, Mr. Winters held executive positions at United Auto and Foamex, most recently as United Auto's Chief Financial Officer and Executive Vice President. Trace International filed a petition under Chapter 11 of the United States Bankruptcy Code in July 1999. From 1983 to 1993, Mr. Winters was a Senior Audit Manager for Coopers & Lybrand. Mr. Winters is a C.P.A. and received an M.B.A. from the University of Michigan and a B.A. in business economics with a concentration in accounting from Calvin College.

Patti P. Tay, age 32, has been our Chief Accounting Officer since February 2002 and Controller since May 1998. Ms. Tay served as a Staff Accountant at KPMG Peat Marwick, LLP from September 1996 to May 1998, and at Salibello & Broder, CPA from May 1995 to September 1996. Prior to this, Ms. Tay was an Auditor at Broadcast Music Inc. from September 1993 to May 1995. Ms. Tay is a C.P.A. and received a B.A. in accounting from Brooklyn College.

Our directors are elected at the annual meeting of stockholders to hold office until the annual meeting of stockholders for the ensuing year or until their successors are elected and qualified.

Officers are elected annually by our directors and serve at the discretion of the Board.

Based solely on a review of Forms 3, 4 and 5 furnished to us with respect to our most recent fiscal year, we believe that all reporting persons currently required to file forms under the Securities Exchange Act of 1934 filed such reports, except that Mr. Brant did not file a Form 4 (one transaction) and Form 5 (two transactions) on a timely basis.

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Item 11. Executive Compensation.

The following table sets forth the cash compensation paid by us during the fiscal years ended October 31, 2001, 2000 and 1999 to our Chief Executive Officer and our four most highly compensated executive officers other than our

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Chief Executive Officer, each of whom was serving at the end of the fiscal year ended October 31, 2001 and whose salary and bonus exceeded \$100,000 (the "Named Executives"):

Summary Compensation Table

Name and Principal Position -----	Year Ended October 31, ---	Annual Compensation		Other Compen -----
		Salary (\$)	Bonus (\$)	
Ryan A. Brant Chairman.....	2001	575,000	790,000	
	2000	344,365	705,812	
	1999	243,873	516,130	
Kelly Sumner Chief Executive Officer.....	2001	359,519	19,317	
	2000	255,702	147,862	
	1999	230,892	120,269	
Paul Eibeler President.....	2001	353,819	95,000	
	2000	80,208	70,000	
Larry Muller Vice President of Operations (2).....	2001	272,083	225,000	
	2000	256,077	133,629	
	1999	215,077	200,808	
Barry S. Rutcofsky Executive Vice President (3).....	2001	271,814	60,000	
	2000	251,346	155,000	
	1999	47,743	---	
James H. David Jr. (4).....	2001	233,000	230,915 (5)	
	2000	105,000	15,000	

(1) The aggregate value of benefits to be reported under the "Other Annual Compensation" column did not exceed the lesser of \$50,000 or 10% of the total of annual salary and bonus reported for the Named Executives.

(2) Mr. Muller is no longer employed by us.

(3) Mr. Rutcofsky became Executive Vice President of Mergers and Acquisitions, a non executive officer position, in May 2001.

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(4) Mr. David is no longer employed by us.

(5) Includes the cash value of approximately \$142,300 of shares of our common

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stock.

The following table sets forth information concerning options granted in the fiscal year ended October 31, 2001 to the Named Executives:

Option Grants in Fiscal Year Ended October 31, 2001

Individual Grants				
Name	Number of Securities Underlying Options Granted (#)	Percent of Total Options Granted to Employees in Fiscal Year (%)	Exercise Price (\$/Sh)	Expiration Date
Ryan A. Brant	279,560		8.625	11/27/01
	200,000	12.5	13.91	4/30/02
Kelly Sumner	25,000		12.375	10/30/01
	250,000		9.1562	12/19/01
	105,000		8.625	11/27/01
	100,000	12.5	13.91	4/30/02
Paul Eibeler.....	15,000		10.90	11/16/01
	40,000		10.00	11/27/01
	100,000		10.1875	7/20/01
	15,000	4.4	11.875	2/19/02
Larry Muller.....	25,000		10.90	11/16/01
	25,000		11.4875	2/19/02
	300,000	9.1	7.00	9/30/01
Barry S. Rutcofsky ...	50,000	1.3	13.00	5/3/01
James H. David Jr.	65,000		8.625	11/27/01
	20,000	2.2	13.91	4/30/02

(1) The potential realizable value columns of the table illustrate values that might be realized upon exercise of the options immediately prior to their expiration, assuming the common stock appreciates at the compounded rates specified over the term of the options. These numbers do not take into account provisions of certain options providing for termination of the option following termination of employment or non-transferability of the options and do not make any provision for taxes associated with exercise. Because actual gains will depend upon, among other things, future performance of the common stock, there can be no assurance that the amounts reflected in this table will be achieved.

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The following table sets forth information concerning the value of options exercised during the fiscal year ended October 31, 2001 and the value of

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unexercised stock options held by the Named Executives as of October 31, 2001:

Aggregated Option Exercises and Year End Values				
Name -----	Shares Acquired on Exercise (#) -----	Value Realized (\$) -----	Number of Securities Underlying Unexercised Options at October 31, 2001 (#)	
			Exercisable -----	Unexercisable -----
Ryan A. Brant.....	263,191	4,451,356	--	--
Kelly Sumner.....	124,400	1,376,890	382,500	277,500
Paul Eibeler.....	90,000	1,222,074	209,999	145,001
Larry Muller.....	106,666	1,097,638	108,855	250,000
Barry S. Rutcofsky.....	110,000	999,500	166,666	33,334
James H. David Jr.....	50,000	582,750	50,834	34,116

*Year-end values for unexercised in-the-money options represent the positive spread between the exercise price of such options and the fiscal year-end market value of the common stock, which was \$13.93 on October 31, 2001.

Director Compensation

Non-employee directors currently receive cash compensation of \$20,000 per annum for serving on the Board of Directors. Non-employee directors are also eligible to receive options under the 1997 Stock Option Plan. During fiscal 2001, Mr. Leeds received options to purchase 30,000 shares, and each of Messrs. Grace, Flug and Lewis received options to purchase 50,000 shares.

Employment Agreements

We entered into an employment agreement, as amended, with Ryan A. Brant for a five-year term commencing August 2000. The Agreement provides that Mr. Brant is entitled to receive an annual salary of \$600,000 and a bonus based on our financial performance.

We entered into an employment agreement with Kelly Sumner for a three-year term commencing February 2001. The agreement provides that Mr. Sumner is entitled to an annual salary of \$425,000 and a bonus based on our financial performance.

We entered into an employment agreement, as amended, with Paul Eibeler for a three-year term commencing July 2000. The agreement provides that Mr. Eibeler is entitled to receive an annual salary of \$375,000 and a bonus based on our financial performance.

We entered into an employment agreement with Karl H. Winters for a three-year term commencing February 2002. The agreement provides that Mr.

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Winters is entitled to an annual salary of \$300,000 and a bonus based on Mr. Winter's performance in implementing certain objectives of the Audit Committee of the Board of Directors. Mr. Winters was also granted options to purchase 200,000 shares of common stock.

We entered into an employment agreement with Mr. Leeds for a three-year term commencing February 2002. The agreement provides that Mr. Leeds is entitled to receive an annual salary of \$350,000 and such bonus as may be determined at the discretion of the Board. Mr. Leeds was also granted options to purchase 400,000 shares of common stock.

The employment agreements provide that if the employment agreement is terminated under certain circumstances, including in the event of a change of control, the executive will be entitled certain severance compensation. The employment agreements also contain confidentiality and non-competition provisions.

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Item 12. Security Ownership of Certain Beneficial Owners and Management.

The following table sets forth certain information as of February 22, 2002, relating to the beneficial ownership of shares of our common stock by (i) each person or entity who is known by us to own beneficially 5% or more of the outstanding common stock, (ii) each of our directors, (iii) each of the Named Executives currently serving and (iv) all directors and executive officers as a group.

Name and Address of Beneficial Owner(1) -----	Number of Shares of Common Stock Beneficially Owned(2) -----	Percentage Comm Benefic -----
FMR Corp (3).....	5,494,650	
Waddell & Reed Financial Services, Inc. (3).....	2,199,300	
Kern Capital Management, LLC (3).....	2,159,300	
Oliver R. Grace, Jr. (4).....	704,279	
Kelly Sumner (5).....	490,000	
Ryan A. Brant	328,729	
Paul Eibeler (6).....	367,500	
Robert Flug (7).....	99,600	
Don Leeds (8).....	94,900	
Mark Lewis (9).....	50,000	
Todd Emmel (10).....	20,000	
All directors and executive officers as		

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a group (ten persons) (11)..... 2,244,493

* Less than 1%.

