ELECTRONIC ARTS 2002 AR

It’s all about the games.

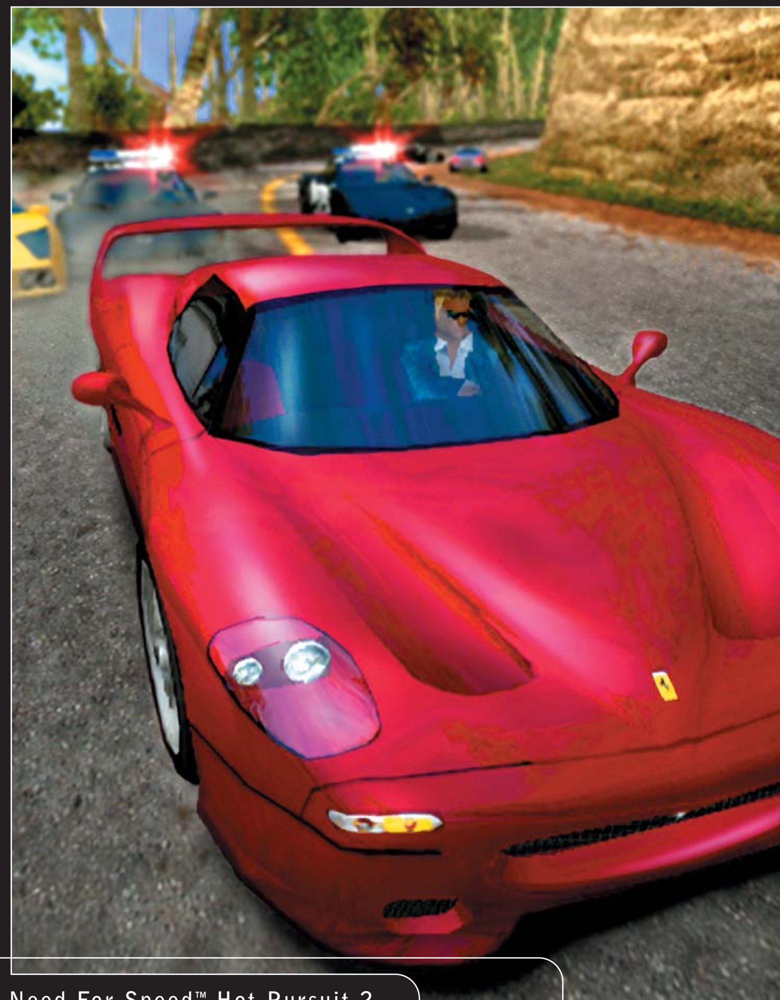
Madden NFL™ 2002

Harry Potter and the Sorcerer's Stone™

The Sims™ Hot Date

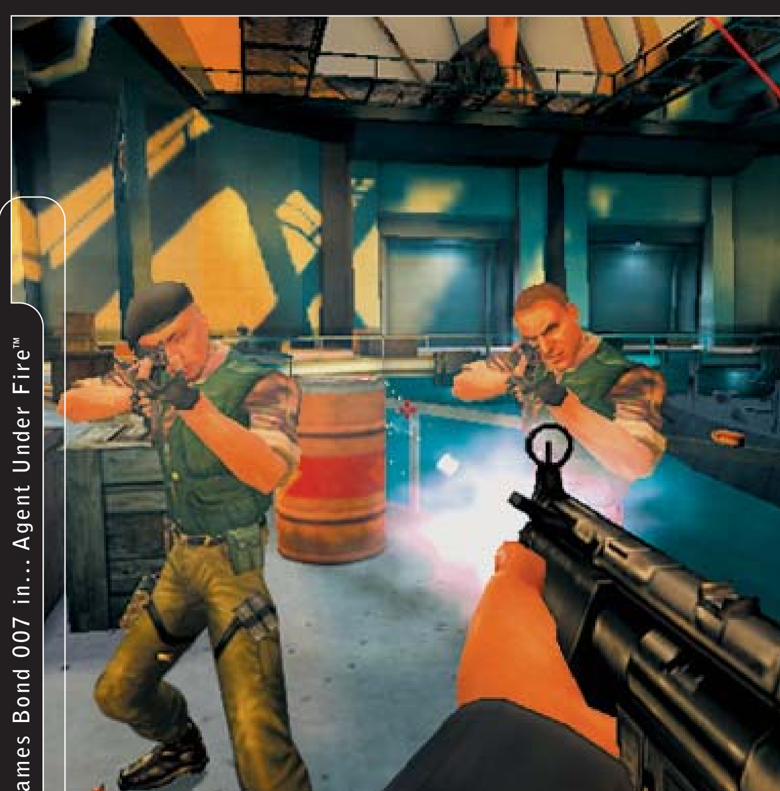
The Lord of the Rings™, The Two Towers™

2002 FIFA World Cup™



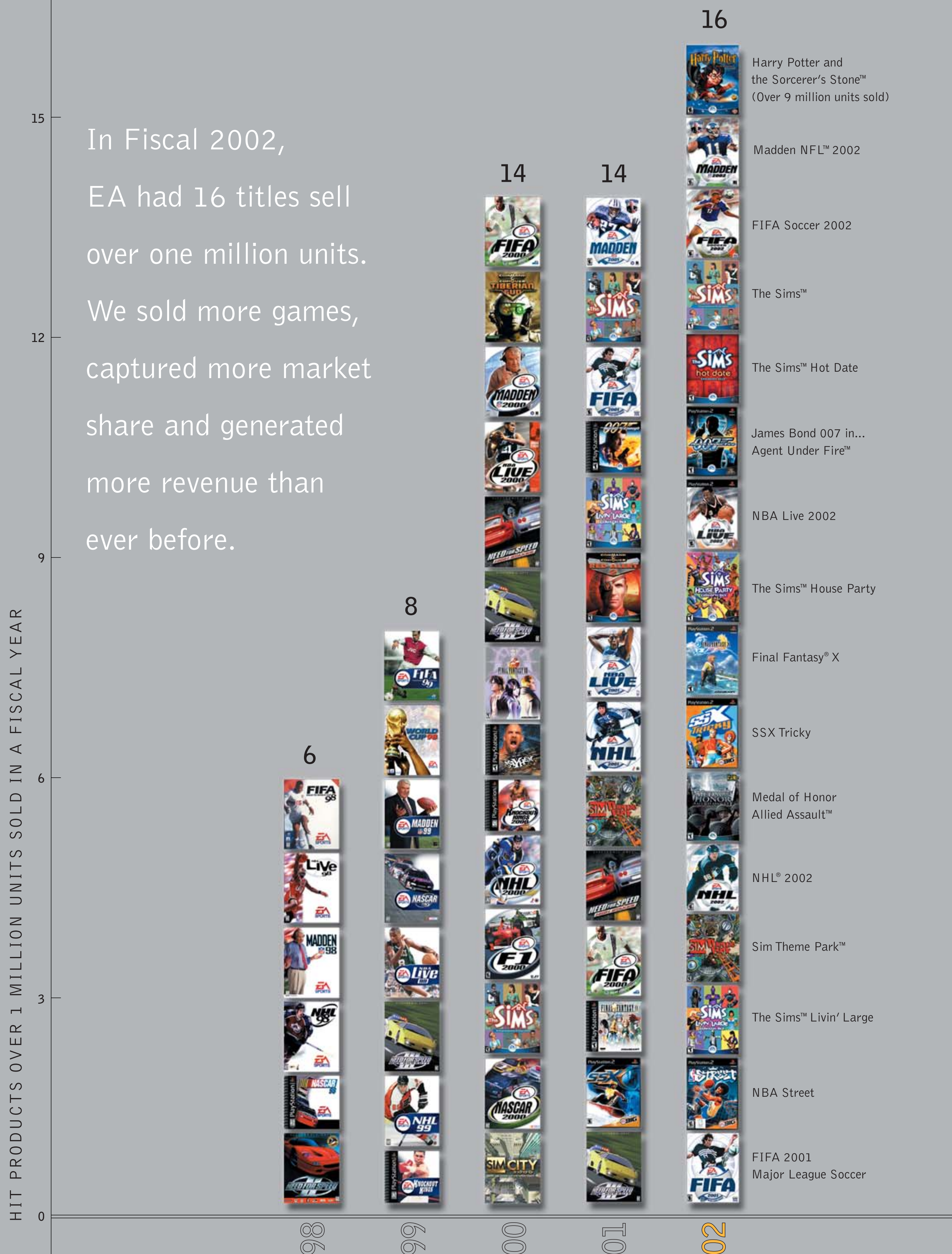
Need For Speed™ Hot Pursuit 2

NBA Street

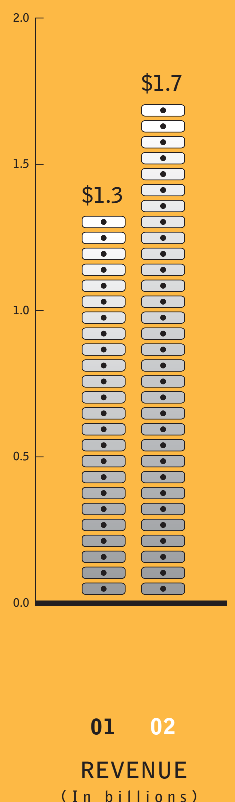


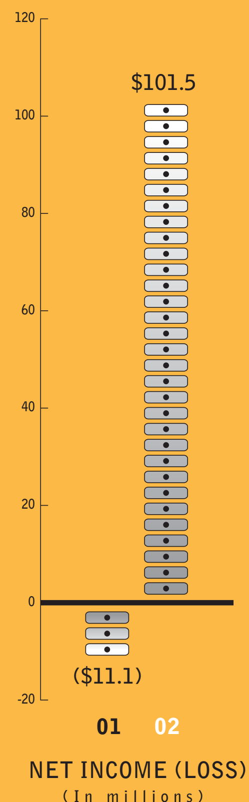
James Bond 007 in... Agent Under Fire™

