Activision Blizzard, Inc.
Form 10-Q
May 07, 2010
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UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

FORM 10-Q

(Mark one)

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

For the Quarterly Period Ended March 31, 2010

OR

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

For the transition period from to

Commission File Number 1-15839

ACTIVISION BLIZZARD, INC.

(Exact name of registrant as specified in its charter)

Delaware (State or other jurisdiction of incorporation or organization)	**95-4803544** (I.R.S. Employer Identification No.)
3100 Ocean Park Boulevard, Santa Monica, CA (Address of principal executive offices)	**90405** (Zip Code)

(310) 255-2000
(Registrant s telephone number, including area code)

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

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

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

Large Accelerated Filer x	Accelerated Filer o
Non-accelerated filer o (Do not check if a smaller reporting company)	Smaller reporting company o

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

The number of shares of the registrant s Common Stock outstanding at April 30, 2010 was 1,243,905,768.

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ACTIVISION BLIZZARD, INC. AND SUBSIDIARIES

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CAUTIONARY STATEMENT

This Quarterly Report on Form 10-Q contains, or incorporates by reference, certain forward-looking statements within the meaning of the Private Securities Litigation Reform Act of 1995. Such statements consist of any statement other than a recitation of historical fact and include, but are not limited to: (1) projections of revenues, expenses, income or loss, earnings or loss per share, cash flow or other financial items; (2) statements of our plans and objectives, including those relating to product releases; (3) statements of future economic performance; and (4) statements of assumptions underlying such statements. We generally use words such as anticipate, believe, could, estimate, expect, forecast, future, intend, may, outlook, plan, positioned, potential, project, remain, scheduled, set to, subject to, to be, upcoming, will, and other similar expressions to help identify forward-looking statements. Forward-looking statements are subject to business and economic risk, reflect management s current expectations, estimates and projections about our business, and are inherently uncertain and difficult to predict. Our actual results could differ materially. The forward-looking statements contained herein speak only at the date on which this Form 10-Q was first filed. Risks and uncertainties that may affect our future results include, but are not limited to, sales levels of Activision Blizzard s titles, shifts in consumer spending trends, the impact of the current macroeconomic environment, the seasonal and cyclical nature of the interactive game market, any further difficulties related to World of Warcraft in China, Activision Blizzard s ability to predict consumer preferences among competing hardware platforms, declines in software pricing, product returns and price protection, product delays, retail acceptance of Activision Blizzard s products, adoption rate and availability of new hardware (including peripherals) and related software, industry competition, including from used games, and from other forms of entertainment, litigation risks and associated costs, rapid changes in technology, industry standards, business models, including online and used games and consumer preferences including interest in specific genres such as music, first-person action and massively multiplayer online games, protection of proprietary rights, maintenance of relationships with key personnel, customers, licensees, licensors, vendors, and third-party developers, including the ability to attract, retain and develop key personnel and developers that can create high quality hit titles, counterparty risks relating to customers, licensees, licensors and manufacturers, domestic and international economic, financial and political conditions and policies, foreign exchange rates and tax rates, and the identification of suitable future acquisition opportunities, and potential challenges associated with geographic expansion, and the other factors identified in Risk Factors included in Part II, Item 1A of this Quarterly Report on Form 10-Q and in our Annual Report on Form 10-K for the year ended December 31, 2009. The forward-looking statements contained herein are based upon information available to us as of the date of this Quarterly Report on Form 10-Q and we assume no obligation to update any such forward-looking statements. Forward-looking statements believed to be true when made may ultimately prove to be incorrect. These statements are not guarantees of our future performance and are subject to risks, uncertainties and other factors, some of which are beyond our control and may cause actual results to differ materially from current expectations.

Activision Blizzard s names, abbreviations thereof, logos, and product and service designators are all either the registered or unregistered trademarks or trade names of Activision Blizzard.