- (1) Unless otherwise indicated, the address of each beneficial owner is Take-Two Interactive Software, Inc., 575 Broadway, New York, New York 10012.
- (2) Unless otherwise indicated, we believe that all persons named in the table have sole voting and investment power with respect to all shares beneficially owned by them. A person is deemed to be the beneficial owner of securities that may be acquired by such person within 60 days from the date of this report upon the exercise of options. Each beneficial owner's percentage ownership is determined by assuming that options that are held by such person (but not those held by any other person) and which are exercisable within 60 days of the date of this report, have been exercised.

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- (3) Based on Schedules 13G filed with the Securities and Exchange Commission as of December 31, 2001.
- (4) Includes: (i) 591,705 shares owned of record by Anglo American Security Fund, L.P., of which Mr. Grace is a general partner (ii) 62,574 shares owned by trusts of which Mr. Grace is a possible beneficiary and (iii) options to purchase 50,000 shares held by Mr. Grace.
- (5) Includes 485,000 shares issuable upon the exercise of options.
- (6) Includes 355,000 shares issuable upon the exercise of options.
- (7) Includes 39,600 shares held by S.L. Danielle, Inc. and 60,000 shares of Common Stock issuable upon the exercise of options.
- (8) Includes 92,500 shares issuable upon the exercise of options.
- (9) Represents 50,000 shares issuable upon the exercise of options.
- (10) Represents 20,000 shares issuable upon the exercise of options.
- (11) Includes 1,152,166 shares issuable upon the exercise of options.

Item 13. Certain Relationships and Related Transactions.

Our principal executive and administrative office, located at 575 Broadway, New York, New York, is approximately 13,300 square feet of office space under a five-year lease with 575 Broadway Corporation, a company controlled by the father of Ryan A. Brant, our Chairman. We pay rent of \$474,000 per annum under this lease. We believe that the terms of the lease are no less favorable than those that could have been obtained from an unaffiliated party.

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Item 14. Exhibits, Financial Statement Schedules and Reports on Form 8-K.

- (a) Exhibits

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- 3.1 Form of Restated Certificate of Incorporation of the Company. (1)
- 3.2 Amendment to Restated Certificate of Incorporation. (1)
- 3.3 By-Laws of the Company. (1)
- 10.1 1997 Stock Option Plan of the Company. (1)
- 10.2 Credit Agreement (the "Credit Agreement"), dated December 7, 1999, by and among the Company, certain of its subsidiaries, certain lenders and Bank of America, N.A., as Agent. (2)
- 10.3 Amendment to Credit Agreement. (4)
- 10.4 Loan Agreement with Lloyds TBS Commercial and Take-Two Interactive Software Europe Ltd. (4)
- 10.5 Employment Agreement, dated July 21, 2000, as amended, by and between the Company and Paul Eibeler. (4)
- 10.6 Employment Agreement dated February 15, 2001 by and between the Company and Kelly Sumner. (4)
- 10.7 Employment Agreement dated February 15, 2002 by and between the Company and Karl H. Winters.
- 10.8 Employment Agreement dated February 15, 2002 by and between the Company and Don Leeds.
- 10.9 Employment Agreement dated August 1, 1998, as amended, by and between the Company and Ryan A. Brant. (5)
- 10.10 Licensed Publishing Agreement dated April 1, 2000 between Sony Computer Entertainment America, Inc. and the Company. (3) *
- 10.11 Publishing Agreement dated May 8, 1998 between Gathering of Developers I, Ltd. and Apogee Software, Ltd/ 3D Realms. (3) *
- 10.12 Xbox Publisher License Agreement dated December 14, 2000 between Microsoft Corporation and the Company. (4) *
- 10.13 Confidential License Agreement for Nintendo GameCube dated September 24, 2001 between Nintendo of America Inc. and the Company. (4) *
- 21.1 Subsidiaries of the Company. (4)
- 23.1 Consent of PricewaterhouseCoopers LLP.

* 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

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(1) Incorporated by reference to the applicable exhibit contained in the Company's Registration Statement on Form SB-2 (File no. 333-6414).

(2) Incorporated by reference to the applicable exhibit contained in the Company's Annual Report on Form 10-K for the year ended October 31, 1999.

(3) Incorporated by reference to the applicable exhibit contained in the Company's Registration Statement on Form S-3 (File No. 333-66748).

(4) Previously filed with the Company's Annual Report on Form 10-K for the year ended October 31, 2001.

(5) August 1, 1998 agreement incorporated by reference to the applicable exhibit contained in the Company's Registration Statement on Form S-1 (File No. 333-748851).

(b) Financial Statement Schedules: Schedule II-Valuation and Qualifying Accounts.

(c) Reports on Form 8-K filed during the quarter ended October 31, 2001: None

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TAKE-TWO INTERACTIVE SOFTWARE, INC. YEAR ENDED OCTOBER 31, 2001

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Report of Independent Accountants

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To the Board of Directors and
Shareholders of Take-Two Interactive Software, Inc.

In our opinion, the accompanying consolidated balance sheets and the related consolidated statements of operations, cash flows and stockholders' equity listed in the accompanying index present fairly, in all material respects, the financial position of Take Two Interactive Software, Inc. and its subsidiaries ("the Company") at October 31, 2001 and October 31, 2000, and the results of their operations and their cash flows for each of the three years in the period ended October 31, 2001 in conformity with accounting principles generally accepted in the United States of America. In addition, in our opinion, the financial statement schedule listed in the accompanying index present fairly, in all material respects, the information set forth therein when read in conjunction with the related consolidated financial statements. These financial statements and financial statement schedule are the responsibility of the Company's management; our responsibility is to express an opinion on these financial statements and financial statement schedule based on our audits. We conducted our audits of these statements in accordance with auditing standards generally accepted in the United States of America, which require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements, assessing the accounting principles used and significant estimates made by management, and evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

As discussed in Note 2 to the consolidated financial statements, the Company restated its financial statements for the year ended October 31, 2000.

As discussed in Note 3 to the consolidated financial statements, effective November 1, 2000, the Company changed its method of accounting for revenue recognition to conform to the requirements of SEC Staff Accounting Bulletin No. 101 Revenue Recognition.

/s/ PricewaterhouseCoopers LLP
New York, New York
February 11, 2002

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TAKE-TWO INTERACTIVE SOFTWARE, INC. and SUBSIDIARIES
Consolidated Balance Sheets
(In thousands, except share data)

	October 31, 2001	October Restated
ASSETS:		
Current assets:		
Cash and cash equivalents	\$ 6,056	\$
Accounts receivable, net of provision for doubtful accounts and sales allowances of \$26,106 and \$11,615 at October 31, 2001 and 2000, respectively	94,950	11
Inventories, net	61,937	5

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Prepaid royalties	21,892	2
Prepaid expenses and other current assets	17,925	1
Investments	6,241	
Deferred tax asset	13,873	
	-----	-----
Total current assets	222,874	21
Property and equipment, net	11,033	
Prepaid royalties	11,097	
Capitalized software development costs, net	11,934	
Investments	75	2
Intangibles, net	88,175	6
Deferred tax asset	7,892	
Other assets	1,917	
	-----	-----
Total assets	\$ 354,997	\$ 33
	=====	=====
LIABILITIES and STOCKHOLDERS' EQUITY:		
Current liabilities:		
Accounts payable	\$ 60,223	\$ 4
Accrued expenses and other current liabilities	20,250	1
Lines of credit	54,073	8
Current portion of capital lease obligation	99	
	-----	-----
Total current liabilities	134,645	14
Capital lease obligation, net of current portion	291	
Loan payable, net of unamortized discount of \$2,732 at October 31, 2000	--	1
	-----	-----
Total liabilities	134,936	16
	-----	-----
Commitments and contingencies (See Note 14)		
Stockholders' equity		
Common stock, par value \$.01 per share; 50,000,000 shares authorized; 36,640,972, and 31,172,866 shares issued and outstanding at October 31, 2001 and 2000, respectively	366	
Additional paid-in capital	213,908	15
Deferred compensation	--	
Retained earnings	16,239	2
Accumulated other comprehensive loss	(10,452)	(1)
	-----	-----
Total stockholders' equity	220,061	17
	-----	-----
Total liabilities and stockholders' equity	\$ 354,997	\$ 33
	=====	=====