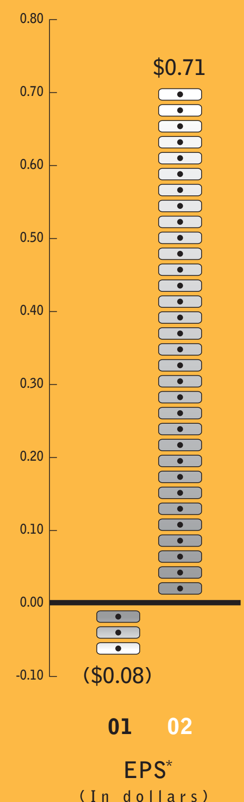
In Fiscal 2002, EA had 16 titles sell over one million units. We sold more games, captured more market share and generated more revenue than ever before.



By Fiscal Year

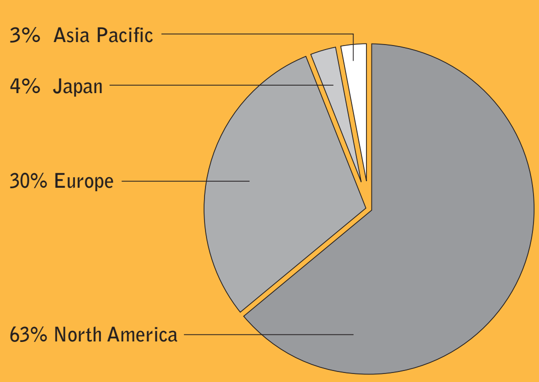


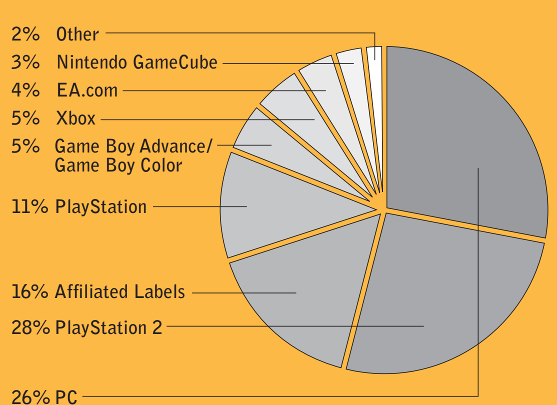




*See Note 1(o) of Notes to Consolidated Financial Statements for an explanation of EPS.

## WORLDWIDE NET REVENUE
Fiscal Year 2002 by Geography




## WORLDWIDE NET REVENUE
Fiscal Year 2002 by Platform



## TO OUR STOCKHOLDERS

In fiscal 2002 we significantly improved our performance versus the previous year and strengthened our position as the industry leader. EA sold more games, captured more market share and generated more revenue than ever before. We capitalized on our strong start in the new console cycle, enhanced our PC business, focused our online operation and grew our portfolio of game franchises. Most importantly, we positioned EA to maintain leadership for the years that lie ahead.