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Part I. FINANCIAL INFORMATION

Item 1. Financial Statements

ACTIVISION BLIZZARD, INC. AND SUBSIDIARIES

CONDENSED CONSOLIDATED BALANCE SHEETS

(Unaudited)

(Amounts in millions, except share data)

	At March 31, 2010	At December 31, 2009
Assets		
Current assets:		
Cash and cash equivalents	$ 2,695	$ 2,768
Short-term investments	647	477
Accounts receivable, net of allowances of $225 million and $317 million at March 31, 2010 and December 31, 2009, respectively	134	739
Inventories	194	241
Software development	217	224
Intellectual property licenses	40	55
Deferred income taxes, net	395	498
Other current assets	164	327
Total current assets	4,486	5,329
Long-term investments	23	23
Software development	4	10
Intellectual property licenses	29	28
Property and equipment, net	131	138
Other assets	11	9
Intangible assets, net	599	618
Trademark and trade names	433	433
Goodwill	7,150	7,154
Total assets	$ 12,866	$ 13,742
Liabilities and Shareholders Equity		
Current liabilities:		
Accounts payable	$ 147	$ 302
Deferred revenues	772	1,426
Accrued expenses and other liabilities	623	779
Total current liabilities	1,542	2,507
Deferred income taxes, net	254	270
Other liabilities	202	209
Total liabilities	1,998	2,986
Commitments and contingencies (Note 13)		
Shareholders equity:		
Common stock, $.000001 par value, 2,400,000,000 shares authorized, 1,366,914,039 and 1,364,117,675 shares issued at March 31, 2010 and December 31, 2009, respectively		
Additional paid-in capital	12,234	12,376
Less: Treasury stock, at cost, 123,506,345 and 113,686,498 at March 31, 2010 and December 31, 2009, respectively	(1,342)	(1,235)
Retained earnings (accumulated deficit)	20	(361)
Accumulated other comprehensive loss	(44)	(24)
Total shareholders equity	10,868	10,756
Total liabilities and shareholders equity	$ 12,866	$ 13,742

The accompanying notes are an integral part of these Condensed Consolidated Financial Statements.

ACTIVISION BLIZZARD, INC. AND SUBSIDIARIES

CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS

(Unaudited)

(Amounts in millions, except per share data)

	For the three months ended March 31, 2010		For the three months ended March 31, 2009	
Net revenues				
Product sales	$	986	$	690
Subscription, licensing, and other revenues		322		291
Total net revenues		1,308		981
Costs and expenses				
Cost of sales product costs		337		296
Cost of sales software royalties and amortization		99		72
Cost of sales intellectual property licenses		43		64
Cost of sales massively multi-player online role-playing game (MMORPG)		54		52
Product development		143		117
Sales and marketing		56		83
General and administrative		65		103
Restructuring				15
Total costs and expenses		797		802
Operating income		511		179
Investment and other income, net				10
Income before income tax expense		511		189
Income tax expense		130		
Net income	$	381	$	189
Earnings per common share				
Basic	$	0.30	$	0.14
Diluted	$	0.30	$	0.14
Weighted average number of shares outstanding				
Basic		1,248		1,308
Diluted		1,264		1,359
Dividends declared per common share	$	0.15	$	

The accompanying notes are an integral part of these Condensed Consolidated Financial Statements.

ACTIVISION BLIZZARD, INC. AND SUBSIDIARIES

CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS

(Unaudited)
(Amounts in millions)

	For the three months ended March 31, 2010	2009
Cash flows from operating activities:		
Net income	$ 381	$ 189
Adjustments to reconcile net income to net cash provided by operating activities:		
Deferred income taxes	90	56
Depreciation and amortization	33	69
Unrealized gain on auction rate securities classified as trading securities		(3)
Unrealized loss on ARS rights from UBS		3
Amortization and write-off of capitalized software development costs and intellectual property licenses (1)	88	68
Stock-based compensation expense (2)	44	30
Excess tax benefits from stock option exercises	(4)	(17)
Changes in operating assets and liabilities:		
Accounts receivable	593	794
Inventories	40	32
Software development and intellectual property licenses	(80)	(75)
Other assets	162	(5)
Deferred revenues	(637)	(276)
Accounts payable	(146)	(160)
Accrued expenses and other liabilities	(337)	(378)
Net cash provided by operating activities	227	327
Cash flows from investing activities:		
Capital expenditures	(12)	(10)
Proceeds from maturities of investments	17	1
Proceeds from sale of available-for-sale investments		2
Payment of contingent consideration	(2)	
Purchases of short-term investments	(187)	
Net cash used in investing activities	(184)	(7)
Cash flows from financing activities:		
Proceeds from issuance of common stock to employees	16	7
Repurchase of common stock	(107)	(313)
Excess tax benefits from stock option exercises	4	17
Net cash used in financing activities	(87)	(289)
Effect of foreign exchange rate changes on cash and cash equivalents	(29)	(1)
Net (decrease) increase in cash and cash equivalents	(73)	30
Cash and cash equivalents at beginning of period	2,768	2,958
Cash and cash equivalents at end of period	$ 2,695	$ 2,988

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(1) Excludes deferral and amortization of stock-based compensation expense.