The accompanying notes are an integral part of these consolidated financial statements

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TAKE-TWO INTERACTIVE SOFTWARE, INC.
Consolidated Statements of Operations
(In thousands, except per share data)

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	Year

	2001

Net sales	\$ 451,056
Cost of sales (includes impairment charge on Internet gaming assets of \$3,786 for the year ended October 31, 2001)	306,264

Gross profit	144,792

Operating expenses:	
Selling and marketing (includes impairment charge on Internet gaming assets of \$401 for the year ended October 31, 2001)	55,253
General and administrative	44,867
Research and development costs	6,190
Depreciation and amortization	12,641
Abandoned offering costs	--

Total operating expenses	118,951

Income from operations	25,841
Non-operating expense (income):	
Interest expenses, net	8,510
Gain on sale of subsidiary	(651)
Loss on available-for-sale Internet securities	21,477
Equity in loss of affiliate	--

Total non-operating expense	29,336
(Loss) income before income taxes, extraordinary item and cumulative effect of change in accounting principle	(3,495)
(Benefit) provision for income taxes	(2,200)

(Loss) income before extraordinary item and cumulative effect of change in accounting principle	(1,295)
Extraordinary item, loss on early extinguishment of debt, net of taxes of \$1,217	1,948
Cumulative effect of change in accounting principle, net of taxes of \$3,558	5,337

Net (loss) income	\$ (8,580)
	=====
Share data:	
Basic:	
Weighted average common shares outstanding	33,961
	=====
(Loss) income before extraordinary item and cumulative effect of change in accounting per share	\$ (0.04)
Extraordinary item per share	(0.06)
Cumulative effect of change in accounting principle per share	(0.16)

Net (loss) income - Basic	\$ (0.25)
	=====

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Diluted:

Weighted average common shares outstanding	33,961
(Loss) income before extraordinary item and cumulative effect of change in accounting per share	\$ (0.04)
Extraordinary item per share	(0.06)
Cumulative effect of change in accounting principle per share	(0.16)
Net (loss) income - Diluted	\$ (0.25)

The accompanying notes are an integral part of these consolidated financial statements.

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TAKE-TWO INTERACTIVE SOFTWARE, INC. and SUBSIDIARIES Consolidated Statements of Cash Flows

	Year
	2001
(In thousands)	
Cash flows from operating activities:	
Net (loss) income	\$ (8,580)
Adjustments to reconcile net income (loss) to net cash provided by (used in) operating activities:	
Depreciation and amortization	12,641
Loss on disposal of fixed assets	219
Gain on sale of subsidiary	(651)
Loss on available-for-sale Internet securities	21,477
Impairment charge on Internet assets	4,187
Stock received in consideration of license revenues	--
Equity in loss of affiliate	--
Extraordinary loss on early extinguishment of debt, net of taxes	1,948
(Benefit) provision for deferred taxes	(8,307)
Provision for doubtful accounts and sales allowances	14,491
Provision for Inventory obsolescence	108
Amortization of various expenses and discounts	2,134
Forfeiture of compensatory stock options in connection with AIM acquisition	--
Issuance of compensatory stock	--
Changes in assets and liabilities, net of acquisitions and disposals:	
Decrease (increase) in accounts receivable	7,325
Increase in inventories, net	(4,034)
Increase in prepaid royalties	(8,279)
Decrease in advances to developers	--
Increase in prepaid expenses and other current assets	(5,470)
(Increase) decrease in capitalized software development costs	(2,710)
(Increase) decrease in other non-current assets	(455)
Increase (decrease) in accounts payable	1,511
(Decrease) increase in accrued expenses and other current liabilities	(236)
Decrease in other liabilities	--
Net cash provided by (used in) operating activities	27,319
Cash flows from investing activities:	

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Purchases of fixed assets	(8,568)
Investment in affiliates	--
Other investment	--
Acquisitions, net of cash acquired	(1,769)
Acquisitions of intangible assets	(3,105)
Proceeds from disposal of a business	215
Additional cash paid for prior acquisition	(252)

Net cash used in investing activities	(13,479)

Cash flows from financing activities:	
Issuance of stock in connection with the secondary public offering, net of issuance costs of \$2,187	--
Proceeds from private placements	20,892
Net (repayments) borrowings under lines of credit	(40,545)
Financing costs	
(Repayment) proceeds from loan payable	(15,000)
Repayments of note payable	--
Proceeds from exercise of stock options and warrants	22,931
Repayments of capital lease obligation	(68)

Net cash (used in) provided by financing activities	(11,790)

Effect of foreign exchange rates on cash	(1,239)

Net increase (decrease) in cash for the period	811
Cash and cash equivalents, beginning of the period	5,245

Cash and cash equivalents, end of the period	\$ 6,056
	=====
Supplemental disclosure of non-cash investing activities:	
Issuance of common stock in connection with acquisitions	\$ 13,981
	=====
Equipment acquired under capital lease	\$ 21
	=====

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TAKE-TWO INTERACTIVE SOFTWARE, INC. and SUBSIDIARIES
Consolidated Statements of Cash Flows

(In thousands)

Year

2001

Supplemental information on businesses acquired:

Fair value of assets acquired

Cash

\$ 331

Current assets

10,417

Non current assets

770

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Investment (including prepaid purchase price for Neo)	--
Intangible assets	25,168
Less, liabilities assumed	
Current Liabilities	(25,809)
Stock and warrants issued	(8,611)
Options issued	--
Disposal adjustment	--
Direct transaction costs	(166)
Investment interest and purchase option	--

Cash paid	2,100
Less, cash acquired	(331)

Net cash paid	\$ 1,769
	=====
Supplemental information on businesses disposed:	
Current assets	\$ (318)
Non current assets	--
Current liabilities	754

Net liabilities (assets) disposed	436
Consideration received for business disposed:	
Stock	--
Cash	215

Gain on sale	\$ (651)
	=====
Cash paid during the year for interest	\$ 8,284
	=====
Cash paid during the year for taxes	\$ 9,793
	=====

The supplemental information on business acquired and disposed for the year ended October 31, 2000 are net of the Toga acquisition and disposal.
(See Note 4)

The accompanying notes are an integral part of the consolidated financial statements.

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TAKE-TWO INTERACTIVE SOFTWARE, INC. and SUBSIDIARIES
Consolidated Statements of Stockholders' Equity
For the years ended October 31, 1999, October 31, 2000 (restated) and
October 31, 2001

(In thousands)

	Common Stock	
	Shares	Amount
	-----	-----
Balance, November 1, 1998	18,072	\$

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Issuance of compensatory stock options and warrants	537
Proceeds from exercise of stock options and warrants	654
Amortization of deferred compensation	--
Forfeiture of compensatory stock options in connection with AIM acquisition	--
Issuance of common stock in connection with acquisitions	763
Issuance of common stock in connection with a public offering, net of issuance costs	3,005
Issuance of common stock in lieu of royalty payments	55
Tax benefit in connection with the exercise of stock options	--
Foreign currency translation adjustment	--
Net income	--

Balance, October 31, 1999	23,086
Proceeds from exercise of stock options and warrants	1,373
Amortization of deferred compensation	--
Issuance of common stock in connection with acquisitions	4,222
Issuance of common stock in connection with private placements, net of issuance costs	2,422
Issuance of warrant in connection with a debt financing	
Issuance of common stock in lieu of repayment of debt assumed from Pixel	168
Retirement of common stock	(98)
Tax benefit in connection with the exercise of stock options	--
Foreign currency translation adjustment	--
Net unrealized loss on investments net of taxes of \$1,736	--
Net income - Restated	--

Balance, October 31, 2000 (restated)	31,173
Proceeds from exercise of stock options and warrants	3,266
Amortization of deferred compensation	--
Issuance of common stock in connection with acquisitions	1,466
Issuance of common stock in connection with private placements, net of issuance costs	1,300
Retirement of common stock	(564)
Tax benefit in connection with the exercise of stock options	--

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Foreign currency translation adjustment	--	
Net unrealized gain on investments net of taxes of \$1,640	--	
Net loss	--	
	-----	-----
Balance, October 31, 2001	36,641	\$
	=====	=====

(In thousands)