Our success is predicated on long-range strategic planning, accurate forecasting, effective risk management and precise execution. EA measures every decision with an understanding that our industry performs in cycles tied to the launch of new hardware platforms. We have exited the very challenging transition period from 32-bit and 64-bit systems to next generation technology that will provide the basis for continued revenue growth and increased profitability.

In the late 1990s, EA made three key strategic decisions:

- We predicted that Sony's PlayStation®2 computer entertainment system would capture global leadership in the next generation of game consoles. As a result, we concentrated on mastering development for that system, aggressively supporting its launch and becoming the number one publisher for that platform.
- We believed that next generation consoles from Sony, Nintendo and Microsoft would trigger unprecedented growth and make video games a mainstream force in entertainment. We, therefore, focused our resources on building technology tools and libraries that would allow us to create new products on multiple platforms in a cost-effective manner.
- We understood that as the company moved through the difficult console transition, we could help insulate our business by generating greater revenue from our PC games and our global distribution capability. We made it a priority to build and acquire new intellectual properties that would drive market share growth on the PC.

Our strategic planning and effective execution through this most recent console transition allowed EA to generate outstanding results in fiscal 2002.

## FISCAL 2002: A YEAR OF LEADERSHIP, GROWTH AND STRATEGIC POSITIONING

In the past year, EA strengthened its position as the worldwide leader in interactive entertainment. We grew our business across all markets; we provided compelling software that powered consumer migration to next generation consoles; we strengthened our powerful sports franchises; we developed important new properties; and we signed long-term co-publishing agreements with significant new partners.

We increased consolidated net revenue by 30 percent to over $1.7 billion and improved consolidated net income by $113 million to $102 million. Revenues were up in all territories, and in North America we celebrated a major milestone with revenue exceeding $1 billion for the first time. Revenue from our core business increased by 29 percent to over $1.6 billion. With higher sales and focused management of our expenses, operating income from our core business increased $163 million, or 132 percent, over the prior year. Pro forma* net income from our core business increased 106 percent to $217 million, and pro forma net income margin increased five points to 13 percent. We increased EA.com revenue by 83 percent to $77 million and by the fourth quarter had reduced our quarterly pro forma operating expenses by over $16 million compared to the peak quarter in the prior year.

EA's strong performance in fiscal 2002 was made possible by the depth and breadth of our product portfolio and the strength of our worldwide distribution system. Among a year of many blockbusters, three titles stood out:

- *Harry Potter and the Sorcerer's Stone™* – Based on the books and movie, this first game in our multi-year agreement with Warner Bros. became the fastest selling title in EA history. Developed for just four platforms, we sold 9.3 million units worldwide in less than five months. In fiscal 2003, our plans for a new *Harry Potter™* game will include next generation consoles for the first time.
- *The Sims™* – This wholly-owned franchise is now the best-selling PC game of all time and is popular around the world. Our most valuable intellectual property will continue to deliver significant revenue and high margins in the coming years.
- *Madden NFL™ 2002* – This powerhouse franchise sold over 4.5 million units across eight platforms and was the number one selling console game in North America in fiscal 2002.

## FISCAL 2002 PERFORMANCE MEASURED BY FOUR KEY INITIATIVES

At EA, we've established four strategic initiatives for guiding our success. These initiatives are as simple as they are ambitious. Our goals are to be the number one software publisher on next generation consoles; to be number one on the PC; and to be number one online. The fourth key initiative is to make EA the number one people company for high-performance teams and individuals.

### INITIATIVE #1: LEADERSHIP ON NEXT GENERATION CONSOLES

EA was the undisputed global leader on next generation consoles in fiscal 2002. Across all systems we were number one in North America, Europe and Asia Pacific. In Japan, we were the leading Western publisher in a market typically dominated by local companies and titles.

On the PlayStation 2 console, which established a decisive lead among the new consoles, EA was the number one publisher with 28 percent market share and five of the top ten titles in the U.S. in fiscal 2002. Standout titles included *Madden NFL 2002*, *NBA Street*, *James Bond 007 in… Agent Under Fire™*, *FIFA Soccer 2002* and *Final Fantasy® X*, which we distribute in North America for our joint venture partner—SquareSoft.

The year's biggest headline was the launch of two new and impressive game consoles, the Xbox™ video game system from Microsoft and the Nintendo GameCube™. Between the launch in November to the end of our fiscal year, EA was the number one independent publisher on both the Xbox and Nintendo GameCube in the U.S.