(2) Includes the net effects of capitalization, deferral, and amortization of stock-based compensation expense.

The accompanying notes are an integral part of these Condensed Consolidated Financial Statements.

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ACTIVISION BLIZZARD, INC. AND SUBSIDIARIES

CONDENSED CONSOLIDATED STATEMENT OF CHANGES IN SHAREHOLDERS EQUITY

For the Three Months ended March 31, 2010

(Unaudited)

(Amounts in millions)

	Common Stock		**Additional Paid-In Capital**	**Treasury Stock**		**Retained Earnings (Accumulated Deficit)**	**Accumulated Other Comprehensive Loss**	**Total Shareholders Equity**
	Shares	**Amount**		**Shares**	**Amount**			
Balance at December 31, 2009	**1,364**	**$**	**$ 12,376**	**(114)**	**$ (1,235)**	**$ (361)**	**$ (24)**	**$ 10,756**
Components of comprehensive income:								
Net income						381		381
Foreign currency translation adjustment							(20)	(20)
Total comprehensive income								361
Issuance of common stock pursuant to employee stock options and restricted stock rights	3		16					16
Stock-based compensation expense related to employee stock options and restricted stock rights			31					31
Dividends declared ($0.15 per common share)			(189)					(189)
Shares repurchased				(10)	(107)			(107)
Balance at March 31, 2010	**1,367**	**$**	**$ 12,234**	**(124)**	**$ (1,342)**	**$ 20**	**$ (44)**	**$ 10,868**

The accompanying notes are an integral part of these Condensed Consolidated Financial Statements.

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ACTIVISION BLIZZARD, INC. AND SUBSIDIARIES

Notes to Condensed Consolidated Financial Statements

(Unaudited)

1. Description of Business and Business Combination

Description of Business

Activision Blizzard, Inc. is a worldwide online, personal computer (PC), console and handheld game publisher. The terms Activision Blizzard, the Company, we, us, and our are used to refer collectively to Activision Blizzard, Inc. and its subsidiaries.

In 2008, a business combination (the Business Combination) by and among Activision, Inc., Sego Merger Corporation, a wholly-owned subsidiary of Activision, Inc., Vivendi S.A. (Vivendi), VGAC LLC, a wholly-owned subsidiary of Vivendi, and Vivendi Games, Inc. (Vivendi Games), a wholly-owned subsidiary of VGAC LLC was consummated. As a result of the consummation of the Business Combination, Activision, Inc. was renamed Activision Blizzard, Inc. (Activision Blizzard).

The common stock of Activision Blizzard is traded on NASDAQ under the ticker symbol ATVI. Vivendi owned approximately 58% of Activision Blizzard s outstanding common stock at March 31, 2010.

We maintain significant operations in the United States, Canada, the United Kingdom (U.K.), France, Germany, Italy, Spain, Australia, Sweden, South Korea, Norway, Denmark, China, and the Netherlands.

Basis of Consolidation and Presentation

Activision Blizzard prepared the accompanying unaudited condensed consolidated financial statements in accordance with the rules and regulations of the Securities and Exchange Commission for interim reporting. As permitted under those rules and regulations, certain notes or other information that are normally required by accounting principles generally accepted in the United States of America (U.S. GAAP) have been condensed or omitted if they substantially duplicate the disclosures contained in the annual audited consolidated financial statements. The unaudited condensed consolidated financial statements should be read in conjunction with the audited consolidated financial statements and notes thereto included in our Annual Report on Form 10-K for the year ended December 31, 2009. In the opinion of management, all adjustments (consisting of normal recurring accruals) considered necessary for fair presentation of our financial position and results of operations in accordance with U.S. GAAP have been included.