	Retained Earnings (Deficit)	Accumul Othe Comprehe Inco (Los
	-----	-----
Balance, November 1, 1998	\$ 2,070	\$
Issuance of compensatory stock options and warrants	--	
Proceeds from exercise of stock options and warrants	--	
Amortization of deferred compensation	--	
Forfeiture of compensatory stock options in connection with AIM acquisition	--	
Issuance of common stock in connection with acquisitions	--	
Issuance of common stock in connection with a public offering, net of issuance costs	--	
Issuance of common stock in lieu of royalty payments	--	
Tax benefit in connection with the exercise of stock options	--	
Foreign currency translation adjustment	--	
Net income	16,332	
	-----	-----
Balance, October 31, 1999	18,402	
Proceeds from exercise of stock options and warrants	--	
Amortization of deferred compensation	--	
Issuance of common stock in connection with acquisitions	--	
Issuance of common stock in connection with private placements, net of issuance costs	--	
Issuance of warrant in connection with a debt financing	--	
Issuance of common stock in lieu of repayment of debt assumed from Pixel	--	
Retirement of common stock	--	
Tax benefit in connection with the exercise of stock options	--	

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Foreign currency translation adjustment	--	(9)
Net unrealized loss on investments net of taxes of \$1,736	--	(2)
Net income - Restated	6,417	
	-----	-----
Balance, October 31, 2000 (restated)	24,819	(12)
Proceeds from exercise of stock options and warrants	--	
Amortization of deferred compensation	--	
Issuance of common stock in connection with acquisitions	--	
Issuance of common stock in connection with private placements, net of issuance costs	--	
Retirement of common stock	--	
Tax benefit in connection with the exercise of stock options	--	
Foreign currency translation adjustment	--	
Net unrealized gain on investments net of taxes of \$1,640	--	2
Net loss	(8,580)	
	-----	-----
Balance, October 31, 2001	\$ 16,239	\$ (10)
	=====	=====

The accompanying notes are an integral part of these consolidated condensed financial statements.

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TAKE-TWO INTERACTIVE SOFTWARE, INC.
Notes to Consolidated Financial Statements

1. Description of the Business

Take-Two Interactive Software, Inc. (the "Company") was incorporated in the State of Delaware in September 1993. The Company develops interactive software games designed for PCs and video game console platforms and publishes games it and other parties develop. It also distributes games for PC's and video game consoles published by third parties.

2. Restatement of Financial Statements

The Company engaged outside Counsel to conduct an investigation into the Company's accounting treatment of certain transactions in fiscal 2000 and 2001. Counsel was assisted in its investigation by forensic accountants.

As a result of the investigation, the Company restated its previously issued consolidated financial statements for fiscal 2000 to eliminate

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\$15,367,000 of net sales made to independent third party distributors and the related cost of sales of \$8,702,000, which were improperly recognized as revenue since the products were later returned or repurchased by the Company.

In addition, the Company reviewed its revenue recognition policy, reserve policies and its accounting for certain other transactions. As a result of this review, the Company restated its previously issued consolidated financial statements for fiscal 2000 for the following transactions:

- o The elimination of \$3,780,000 of sales and related cost of sales of \$2,236,000 that were previously recognized for products that had not been shipped within the period.
- o A non-cash charge of \$19,206,000 to record the Company's portion of the losses incurred by an affiliate accounted for under the equity method in accordance with the provisions of EITF Issue No. 99-10 (see Note 7), and a relating net reduction for post acquisition amortization of \$710,000 after the Company acquired the remaining 80% interest in this entity (see Note 4).
- o The elimination of \$2,563,000 of license revenue in connection with a business combination (see Note 5).

The Company's 2000 financial statements have been restated as follows (presented in thousands, except per share data):

	Year ended October 31, 2000	
	----- As Reported	As Restated -----
Statement of Operations Data:		
Net sales *	\$ 387,006	\$ 364,001
Cost of sales *	\$ 247,796	\$ 235,978
Depreciation and amortization	\$ 9,805	\$ 8,680
Income from operations	\$ 45,061	\$ 33,309
Equity in loss of affiliate	\$ 763	\$ 19,969
Income before provision for income taxes	\$ 38,229	\$ 8,961
Provision for income taxes	\$ 13,266	\$ 2,544
Net income	\$ 24,963	\$ 6,417
Basic income per share	\$ 0.91	\$ 0.23
Diluted income per share	\$ 0.88	\$ 0.23

- * Restated amounts give effect to reclassification of certain amounts to conform to current year presentation including the reduction in net sales and costs of sales by approximately \$1.3 million.

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Notes to Consolidated Financial Statements

	October 31, 2000	
	----- As Reported	As Restated -----
Balance Sheet Data		
Accounts receivable*	\$134,877	\$110,783
Inventories*	\$ 44,922	\$ 53,798
Prepaid royalties - current	\$ 19,721	\$ 24,093
Deferred tax assets	\$ 666	\$ 9,243
Intangible assets	\$ 90,505	\$ 66,562
Other assets, net	\$ 1,565	\$ 2,558
Total assets	\$351,641	\$330,257
Accounts payable	\$ 47,972	\$ 46,566
Accrued expenses and other current liabilities*	\$ 19,357	\$ 16,189
Total liabilities	\$164,639	\$160,065
Retained earnings	\$ 43,365	\$ 24,819
Total liabilities and stockholders equity	\$351,641	\$330,257

* Restated amounts reflect a reclassification relating to the presentation of allowance for returns.

All applicable amounts relating to the aforementioned restatements have been reflected in these consolidated financial statements and notes thereto.

3. Significant Accounting Policies

Basis of Presentation

The consolidated financial statements include the financial statements of the Company and its wholly owned subsidiaries. All intercompany balances and transactions have been eliminated in consolidation.

Certain amounts in the financial statements of the prior years have been reclassified to conform to the current year presentation for comparative purposes.

Risks and Uncertainties

Substantially all of the Company's net sales are derived from software publishing and distribution activities, which are subject to increasing competition, rapid technological change and evolving consumer preferences, often resulting in the frequent introduction of new products and short product lifecycles. Accordingly, the Company's profitability and growth prospects depend upon its ability to continually acquire, develop and market new, commercially successful software products and obtain adequate financing, if required. If the Company fails to continue to acquire, develop and market commercially successful software products, its operating results, cash flows and financial condition could be materially adversely affected in the near future.

The preparation of financial statements in conformity with generally accepted accounting principles requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and the disclosure of contingent assets and liabilities at the dates of the financial statements and the reported amounts of revenues and expenses during the reporting periods. The most significant estimates and assumptions relate to the recoverability of prepaid royalties, capitalized software development costs and other intangibles, inventories, realization of deferred income taxes and the adequacy of allowances for returns, price protection and doubtful accounts. Actual amounts could differ significantly from these estimates.

Concentration of Credit Risk

A significant portion of the Company's cash balance is maintained with several major financial institutions with satisfactory standing and, while attempting to limit credit exposure with any single institution, there are times that balances will exceed insurable amounts.

If the financial condition and operations of the Company's customers deteriorate, the risk of collection could increase substantially. As of October 31, 2001 and 2000, the receivable balances from the Company's largest customer amounted to approximately 11.7% and 10.1% of the Company's net receivable balance, respectively. For the years ended October 2001, 2000, and 1999, the Company's five largest customers accounted for 20.9%, 22.7%, and 24.6% of net sales, respectively. Except for the largest customer noted above, all receivable balances from the remaining customers were less than 10%. The Company maintains insurance, to the extent available, on the receivable balances.

Revenue Recognition

Publishing revenue is derived from the sale of internally developed interactive software titles or from the sale of titles licensed from a third party developer. Publishing revenue amounted to \$242,913,000 \$186,118,000 and \$159,117,000 in 2001, 2000 and 1999, respectively.

Distribution revenue is derived from the sale of third-party interactive software titles and hardware. Distribution revenue amounted to \$208,143,000, \$177,883,000 and \$145,597,000 for 2001, 2000 and 1999, respectively.

The Company recognizes revenue in accordance with Statement of Position ("SOP") 97-2 "Software Revenue Recognition", as amended by SOP 98-9 "Modification of SOP 97-2 Software Revenue Recognition with respect to Certain Transactions." SOP 97-2 provides guidance on applying generally accepted accounting principles in recognizing revenue on software transactions. SOP 98-9 deals with the determination of vendor specific objective evidence of fair value in multiple element arrangements, such as maintenance agreements sold in conjunction with software packages. The Company's transactions generally include only one element, the interactive software game. The Company recognizes revenue, when the price is fixed and determinable, there is persuasive evidence of an arrangement, the fulfillment of its obligations under any such arrangement and determination that collection is probable. Accordingly, revenue is recognized when title and all risks of loss are transferred to the customer, which is generally upon receipt. The Company's payment arrangements with its customers provide primarily 60 day terms and to a limited extent with certain customers 30, 90 or 120 day terms.