By year end, EA stood as the most prolific company on next generation platforms, releasing 18 titles on the PlayStation 2 console, 10 on the Xbox and five on the Nintendo GameCube.

### INITIATIVE #2: LEADERSHIP ON THE PC

EA is the number one entertainment software publisher on the PC in North America, Europe and Asia Pacific, and number two in Japan. We earned a 22 percent market share on the PC in the U.S. and had four of the top five titles in fiscal 2002.

The key driver of this success is the ongoing popularity of *The Sims*. The core product has sold in excess of 6.5 million units and was the best-selling PC game for the second year in a row—an extraordinary achievement. *The Sims* has inspired four expansion packs—*Livin' Large*, *House Party*, *Hot Date* and *Vacation*—to bring total franchise sales to more than 15 million units to date.

EA increased PC market share across all territories with the release of other popular titles including *Medal of Honor Allied Assault*™, *Harry Potter and the Sorcerer's Stone* and *Command & Conquer Renegade*.™

### INITIATIVE #3: LEADERSHIP ONLINE

In fiscal 2002, we increased EA.com℠ revenue 83 percent; we reduced spending and focused on operational efficiencies; we successfully integrated games and customers from our ad-driven Pogo™ site; and we zeroed in on the development of core products such as *Earth & Beyond*™ and the highly anticipated *The Sims Online*.™ We are working hard to reach profitability and are targeting our first break-even quarter in fiscal 2003 when we release *The Sims Online*.

Based on total minutes served, EA.com is the fourth largest website behind only AOL, MSN and Yahoo!. At the end of our fiscal year, EA.com had more than 13 million unique monthly visitors who spent in excess of 4.6 billion minutes on the site—41 percent of the total U.S. online gaming market.

### INITIATIVE #4: TO BE THE NUMBER ONE PEOPLE COMPANY FOR HIGH-PERFORMANCE TEAMS AND INDIVIDUALS

Our strategy for achieving this goal is to work with the very best talent, to provide training and career development and to offer rewarding compensation and benefit programs. This initiative has enhanced the quality of our organization and has attracted the attention of creative people in other sectors of the entertainment industry. Our human resources function has become a strategic weapon for EA—attracting, hiring and retaining the very best talent in our industry. We are committed to making EA the best place to work for people that share our passion for interactive entertainment and performance excellence.

## BUILDING ON LEADERSHIP IN FISCAL 2003 AND INTO THE NEXT TECHNOLOGY CYCLE

Our management team has navigated several cycles of technology transition. We made the difficult decisions that were required to move EA successfully through a challenging period. Now we are well positioned to capture the growth of the new cycle. Revenues from our core packaged goods business will increase, operating margins will expand and our EA.com business will reach its first break-even quarter in fiscal 2003.

In fiscal 2003 EA will build on solid franchises and innovate with new titles.

- Dramatic enhancements and new functionality will appear in blockbuster sports products like *FIFA Soccer*, *Madden NFL Football* and *NBA Live*.
- Games will be inspired by films like *Harry Potter and the Chamber of Secrets*, *The Lord of the Rings* and *James Bond*.
- Stunning new versions of classics like *SimCity*,™ *Need for Speed*™ and *Command & Conquer*™ will be released.
- Distribution agreements with entertainment giants like LEGO System A/S, Fox Interactive, LucasArts, SquareSoft and Capcom will enrich our product portfolio.
- *The Sims Online* will allow subscribers to create characters, build environments and live out fantasies in a persistent state world.

We have long believed that interactive entertainment would grow from a niche market into mainstream entertainment—now we are helping to drive that reality. Revenues from a successful game can rival or exceed those of a successful film, and our demographics are becoming as broad as the audience for television.

As the industry moves into the "sweet spot" of this cycle, EA management is already beginning to plan for the next generation of technology. We are building our team of talented and experienced people, defining our strategic direction and working towards our goal of making EA one of the most exciting and profitable entertainment companies of the 21st century.

Finally, I want to thank our employees, business partners, customers and stockholders for their commitment and support of Electronic Arts.

Sincerely,

Larry Probst

Lawrence F. Probst III
**CHAIRMAN AND CHIEF EXECUTIVE OFFICER**

*Pro forma net income (loss) excludes unusual events or transactions, such as restructuring and asset impairment costs and charges for acquired in-process technology, and also excludes amortization of intangibles and non-cash stock compensation charges. In addition, pro forma net income (loss) for the core business and EA.com provides for the allocation of income taxes on a proportional basis to the respective income or loss from each of these segments. See financial statements beginning on page 42 for GAAP presentation.