The accompanying unaudited condensed consolidated financial statements include the accounts and operations of Activision Blizzard. All intercompany accounts and transactions have been eliminated. The condensed consolidated financial statements have been prepared in conformity with U.S. GAAP. The preparation of the condensed consolidated financial statements in conformity with U.S. GAAP requires management to make estimates and assumptions that affect the amounts reported in the condensed consolidated financial statements. Actual results could differ from these estimates and assumptions.

The prior year condensed consolidated statement of cash flows for the period ended March 31, 2009 has been adjusted to correct immaterial errors related to the elimination of intercompany receivables and payables in the consolidated balance sheets at March 31, 2009 and December 31, 2008 (not included herein). The corrections reduced the accounts receivable and accounts payable line items in the March 31, 2009 consolidated balance sheet by $4 million and reduced the accounts receivable and accounts payable line items in the December 31, 2008 consolidated balance sheet by $236 million. These corrections correspondingly impacted the change in accounts receivable and accounts payable in the condensed consolidated statement of cash flows for the period ended March 31, 2009 by $232 million. These corrections had no impact on net income, earnings (loss) per share or net cash provided by operating, investing and financing activities.

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

The Company considers events or transactions that occur after the balance sheet date, but before the financial statements are issued to provide additional evidence relative to certain estimates or to identify matters that require additional disclosures.

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2. Inventories

Our inventories consist of the following (amounts in millions):

	At March 31, 2010	At December 31, 2009
Finished goods	$ 161	$ 201
Purchased parts and components	33	40
	$ 194	$ 241

3. Intangible assets, net

Intangible assets, net consist of the following (amounts in millions):

	At March 31, 2010			
	Estimated useful lives	Gross carrying amount	Accumulated amortization	Net carrying amount
Acquired definite-lived intangible assets:				
License agreements	3 - 10 years	$ 173	$ (68)	$ 105
Game engines	2 - 5 years	61	(37)	24
Internally developed franchises	11 - 12 years	574	(111)	463
Favorable leases	1 - 4 years	5	(4)	1
Distribution agreements	4 years	18	(12)	6
Acquired indefinite-lived intangible assets:				
Activision trademark	Indefinite	386		386
Acquired trade names	Indefinite	47		47
Total		$ 1,264	$ (232)	$ 1,032

	At December 31, 2009			
	Estimated useful lives	Gross carrying amount	Accumulated amortization	Net carrying amount
Acquired definite-lived intangible assets:				
License agreements	3 - 10 years	$ 173	$ (65)	$ 108
Developed software	1 - 2 years	288	(288)	
Game engines	2 - 5 years	61	(33)	28
Internally developed franchises	11 - 12 years	574	(101)	473
Favorable leases	1 - 4 years	5	(4)	1
Distribution agreements	4 years	18	(10)	8
Other intangibles	0 - 2 years	5	(5)	
Acquired indefinite-lived intangible assets:				
Activision trademark	Indefinite	386		386
Acquired trade names	Indefinite	47		47
Total		$ 1,557	$ (506)	$ 1,051

Amortization expense of intangible assets was $18 million and $49 million for the three months ended March 31, 2010 and 2009, respectively.

The gross carrying amount as of March 31, 2010 and December 31, 2009 in the tables above reflect a new cost basis for license agreements, game engines and internally developed franchises due to impairment charges taken for the year ended December 31, 2009. The new cost basis includes the original gross carrying amount, less accumulated amortization and impairment charges of the impaired assets as of December 31, 2009.

At March 31, 2010, future amortization of definite-lived intangible assets is estimated as follows (amounts in millions):

2010 (remaining nine months)	$	101
2011		96
2012		87
2013		62
2014		54
Thereafter		199
Total	$	599

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4. Income taxes

The income tax expense of $130 million for the three months ended March 31, 2010 reflects an effective tax rate of 25%. The effective tax rate of 25% for the three months ended March 31, 2010 differs from the statutory rate of 35% primarily due to foreign income taxes provided at lower rates, geographic mix in profitability, recognition of California research and development credits and IRC 199 domestic production deductions. We did not record a tax benefit for federal research credits during the quarter ended March 31, 2010 since as of March 31, 2010, unlike in past years, the federal research credit extension had not yet been signed into law.