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The Company's distribution arrangements with customers generally do not give customers the right to return products; however, the Company at its discretion may accept product returns for stock balancing or defective products. In addition, the Company sometimes negotiates accommodations to customers, including price discounts, credits and product returns, when demand for specific products falls below expectations. The Company's publishing arrangements require the Company to accept product returns. The Company establishes a reserve for future returns and other allowances based primarily on its return policies, price protection and historical return rates. The Company may not have a reliable basis to estimate returns and allowances for certain customers or it may be unable to determine that collection of the receivable is probable. In such circumstances, the Company defers the revenues at the time of the sale and recognizes them when collection of the related receivable becomes probable or cash is received.

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TAKE-TWO INTERACTIVE SOFTWARE, INC. Notes to Consolidated Financial Statements

Effective November 1, 2000, the Company adopted Staff Accounting Bulletin ("SAB") No. 101, "Revenue Recognition in Financial Statements". Consistent with the guidelines provided in SAB No. 101, the Company changed its revenue recognition policy to recognize revenue as noted above. Prior to the adoption of SAB 101, the Company recognized revenue upon shipment. As a result of adopting SAB 101, net sales and cost of sales of approximately \$27.2 million and \$18.3 million, respectively, which were originally recognized in the year ended October 31, 2000 were also recognized in the year ended October 31, 2001. The cumulative effect of the application of the revenue recognition policies set forth in SAB 101 for the year ended October 31, 2001 was approximately \$5.3 million net of tax benefit of approximately \$3.6 million or \$0.16 per share. Had the Company adopted SAB 101 as of the beginning of fiscal 2000, the unaudited pro forma net sales, net income and diluted earnings per share for the year ended October 31, 2000 would have been approximately \$345 million, \$4.6 million and \$0.16, respectively. It is impracticable for the Company to present proforma information for periods prior to fiscal 2000.

Advertising

The Company expenses advertising costs as incurred. The Company shares portions of certain customers' advertising expenses through co-op advertising arrangements. Co-op advertising allowances provided to customers are recognized at the time the revenue is recognized. Advertising expense for the years ended October 31, 2001, 2000, and 1999 amounted to \$22,983,000, \$16,769,000 and \$11,986,000, respectively.

Cash and Cash Equivalents

The Company considers all highly liquid instruments purchased with original maturities of three months or less to be cash equivalents.

Inventory

Inventories are stated at the lower of average cost or market. The Company periodically evaluates the carrying value of its inventories

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and makes adjustments as necessary. Reserves for product returns are included in the inventory balance.

Prepaid Royalties

The Company's agreements with licensors and developers generally provide it with exclusive publishing rights and require it to make advance royalty payments that are recouped against royalties due to the developer based on product sales. Prepaid royalties are amortized as cost of sales based on the greater of the proportion of current year sales to total of current and estimated future sales on a title by title basis for that title or the contractual royalty rate based on actual net product sales. The Company continually evaluates the recoverability of prepaid royalties and charges to cost of sales the amount that management determines is probable that will not be recouped at the contractual royalty rate in the period in which such determination is made. Included in prepaid royalties at October 31, 2001 and 2000, respectively are \$13,811,000 and \$9,029,000 related to titles that have not been released yet. Prepaid royalties are classified as current and non-current assets based upon estimated net product sales within the next year. Prepaid royalties were written down by \$975,000 \$501,000 and \$1,308,000 for the years ended October 31, 2001, 2000 and 1999, respectively, to estimated net realizable value. Amortization of prepaid royalties amounted to \$17,598,000, \$16,849,000 and \$12,144,000 during fiscal years 2001, 2000, and 1999, respectively.

Capitalized Software Development Costs (Including Film Production Costs)

The Company capitalizes internal software development costs subsequent to establishing technological feasibility of a title. Amortization of such costs as a component of cost of sales is recorded on a product-by-product basis upon product release based on the greater of the proportion of current year sales to total of current and estimated future sales for that title or the straight-line method over the remaining estimated useful life of the product. The Company continually evaluates the recoverability of capitalized software costs. Capitalized Software Development Costs represent the costs associated with the internal development of the Company's publishing products. Capitalized software costs were written down by \$389,000 and \$698,000 to estimated net realizable value for the years ended October 31, 2001 and 1999, respectively. No capitalized software costs were written down for the year ended October 31, 2000. Amortization of capitalized software costs amounted to \$3,780,000, \$1,451,000 and \$1,136,000 during 2001, 2000, and 1999, respectively.

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TAKE-TWO INTERACTIVE SOFTWARE, INC.
Notes to Consolidated Financial Statements

Property and Equipment

Office equipment, furniture and fixtures and automobiles are depreciated using the straight-line method over their estimated lives ranging from five to seven years. Computer equipment and software are depreciated using the straight-line method over three years. Leasehold improvements are amortized over the lesser of the term of the related lease or estimated useful lives. Accumulated amortization includes the

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amortization of assets recorded under capital leases, which amounted to approximately \$202,000 and \$73,000 at October 31, 2001 and 2000, respectively. The cost of additions and betterments are capitalized, and repairs and maintenance costs are charged to operations in the periods incurred. When depreciable assets are retired or sold, the cost and related allowances for depreciation are removed from the accounts and the gain or loss is recognized. The carrying values of these assets are recorded at historical cost. The cost of major additions and betterments is capitalized.

Intangible Assets

Intangible assets consist of identifiable intangibles and the remaining excess purchase price paid over identified intangible and tangible net assets of acquired companies (goodwill). Intangible assets are amortized under the straight-line method over the period of expected benefit of seven years for the acquisition of development studios and ten years for the acquisition of distribution operations. The Company assesses the recoverability of its intangible assets by determining whether the carrying value can be recovered through estimated future undiscounted cash flows over its remaining life. If estimated future cash flows indicate that the unamortized balance will not be recovered, an adjustment will be made to reduce the carrying value to an amount consistent with estimated future cash flows discounted at the Company's incremental borrowing rate. Cash flow estimates are based on trends of historical performance and management's estimate of future performance, giving consideration to existing and anticipated competitive and economic conditions.

Impairment of Long-Lived Assets

The Company accounts for long-lived assets in accordance with the provisions of Statement of Financial Accounting Standards No. 121, "Accounting for Impairment of Long-Lived Assets and Long Lived Assets to be Disposed Of" ("SFAS 121"). SFAS 121 requires that long-lived assets be reviewed for impairment whenever events or changes in circumstances indicate that the carrying amount of an asset may not be recoverable. The Company compares the carrying amount of the asset to the estimated undiscounted future cash flows expected to result from the use of the asset. If the carrying amount of the asset exceeds estimated expected undiscounted future cash flows, the Company records an impairment charge for the difference between the carrying amount of the asset its fair value. The estimation of fair value is generally measured by discounting expected future cash flows at the Company's incremental borrowing rate or fair value if available.

Stock-Based Compensation

The Company accounts for its employee stock option plans in accordance with Accounting Principles Board Opinion No. 25, "Accounting for Stock Issued to Employees" ("APB 25"). Under APB 25, generally no compensation expense is recorded when the terms of the award are fixed and the exercise price of the employee stock option equals or exceeds the fair value of the underlying stock on the date of grant. The Company adopted the disclosure-only provisions of Statement of Financial Accounting Standards ("SFAS") No. 123, "Accounting for Stock-Based Compensation" ("SFAS 123").

Net (Loss) Income per Share

Basic earnings per share ("EPS") is computed by dividing the net (loss) income applicable to common stockholders for the year by the

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weighted-average number of common shares outstanding during the year. Diluted EPS is computed by dividing the net (loss) income applicable to common stockholders for the year by the weighted-average number of common and common stock equivalents, which include common shares issuable upon the exercise of stock options and warrants outstanding during the year. Common stock equivalents are excluded from the computation if their effect is antidilutive.

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TAKE-TWO INTERACTIVE SOFTWARE, INC.
Notes to Consolidated Financial Statements

Comprehensive Income (Loss)

Comprehensive income (loss) represents the change in net assets of a business enterprise during a period from transactions and other events and circumstances from non-owner sources. Comprehensive income (loss) of the Company includes net income adjusted for the change in foreign currency translation adjustments and the change in net unrealized gain (loss) from investments.

Income Taxes

The Company recognizes deferred taxes under the asset and liability method of accounting for income taxes. Under the asset and liability method, deferred income taxes are recognized for differences between the financial statement and tax bases of assets and liabilities at currently enacted statutory tax rates for the years in which the differences are expected to reverse. The effect on deferred taxes of a change in tax rates is recognized in income in the period that includes the enactment date. In addition, valuation allowances are established when necessary to reduce deferred tax assets to the amounts expected to be realized.

Foreign Currency Translation

The functional currency for the Company's foreign operations is the applicable local currency. Accounts of foreign operations are translated into U.S. dollars using quarter or year-end exchange rates for assets and liabilities at the balance sheet date and average prevailing exchange rates for the period for revenue and expense accounts. Adjustments resulting from translation are included in other comprehensive income (loss).

Fair Value of Financial Instruments

The carrying amounts of the Company's financial instruments, including cash and cash equivalents, accounts receivable, accounts payable and accrued liabilities, approximate fair value because of their short maturities. The carrying amount of prepaid royalties and investments approximate fair value based upon the recoverability of these assets. The carrying amount of the Company's lines of credit approximates fair value because the interest rates of the lines of credit are based on floating rates identified by reference to market rates. The carrying amounts of the Company's loan payable and capital lease obligations approximate the fair value of such instruments based upon management's best estimate of interest rates that would be available to the Company for similar debt obligations at October 31, 2001.

The Company enters into forward foreign exchange contracts to a limited

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extent to manage the risk associated with currency fluctuations on certain sales and purchase commitments denominated in foreign currencies. The Company's forward foreign exchange contracts are primarily denominated in certain European currencies and are for periods consistent with the terms of the underlying transactions, which is less than one year. Gains and losses resulting from the impact of currency exchange rate movements on contracts that qualify, as effective hedges are not recognized in operations until the underlying hedged transactions are recognized. Upon recognition, such gains and losses are recorded in operations as an adjustment to the carrying amount of the underlying transactions in the period in which these transactions are recognized. As of October 31, 2001, there are no forward foreign exchange contracts outstanding. As of October 31, 2000, the contract amount of forward foreign exchange contracts outstanding was approximately \$678,000.

Recently Issued Accounting Pronouncements

In July 2001, the FASB issued Statement of Financial Accounting Standard No. 141, "Business Combinations" ("SFAS 141") and Statement of Financial Accounting Standard No. 142, "Goodwill and Other Intangible Assets" ("SFAS 142").

SFAS 141 establishes accounting and reporting for business combinations by requiring that all business combinations be accounted for under the purchase method. Use of the pooling-of-interests method is no longer permitted. SFAS 141 also provides guidance on purchase accounting related to the recognition of intangible assets and accounting for negative goodwill. SFAS 141 requires that the purchase method be used for business combinations initiated after June 30, 2001.

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TAKE-TWO INTERACTIVE SOFTWARE, INC. Notes to Consolidated Financial Statements

SFAS 142 changes the accounting for goodwill from an amortization method to an impairment-only approach. Upon adoption of SFAS 142, amortization of goodwill recorded for business combinations consummated prior to July 1, 2001 will cease, and intangible assets acquired prior to July 1, 2001 that do not meet the criteria for recognition under SFAS 141 will be reclassified to goodwill. Goodwill will be subject to an annual impairment test, including a transitional impairment test required upon adoption of SFAS 142 for which companies have six months to complete. The provisions of SFAS 142 will be effective for fiscal years beginning after December 15, 2001; however, early adoption is permitted. The Company anticipates the early adoption of SFAS 142 as of the beginning of fiscal 2002. The Company is still in the process of reallocating previously identifiable intangibles that do not meet the criteria of SFAS 141 into Goodwill and evaluating the useful lives of its remaining identifiable intangibles. However, the Company currently estimates that unaudited pro forma income (loss) before extraordinary item and cumulative effect of change in accounting principle and the respective diluted EPS and net income and diluted EPS would have been approximately \$2.9 million and \$0.08 and (\$4.4 million) and (\$0.13), respectively for the year ended October 31, 2001 had the provisions of the new standards been applied in that year. The Company is in the process of completing its step one transition assessment of goodwill. However, it does not currently anticipate having to record transition impairment of goodwill or other intangible assets as a cumulative effect as a result of these new standards.

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In August 2001, the FASB issued Statement of Financial Accounting Standard No.143, "Accounting for Obligations Associated with the Retirement of Long-Lived Assets" ("SFAS 143"). The objective of SFAS 143 is to provide accounting guidance for legal obligations associated with the retirement of long-lived assets. The retirement obligations included within the scope of this pronouncement are those that an entity cannot avoid as a result of either the acquisition, construction or normal operation of a long-lived asset. Components of larger systems also fall under this pronouncement, as well as tangible long-lived assets with indeterminable lives. The provisions of SFAS 143 are effective for financial statements issued for fiscal years beginning after June 15, 2002. The Company is currently evaluating the expected impact of the adoption of SFAS 143 on the Company's financial condition, cash flows and results of operations. The Company will adopt the standard in the first quarter of fiscal 2003.

In October 2001, the FASB issued Statement of Financial Accounting Standard No.144, "Accounting for the Impairment or Disposal of Long-Lived Assets" ("SFAS 144"). The objectives of SFAS 144 are to address significant issues relating to the implementation of SFAS 121 and to develop a single accounting model, based on the framework established in SFAS 121, for long-lived assets to be disposed of by sale, whether previously held and used or newly acquired. The provisions of SFAS 144 are effective for financial statements issued for fiscal years beginning after December 15, 2001. The Company is currently evaluating the expected impact of the adoption of SFAS 144 on the Company's financial condition and results of operations. The Company will adopt the standard at the first quarter of fiscal 2003.

4. Business Acquisitions (See Note 5)

The Company acquired a number of companies that develop, publish or distribute interactive software games during the three-year period ended October 31, 2001. The aggregate purchase price, including cash payments and issuance of its common stock was \$28.1 million, \$65.4 million, and \$9.7 million in 2001, 2000 and, 1999, respectively. The value of the Company's common stock issued in connection with these acquisitions has been based on the market price of the Company's common stock at the time such proposed transactions were agreed and announced. The aggregate purchase price excludes the value of stock issued for acquisitions accounted for as pooling of interests.

In 1999, 1,033,000 shares of the Company's common stock were issued for the acquisition of Talonsoft, Inc. ("Talonsoft") accounted for as pooling of interests. The Company's consolidated financial statements including the related notes had been restated as of the earliest period presented to include the results of operations, financial position and cash flows of Talonsoft.

The acquisitions described below have been accounted for as purchase transactions in accordance with APB No. 16 and SFAS 141 (for transactions after July 1, 2001) and, accordingly, the results of operations and financial position of the acquired businesses are included in the Company's consolidated financial statements from the respective dates of acquisition.

2001 transactions

In July 2001, the Company acquired all of the outstanding capital stock of Techcorp Limited ("Techcorp"), a Hong Kong based design and engineering firm specializing in video game accessories. In

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consideration, the Company issued 30,000 shares of the Company's restricted common stock (valued at \$572,000), paid \$100,000 in cash and assumed net liabilities of approximately \$2.9 million. In connection with the acquisition, the Company recorded goodwill of \$3,558,000 on a preliminary basis. The Company is in the process of obtaining an independent third party valuation in support of its preliminary purchase price allocation. The Company will make the required adjustments, if any, upon completion of such valuation. In accordance with SFAS 141, the Company is not amortizing the goodwill recorded in connection with this acquisition.

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TAKE-TWO INTERACTIVE SOFTWARE, INC. Notes to Consolidated Financial Statements

In November 2000, the Company acquired all of the outstanding capital stock of VLM Entertainment Group, Inc. ("VLM"), a company engaged in the distribution of third-party software products. In connection with this transaction, the Company paid the former stockholders of VLM \$2 million in cash and issued 875,000 shares of the Company's common stock (valued at \$8.0 million) and assumed net liabilities of approximately \$10.6 million. In connection with this transaction, the Company recorded intangible assets of approximately \$20.7 million on a preliminary basis. The Company is in the process of obtaining an independent third party valuation in support of its preliminary purchase price allocation. The Company will make the required adjustments, if any, upon completion of such valuation.

In connection with the sale of Toga to Gameplay in October 2000, the Company agreed to acquire Gameplay's game software development and publishing business - Neo Software Produktions GMBH ("Neo"). Such acquisition was completed in January of 2001. See Note 5 for further discussion of this transaction.