For the three months ended March 31, 2010, the tax rate is based on our projected annual effective tax rate for 2010, and also includes certain discrete tax items recorded during the period. Our tax expense of $130 million for the three months ended March 31, 2010 reflects an effective tax rate of 25% which differs from the effective tax rate of 0% for the three months ended March 31, 2009 primarily due to tax benefits recorded during the prior period related to the release of valuation allowances on foreign net operating losses and the impact of changes to California tax laws.

5. Software development and intellectual property licenses

The following table summarizes the components of our software development and intellectual property licenses (amounts in millions):

		At March 31, 2010		At December 31, 2009
Internally developed software costs	$	160	$	182
Payments made to third-party software developers		61		52
Total software development costs	$	221	$	234
Intellectual property licenses	$	69	$	83

Amortization, write-offs and impairments are comprised of the following (amounts in millions):

	Three months ended March 31,			
		2010		2009
Amortization of capitalized software development costs and intellectual property licenses	$	101	$	72
Write-offs and impairments		15		

6. Comprehensive income and accumulated other comprehensive loss

Comprehensive Income

The components of comprehensive income for the three months ended March 31, 2010 and 2009 were as follows (amounts in millions):

	Three months ended March 31, 2010	2009
Net income	$ 381	$ 189
Other comprehensive loss:		
Foreign currency translation adjustment	(20)	(2)
Unrealized depreciation on investments, net of taxes		(1)
Other comprehensive loss	(20)	(3)
Comprehensive income	$ 361	$ 186

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The components of accumulated other comprehensive loss at March 31, 2010 and December 31, 2009 were as follows (amounts in millions):

	At March 31, 2010	At December 31, 2009
Foreign currency translation adjustment	$ (42)	$ (22)
Unrealized depreciation on investments, net of deferred income taxes of $(2) for March 31, 2010 and December 31, 2009	(2)	(2)
Accumulated other comprehensive loss	$ (44)	$ (24)

Income taxes were not provided for foreign currency translation items as these are considered indefinite investments in non-U.S. subsidiaries.

7. Cash and Cash Equivalents

Cash and cash equivalents primarily consist of deposits held at major banks and money market funds with original maturities of three months or less at the date of purchase.

The following table summarizes the components of our cash and cash equivalents (amounts in millions):

	At March 31, 2010	At December 31, 2009
Cash and time deposits	$ 294	$ 464
Securities with original maturities of three months or less	40	
Money market funds	2,361	2,304
Total cash and cash equivalents	$ 2,695	$ 2,768

8. Fair value measurements

Fair Value Measurements on a Recurring Basis

FASB literature regarding fair value measurements for financial and non-financial assets and liabilities establishes a three-level fair value hierarchy that prioritizes the inputs used to measure fair value. This hierarchy requires entities to maximize the use of observable inputs and minimize the use of unobservable inputs. The three levels of inputs used to measure fair value are as follows:

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

- Level 2 Observable inputs other than quoted prices included in Level 1, such as quoted prices for similar assets or liabilities in active markets or other inputs that are observable or can be corroborated by observable market data.

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

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

	As of March 31, 2010	Fair Value Measurements at Reporting Date Using: Quoted Prices in Active Markets for Identical Financial Instruments (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)	Balance Sheet Classification
Financial assets:					
Money market funds	$ 2,361	$ 2,361	$	$	Cash and cash equivalents
Securities with original maturities of three months or less	40	40			Cash and cash equivalents
Mortgage backed securities	1		1		Short-term investments
Auction rate securities held through UBS	54			54	Short-term investments
U.S. government agency securities	560	560			Short-term investments
Auction rate securities held through Morgan Stanley Smith Barney LLC	23			23	Long-term investments
ARS rights from UBS(a)	7			7	Other assets current
Total financial assets at fair value	$ 3,046	$ 2,961	$ 1	$ 84	
Financial liabilities:					
Other financial liability	$ (23)	$	$	$ (23)	Other liabilities current
Total financial liabilities at fair value	$ (23)	$	$	$ (23)	