The following table sets forth the components of the purchase price of the 2001 acquisitions (in thousands):

	Neo -----	VLM -----	Techcorp -----	Tot -----
Cost of the acquisition:				
Value of business sold (Prepaid purchase price-Neo) or stock issued	\$ 17,266	\$ 8,039	\$ 572	\$ 25,877
Cash	--	2,000	100	2,100
Transaction Costs	109	27	30	166
	-----	-----	-----	-----
Total	\$ 17,375	\$ 10,066	\$ 702	\$ 28,143
	=====	=====	=====	=====
Allocation of purchase price:				
Current Assets	\$ 2	\$ 9,852	\$ 894	\$ 10,748
Non-Current Assets	71	201	498	770
Liabilities	(881)	(20,680)	(4,248)	(25,809)

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Goodwill	7,282	12,362	3,558	23
Customer Lists	--	8,331	--	8
Technology	8,037	--	--	8
Trademarks	1,939	--	--	1
Workforce	925	--	--	
	-----	-----	-----	-----
Total	\$ 17,375	\$ 10,066	\$ 702	\$ 28
	=====	=====	=====	=====

Certain of Neo's internet-related technology assets were determined to be impaired in April 2001. Accordingly, the Company recorded as cost of sales a non-cash impairment charge of \$3,786,000 consisting of \$2,350,000 relating to server maintenance technologies and \$1,047,000 relating to multiplayer technologies developed by Neo's development studio in connection with Online Pirates and \$389,000 of capitalized software relating to other products to be developed by Neo. In addition, the Company recorded as selling and marketing expenses an impairment charge of \$401,000 related to online sales promotions.

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TAKE-TWO INTERACTIVE SOFTWARE, INC.
Notes to Consolidated Financial Statements

2000 Transactions

In August 2000, the Company acquired all of the outstanding capital stock of PopTop Software, Inc. ("PopTop") for 559,100 shares of its Common Stock (valued at \$5.8 million) and assumed net liabilities of approximately \$88,000.

In April 2000, the Company acquired the remaining 80.1% of the equity interest of Gathering of Developers, Ltd ("Gathering") for 1,060,000 shares of its Common Stock (valued at \$10.4 million) and assumed liabilities of approximately \$3 million. In accordance with the provisions of EITF 99-10, the Company recorded an additional charge of \$19,206,000 (see Notes 2 and 7) which effectively reduced the cost of the acquisition of Gathering by the same amount. The result was a net reduction for post acquisition amortization of \$710,000 comprised of a \$1,125,000 reduction of the amortization of intangible assets offset by an increase of \$415,000 in the amortization of prepaid royalties.

In March 2000, the Company acquired all of the outstanding capital stock of Toga, the parent company of Pixel Broadband Studios, Ltd. ("Pixel"). In connection with this acquisition, the Company paid \$4.5 million in cash, issued 2,561,000 shares of its Common Stock (valued at \$38.6 million), issued a warrant to purchase the stock of Pixel to the founder of Pixel (valued at \$1.75 million based on the Black-Scholes pricing model) and assumed net liabilities of approximately \$3.3 million. Toga was sold in October 2000 to Gameplay.com PLC ("Gameplay") (See Note 5).

The following table sets forth the components of the purchase prices of the 2000 acquisitions (net of the disposition of Toga) (in thousands):

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	Gathering -----	Pop Top -----	Toga -----	Total -----
Cost of the acquisition:				
Value of stock issued	\$ 10,402	\$ 5,836	\$ 38,578	\$ 54,816
Value of warrants issued	--	--	1,750	1,750
Cash	--	--	4,458	4,458
Investments and advances at time of acquisition	3,964	--	--	3,964
Transaction Costs	48	32	320	400
	-----	-----	-----	-----
Total	\$ 14,414	\$ 5,868	\$ 45,106	\$ 65,388
Allocation of purchase price:				
Current Assets	\$ 4,063	\$ --	\$ --	\$ 4,063
Non-Current Assets	72	66	--	138
Liabilities	(6,675)	(154)	(3,279)	(10,108)
Goodwill	8,128	\$ 5,110	\$ --	13,238
Trademarks	8,826	846	--	9,672
Prepaid purchase price - Neo	--	--	17,266	17,266
Gameplay Investment	--	--	31,119	31,119
	-----	-----	-----	-----
Total	\$ 14,414	\$ 5,868	\$ 45,106	\$ 65,388

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TAKE-TWO INTERACTIVE SOFTWARE, INC.
Notes to Consolidated Financial Statements

Unaudited proforma information

The unaudited pro forma data below for the years ended October 31, 2001 and 2000 is presented as if purchase acquisitions for fiscal 2000 and 2001 had been made as of November 1, 1999. The unaudited pro forma financial information is based on management's estimates and assumptions and does not purport to represent the results that actually would have occurred if the acquisitions had, in fact, been completed on the dates assumed, or which may result in the future. The unaudited pro forma financial information includes purchase acquisitions that are significant to the Company's operations.

	Unaudited Pro forma (in thousands, except for per share d October 31, 2001		October 31
	-----	-----	-----
Total Revenues	\$	458,665	\$ 4
Income before extraordinary item and cumulative effect of change in accounting:	\$	(4,079)	\$
Net income per share - Basic	\$	(0.12)	\$

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Net income per share - Diluted \$ (0.12) \$

Included in the unaudited pro forma information is amortization of goodwill of approximately \$7,320,000 and \$7,744,000 net of taxes of \$2,799,000 and \$3,081,000 for the years ended October 31, 2001 and 2000, respectively.

1999 transactions

In 1999, the Company paid \$1.2 million in cash, issued 638,000 shares of its common stock (valued at \$6.1 million), incurred direct transaction costs of approximately \$400,000 and assumed liabilities of approximately \$15.9 million for all acquisitions accounted for as purchases. These acquisitions were LDA Distribution Limited, Joytech Europe Limited, DVDWave.com, Funsoft Nordic A.S., Triad Distributors, Inc., Global Star Software Ltd., DMA Design Holdings Limited, DMA Design Limited and CD Verte, S.p.A. ("CD Verte") and a minority interest in Bungie Software. In addition, for CD Verte, the Company paid \$800,000 on December 1, 1999 and will pay an additional \$1.2 million, subject to a potential downward adjustment based on net income of the acquired entity, over a three-year period.

5. Disposition of Assets

In July 2001, the Company sold all of the outstanding capital stock of Jack of All Games UK, a video game distributor, to Jay Two Limited, an unaffiliated third-party controlled by Freightmasters Ltd., for approximately \$215,000. In connection with the sale, the purchaser assumed net liabilities of \$436,000. The Company recorded a non-operating gain of \$651,000 net of taxes relating to the sale.

In October 2000, the Company sold all of the outstanding shares of Toga to Gameplay and simultaneously entered into a license agreement with Gameplay for the online distribution of certain of the Company's PC games. Toga had been purchased in March 2000 (see Note 4). The Company received (i) 15,371,698 shares of Gameplay's common stock (valued at approximately \$31.1 million); (ii) a warrant to purchase 1,000,000 shares of Gameplay stock (the Company assigned no value to the warrant); and (iii) a joint exploitation agreement with Gameplay under which the Company acquired rights to the software development business of Neo - a subsidiary of Gameplay (valued at approximately \$17.3 million). The value of such right was recorded as prepaid purchase price at the time of Toga's sale and has been included in intangible assets at October 31, 2000.

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TAKE-TWO INTERACTIVE SOFTWARE, INC.
Notes to Consolidated Financial Statements

The Company recognized a loss of \$286,000 on the sale of Toga, which was recorded as a component of "gain on sale of subsidiary, net" on the 2000 Consolidated Statement of Operations. The Company obtained an independent third party valuation in support of the value assigned to its right to acquire Neo. In January 2001, the Company completed the acquisition of Neo and assumed net liabilities of approximately \$808,000, in addition to the prepaid purchase price of \$17.3 million noted above.

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In June 2000, the Company sold its 19.9% equity interest in Bungie Software ("Bungie") to Microsoft Corporation for approximately \$5 million in cash. The Company did not realize any gain or loss on this transaction. Separately, the Company sold its exclusive Halo publishing and distribution rights to Bungie for \$4 million in cash, a royalty free license to Bungie's Halo technology in connection with the development of two original products and all right, title and interest to the Myth franchise and the PC and Playstation(R) 2 game, Oni. The Company recorded this transaction as net sales of \$5.5 million after giving effect to the receipt of \$9 million in cash and \$5.8 million of assets (consisting of \$2.8 million relating to Oni, \$1.5 million relating to Myth and \$1.5 million relating to the license to use Halo game engine technology for two original products), net of \$9.3 million of assets sold. The Company obtained independent third party valuations in support of the transaction.