	As of December 31, 2009	Fair Value Measurements at Reporting Date Using: Quoted Prices in Active Markets for Identical Financial Instruments (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)	Balance Sheet Classification
Financial assets:					
Money market funds	$ 2,304	$ 2,304	$	$	Cash and cash equivalents
Mortgage backed securities	2		2		Short-term investments
Auction rate securities held through UBS	54			54	Short-term investments
U.S. government agency securities	389	389			Short-term investments
Auction rate securities held through Morgan Stanley Smith Barney LLC	23			23	Long-term investments
ARS rights from UBS(a)	7			7	Other assets current
Total financial assets at fair value	$ 2,779	$ 2,693	$ 2	$ 84	
Financial liabilities:					
Other financial liability	$ (23)	$	$	$ (23)	Other liabilities current
Total financial liabilities at fair value	$ (23)	$	$	$ (23)	

(a) ARS rights from UBS represent an offer from UBS providing us with the right to require UBS to purchase our ARS held through UBS at par value. To value the ARS rights, we considered the intrinsic value, time value of money, and our assessment of the credit worthiness of UBS.

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Other financial liability represents the earn-out liability from a previous acquisition. The earn-out liability was recorded at fair value at the date of the Business Combination as it will be settled by a variable number of shares of our common stock based on the average closing price for the five business days immediately preceding issuance of the shares. When estimating the fair value, we considered our projection of revenues from the related titles under the earn-out provisions.

There were no changes in the Level 3 table balances as of March 31, 2010 and as a result, no updated Level 3 table is required. The following table provides a reconciliation of the beginning and ending balances of our financial assets and financial liabilities classified as Level 3 by major categories (amounts in millions) at March 31, 2009:

	Level 3			
	Auction rate securities (a)	**ARS rights from UBS (b)**	**Total financial assets at fair value**	**Other financial liabilities**
Balance at January 1, 2009	$ 78	$ 10	$ 88	$ (31)
Total gains or (losses) (realized/unrealized)				
Included in earnings	2	(3)	(1)	
Included in other comprehensive loss	(1)		(1)	
Balance at March 31, 2009	$ 79	$ 7	$ 86	$ (31)
The amount of total gains or (losses) for the period included in earnings attributable to the change in unrealized gains or losses relating to assets still held at March 31, 2009	$ 2	$ (3)	$ (1)	$

(a) Liquidity for these auction rate securities is typically provided by an auction process which allows holders to sell their notes and resets the applicable interest rate at pre-determined intervals, usually every 7 to 35 days. On an industry-wide basis, many auctions have failed, and there is, as yet, no meaningful secondary market for these instruments. Each of the auction rate securities in our investment portfolio at March 31, 2010 has experienced a failed auction and there is no assurance that future auctions for these securities will succeed. An auction failure means that the parties wishing to sell their securities could not be matched with an adequate volume of buyers. In the event that there is a failed auction, the indenture governing the security requires the issuer to pay interest at a contractually defined rate that is generally above market rates for other types of similar instruments. The securities for which auctions have failed will continue to earn interest at the contractual rate and be auctioned every 7 to 35 days until the auction succeeds, the issuer calls the securities or they mature. As a result, our ability to liquidate and fully recover the carrying value of our auction rate securities in the near term may be limited or non-existent.

Consequently, fair value measurements have been estimated using an income-approach model (discounted cash-flow analysis). When estimating the fair value, we consider both observable market data and non-observable factors, including credit quality, duration, insurance wraps, collateral composition, maximum rate formulas, comparable trading instruments, and likelihood of redemption. Significant assumptions used in the analysis include estimates for interest rates, spreads, cash flow timing and amounts, and holding periods of the securities. Assets measured at fair value using significant unobservable inputs (Level 3) represent 3% of our financial assets measured at fair value on a recurring basis.

(b) ARS rights from UBS represent an offer from UBS providing us with the right to require UBS to purchase our ARS held through UBS at par value. To value the ARS rights, we considered the intrinsic value, time value of money, and our assessment of the credit worthiness of UBS.

The carrying amount of cash and cash equivalents, accounts receivable, accounts payable and accrued expenses is reasonable approximation of fair value due to their short-term nature. Our U.S. government agency securities and mortgage-backed securities are carried at fair value with fair values estimated based on quoted market prices or estimated based on quoted market prices of financial instruments with similar characteristics. Both short-term and long-term ARS are carried at fair value with fair values estimated using an income-approach model (specifically, a discounted cash-flow analysis). We carry derivative instruments, including foreign exchange contracts, on the balance sheet as other assets or liabilities at their fair value. The fair value of foreign currency contracts is estimated based on the prevailing exchange rates of the various hedged currencies as of the end of the period.

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Fair Value Measurements on a Non-Recurring Basis

We measure the fair value of certain assets on a non-recurring basis, generally annually or when events or changes in circumstances indicate that the carrying amount of the assets may not be recoverable. For the three month period ended March 31, 2010, there were no impairment charges related to assets that are measured on a non-recurring basis.

The table below presents an intangible asset that is not subject to recurring fair value measurement at December 31, 2009 (amounts in millions):

		Fair Value Measurements at Reporting Date Using			
	As of December 31, 2009	Quoted Prices in Active Markets for Identical Financial Instruments (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)	Total Losses
Non-financial assets:					
Intangible assets, net	$ 278	$	$	$ 278	$ 409
Total non-financial assets at fair value	$ 278	$	$	$ 278	$ 409

In the fourth quarter of fiscal year ending 2009, with the franchise and industry results of the holiday season, our outlook for the console platforms was significantly revised. With the continued economic downturn within our industry in 2009 and the change in the buying habits of casual consumers, we reassessed our overall expectations as of December 31, 2009. We considered these economic changes during our 2010 planning process conducted during the months of November and December, which resulted in a strategy change to focus on fewer title releases in the casual and music genres. As we consider this a triggering event, we updated our future projected revenues streams for certain franchises in the casual games and music genres. We performed recoverability and, where applicable, impairment tests on the related intangible assets in accordance with ASC Subtopic 360-10.

Determining whether impairment has occurred requires various estimates and assumptions, including determining which cash flows are directly related to the potentially impaired asset, the estimated remaining useful life over which cash flows will occur, the amount of these cash flows and the asset s residual value, if any. For intangible assets that did not pass the recoverability test, measurement of an impairment loss requires a determination of fair value, which is based on the best information available. Considering the characteristics of the assets being valued and the availability of information, the Company used the income approach, which presumes that the value of an asset can be estimated by the net economic benefit to be received over the estimated remaining useful life of the asset, discounted to present value. We derived the required cash flow estimates from our historical experience and our internal business plans and applied an appropriate discount rate. Based on this analysis, we recorded impairment charges of $24 million, $12 million and $373 million to license agreements, game engines and internally developed franchises intangible assets, respectively, for the year ended December 31, 2009 within our Activision operating segment.

9. Operating segments and geographic region

Our operating segments are consistent with our internal organizational structure, the manner in which our operations are reviewed and managed by our Chief Executive Officer, our Chief Operating Decision Maker (CODM), the manner in which operating performance is assessed and resources are allocated, and the availability of separate financial information. We do not aggregate operating segments.

Currently, we operate under three operating segments:

Activision Publishing, Inc.

Activision Publishing, Inc. (Activision) is a leading international publisher of interactive software products and peripherals. Activision develops and publishes video games on various consoles, handheld platforms and the PC platform through internally developed franchises and license agreements. Activision currently offers games that operate on the Sony Computer Entertainment, Inc. (Sony) PlayStation 2 (PS2), Sony PlayStation 3 (PS3), Nintendo Co. Ltd. (Nintendo) Wii (Wii), and Microsoft Corporation (Microsoft) Xbox 360 (Xbox 360) console systems the Sony PlayStation Portable (PSP)

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and Nintendo Dual Screen (NDS) handheld devices; the PC; the Apple iPhone; and the handheld game system Nintendo DSi. Our Activision business involves the development, marketing, and sale of products directly, by license, or through our affiliate label program with certain third-party publishers. Activision s products cover diverse game categories including action/adventure, action sports, racing, role-playing, simulation, first-person action, music, and strategy. Activision s target customer base ranges from casual players to core gamers, and children to adults.

Blizzard Entertainment, Inc.

Blizzard Entertainment, Inc. (Blizzard) is a leader in terms of subscriber base and revenues generated in the subscription-based massively multi-player online role-playing game (MMORPG) category. Blizzard internally develops and publishes PC-based computer games and maintains its proprietary online-game related service, Battle.net. Our Blizzard business involves the development, marketing, sales and support of role playing action and strategy games. Blizzard also develops, hosts, and supports its online subscription-based games in the MMORPG category. Blizzard is the development studio and publisher best known as the creator of *World of Warcraft* and the multiple award winning Diablo, StarCraft, and World of Warcraft franchises. Blizzard distributes its products and generates revenues worldwide through various means, including: subscription revenues (which consist of fees from individuals playing *World of Warcraft*, prepaid cards and other value added service revenues); retail sales of physical boxed products; electronic download sales of PC products; and licensing of software to third-party, or related party companies that distribute *World of Warcraft* in Russia, China, and Taiwan.