In February 2000, the Company sold all of its interest in Falcon Ventures Corporation d/b/a DVDWave.com to eUniverse, Inc. ("eUniverse") in exchange for 310,000 shares of eUniverse's common stock. The Company recognized a gain of \$1,976,000 and recorded such gain as a component of "Gain on sale of subsidiary, net" on the Consolidated Statement of Operations.

6. Intangible Assets

Intangible assets consist of trademarks, intellectual property, customer lists, acquired technology and the excess purchase price paid over identified intangible and tangible net assets of acquired companies (goodwill).

In December 2000, the Company acquired the exclusive worldwide publishing rights to the franchise of Duke Nukem PC and video games, including the PC, console and sequel rights to Duke Nukem Forever. In connection with the transaction, the Company paid \$2.3 million in cash and issued 557,103 shares of its common stock (valued at approximately \$5.4 million). In addition, the Company is contingently liable to make a further payment of \$6 million upon delivery of the gold master of Duke Nukem Forever. The Company recorded an intangible asset of \$7.7 million related to the intellectual property purchased in this transaction on a preliminary basis. The Company is in the process of obtaining an independent third party valuation in support of its preliminary valuation. The Company will make the required adjustments, if any, upon completion of such valuation. The additional \$6 million will be recorded as an additional intangible asset upon resolution of the contingency.

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TAKE-TWO INTERACTIVE SOFTWARE, INC.
Notes to Consolidated Financial Statements

The following table sets forth the components of the intangible assets as of October 31, 2001 and 2000 (in thousands):

October 31, 2001	October 31, 2000
-----	-----

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Goodwill	\$ 70,191	\$ 45,183
Prepaid purchase price -Neo (Note 5)	--	17,266
Trademarks	13,922	11,983
Customer lists	9,081	803
Intellectual property	8,527	--
Technology	4,640	--
Workforce	925	--
	-----	-----
	107,286	75,235
Less - accumulated amortization	19,111	8,673
	-----	-----
	\$ 88,175	\$ 66,562
	-----	-----

Amortization expense for the years ended October 31, 2001, 2000, and 1999, amounted to \$9,309,000, \$6,919,000, and \$1,662,000, respectively.

7. Investment in Affiliate

In May 1998, the Company entered into a distribution agreement with Gathering, a publisher of PC and video games. Pursuant to the agreement, the Company agreed to pay Gathering advance royalty payments of up to \$7.5 million for the rights to distribute certain PC titles. In February 1999, the Company amended the May 1998 distribution agreement under which the Company agreed to pay Gathering advance royalty payments of up to \$12.5 million (inclusive of the payments under the May 1998 agreement). The Company's advance royalty payments under the February 1999 agreement were to be recouped from royalties due to Gathering under the distribution agreement after payment of the Company's distribution fee. The Company also made advance royalty payments to Gathering in a similar arrangement under various publishing agreements for video games.

In February 1999, the Company purchased a 19.9% equity interest in Gathering for approximately \$4 million. The investment was accounted for by the equity method due to the Company having significant influence over Gathering. The difference between the carrying value of the investment and the underlying equity in the net assets of approximately \$4,377,000, was attributed to goodwill and was amortized using the straight-line method over the period of expected benefit of seven years. Such amortization has been included in the equity in loss of affiliate.

In addition, the equity holders of Gathering granted the Company an option to purchase all of their interests, exercisable on two separate occasions during the six-month periods ending April 30, 2001 and 2002 based on a fixed formula. In consideration of the option grant, the Company issued to Gathering's equity holders 125,000 shares of common stock, valued at \$1,275,000, which was amortized over the term of the purchase option, which expired unexercised in April 2000 upon acquisition of the remaining 80% equity interest in Gathering (see Note 4).

Until October 31, 1999, the Company recognized its proportionate share of the losses in Gathering using the equity method of accounting. Effective November 1, 1999, the Company recognized its share of losses in accordance with the provisions of EITF 99-10, "Percentage Used to Determine the Amount of Equity Method Losses." This resulted in an additional charge of \$19,206,000 (See Note 2).

TAKE-TWO INTERACTIVE SOFTWARE, INC.
Notes to Consolidated Financial Statements

8. Investments

Investments are comprised of marketable equity securities and are classified as current and non-current assets. The investments are accounted for under the cost method as "available-for-sale" in accordance with Statement of Financial Standards No. 115 "Accounting for Certain Investments in Debt and Equity Securities". The investments are stated at fair value, with unrealized appreciation reported as a separate component of accumulated other comprehensive income (loss) in stockholders' equity.

During 2001, the Company recorded an impairment charge of \$21,477,000, consisting of approximately \$19,171,000 relating to its investment in Gameplay, \$2,000,000 relating to its investment in eUniverse, Inc. based on the quoted market prices and \$306,000 relating to its investment in a privately-held company, which is included in other non-current assets. All of these investments were deemed to be other than temporarily impaired. In addition, the Company recorded unrealized gains and losses on its remaining investments through other comprehensive income (loss).

As of October 31, 2001 and 2000, investments consist of (in thousands):

	2001		2000	
	Current	Non Current	Current	Non Current
Average cost	\$ 5,988	\$ 75	\$ 2,896	\$ 33,084
Unrealized gains (losses)	\$ 253	\$ --	30	(4,597)
Fair value	\$ 6,241	\$ 75	\$ 2,926	\$ 28,487

For the fiscal years ended October 31, 2001 and 2000, the gross proceeds from the sale of investments were \$11,000 and \$639,000, respectively. The gross realized losses from these sales totaled \$69,000 and \$180,000, respectively. The loss on sale of securities is based on the average cost of the individual securities sold.

9. Inventories

As of October 31, 2001 and 2000, inventories consist of (in thousands):

	2001	2000
Parts and supplies	\$ 1,468	\$ 496
Finished products	60,469	53,302
	\$61,937	\$53,798

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10. Fixed Assets

As of October 31, 2001 and 2000, fixed assets consist of (in thousands):

	2001	2000
	-----	-----
Computer equipment	\$ 5,705	\$ 3,737
Office equipment	1,583	816
Computer software	4,357	537
Furniture and fixtures	1,876	1,710
Automobiles	438	305
Leasehold improvements	2,209	1,086
Capital leases	398	348
	-----	-----
	16,566	8,539
Less: accumulated depreciation and Amortization	(5,533)	(3,279)
	-----	-----
	\$ 11,033	\$ 5,260
	=====	=====

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TAKE-TWO INTERACTIVE SOFTWARE, INC.
Notes to Consolidated Financial Statements

In 2001, the Company capitalized costs of approximately \$2.8 million associated with software and hardware upgrades to its accounting systems.

Depreciation expense for the years ended October 31, 2001, 2000, and 1999, amounted to \$3,731,000, \$1,761,000, and \$1,160,000, respectively.

11. Lines of Credit

As of October 31, 2001 and 2000, lines of credit consist of (in thousands):

	2001	2000
	-----	-----
Line of credit with Bank of America - 4.94% to 6.01% (8.38 to 9.23% in 2000)	\$48,701	\$70,599
Line of credit with Barclays' Bank - 5.25% to 5.75% (7.4% in 2000)	--	14,006
Line of credit with Lloyds TSB Bank plc - 4.5% to 5.75%	5,372	--
	-----	-----
	\$54,073	\$84,605
	=====	=====

In February 2001, five of the Company's European subsidiaries entered into a credit facility agreement with Lloyds TSB Bank plc ("Lloyds") under which Lloyds agreed to make available borrowings of up to \$19 million linked to the British Pound Sterling. Borrowings under the line

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of credit are collateralized by: (i) a guarantee by the Company for approximately \$23 million, plus interest and other costs, as defined; (ii) an unlimited debenture by the European subsidiaries and (iii) an assignment of the proceeds of the insurance policies, as defined, taken out in respect of the European subsidiaries accounts receivables. The outstanding balance and available credit under the revolving line of credit were \$5,372,000 and \$15,076,000 respectively, as of October 31, 2001. Advances under the credit facility bear interest at the rate of 1.25% per annum over the bank's base rate. The credit facility originally expired in December 2001 but has been extended through March 31, 2002.

In December 1999, the Company entered into a credit agreement with a group of lenders led by Bank of America, N.A., as agent, which provides for borrowings of up to \$75,000,000. The Company may increase the credit line up to \$85,000,000 subject to certain conditions. Interest accrues on such advances at the bank's prime rate plus 0.5%