Activision Blizzard Distribution

Activision Blizzard Distribution (Distribution) consists of operations in Europe that provide warehousing, logistical, and sales distribution services to third-party publishers of interactive entertainment software, our own publishing operations, and manufacturers of interactive entertainment hardware.

The CODM reviews segment performance exclusive of the impact of the deferred net revenues and related cost of sales, stock-based compensation expense, restructuring expense, amortization of intangible assets and purchase price accounting related adjustments, and integration and transaction costs. Information on the operating segments and reconciliations of total net revenues and total segment income (loss) from operations to consolidated net revenues and operating income (loss) for the three months ended March 31, 2010 and 2009 are presented below (amounts in millions):

	Three months ended March 31,			
	2010	**2009**	**2010**	**2009**
	Net revenues		**Income (loss) from operations**	
Activision	$ 337	$ 348	$ 7	$ (27)
Blizzard	306	291	158	143
Distribution	71	85		3
Operating segments total	714	724	165	119
Reconciliation to consolidated net revenues / operating income:				
	594	256	410	167

Net effect from deferral of net revenues and related cost of sales				
Stock-based compensation expense			(44)	(28)
Restructuring			(3)	(15)
Amortization of intangible assets and purchase price accounting related adjustments			(17)	(46)
Integration and transaction costs				(14)
Other*		1		(4)
Consolidated net revenues / operating income	$ 1,308	$ 981	$ 511	$ 179

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Geographic information for the three months ended March 31, 2010 and 2009 is based on the location of the selling entity. Net revenues from external customers by geographic region were as follows (amounts in millions):

	Three months ended March 31, 2010		Three months ended March 31, 2009	
Net revenues by geographic region:				
North America	$	703	$	524
Europe		524		392
Asia Pacific		81		64
Total geographic region net revenues		1,308		980
Other*				1
Total consolidated net revenues	$	1,308	$	981

Net revenues by platform were as follows (amounts in millions):

	Three months ended March 31, 2010		Three months ended March 31, 2009	
Net revenues by platform:				
MMORPG	$	306	$	314
Console		839		503
Hand-held		39		32
PC and other		53		46
Total platform net revenues		1,237		895
Distribution		71		85
Other*				1
Total consolidated net revenues	$	1,308	$	981

**Represents Non-Core activities, which are legacy Vivendi Games divisions or business units that we have exited, divested or wound down as part of our restructuring and integration efforts as a result of the Business Combination. Prior to July 1, 2009, Non-Core activities were managed as a stand-alone operating segment; however, in light of the minimal activities and insignificance of Non-Core activities, as of that date we ceased their management as a separate operating segment and consequently, we are no longer providing separate operating segment disclosure and have reclassified our prior periods segment presentation so that it conforms to the current period s presentation.*

We did not have any single external customer that accounted for 10% or more of consolidated net revenues for the three month periods ended March 31, 2010 or 2009.

10. Goodwill

The changes in the carrying amount of goodwill by operating segment for the three months ended March 31, 2010 are as follows (amounts in millions):

	Activision	Blizzard	Distribution	Total
Balance at December 31, 2009	$ 6,964	$ 178	$ 12	$ 7,154
Tax benefit credited to goodwill	(4)			(4)
Balance at March 31, 2010	$ 6,960	$ 178	$ 12	$ 7,150

The tax benefit credited to goodwill represents the tax deduction resulting from the exercise of stock options that were outstanding and vested at the consummation of the Business Combination and included in the purchase price of Activision, Inc. to the extent that the tax deduction did not exceed the fair value of those options. Conversely, to the extent that the tax deduction did exceed the fair value of those options, the tax benefit is credited to additional paid in capital.

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11. Computation of basic/diluted earnings per common share

The following table sets forth the computation of basic and diluted earnings per common share (amounts in millions, except per share data):

	Three months ended March 31,