This Annual Report, including this Letter to Stockholders, as well as Management's Discussion and Analysis on pages 14 to 40, contains forward-looking statements about circumstances that have not yet occurred. All statements, trend analysis and other information related to markets, our products and trends in revenue, as well as other statements including such words as "anticipate", "believe" or "expect" and statements in the future tense are forward-looking statements. These forward-looking statements are subject to business and economic risks and actual events or our actual future results could differ materially from those set forth in the forward-looking statements due to such risks and uncertainties. We will not necessarily update information if any forward-looking statement later turns out to be inaccurate. Risks and uncertainties that may affect our future results and performance include, but are not limited to those listed under the heading "Risk Factors" at page 39 of this Annual Report and discussed under the same heading in our Annual Report on Form 10-K for the year ended March 31, 2002.

# ELECTRONIC ARTS 20-YEAR HISTORICAL REVIEW

1982

Electronic Arts becomes the 136th company to enter the explosive home computer software market. Our slogan, "We See Farther," signals our intent to be a long-term leader in a new kind of entertainment.



1983

EA ships our first software products for the Apple II and Atari.


1984

*Skyfox* is EA's first #1 title.

EA establishes the industry's first direct field sales force, selling direct to retailers.



1985

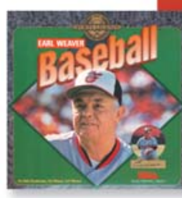
EA launches an affiliated labels program to capitalize on our direct field sales force.

1986

EA ships our first 16-bit games for the IBM PC and Commodore Amiga.

EA becomes the #1 software producer for the Amiga.

EA's development tool, *DeluxePaint*, becomes an instant best-seller on the Amiga and standard among graphic designers.


1987

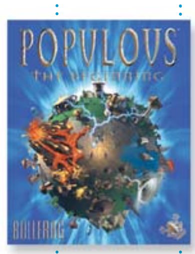
*Chuck Yeager's Advanced Flight Trainer* is EA's first #1 title on the IBM PC.

*Earl Weaver Baseball* is EA's first #1 sports simulation title and the start of our leading sports franchise.

EA opens an office in the U.K. and begins our worldwide expansion.

1988

EA further expands our world presence with our first full year of Australian distribution.

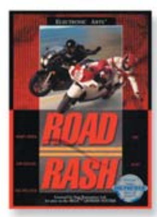



1989

EA becomes a publicly-traded company on the NASDAQ at a split-adjusted price of $1.

*Populous*, published in the U.K., sells 165,000 units in its first year.

EA's U.K. office is named Software House of the Year by The European Golden Joystick Awards.




1990

EA releases our first games for the Sega Genesis and captures an early lead on that platform.

EA becomes the leading independent supplier of 16-bit entertainment software in the U.S.

1991

EA introduces EA SPORTS, the industry's most popular brand.

*John Madden Football* is introduced for the Super Nintendo Entertainment System and becomes the #1 title during the holidays.

EA acquires Distinctive Software, Inc. in Vancouver which becomes EA Canada.

EA has our first $100 million year.


1992

EA acquires Origin Systems, Inc in Austin, TX.

EA extends our global distribution to Japan.

EA has our first $100 million quarter.

82 83 84 85 86 87 88 89 90 91 92


1993

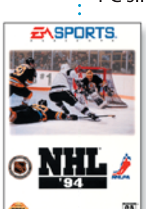
EA acquires the exclusive interactive FIFA license. Our FIFA games will go on to become one of our best-selling sports games.

EA SPORTS tagline "If It's in the Game, It's in the Game" is born.

1994

EA acquires DROSoft in Spain and strengthens our European distribution.

*NHL'94* hits #1 on Sega Genesis and the PC simultaneously.




1995

EA acquires Bullfrog Productions Ltd. in the U.K.

EA strengthens its distribution throughout Europe by opening a Nordic office that distributes in Norway, Sweden, Denmark, Finland and Iceland, and through the acquisition of Kingsoft GmbH in Germany.


*FIFA Soccer '96* is the #1 title across Europe on all platforms.

EA begins to sell products for the Sega Saturn and Sony PlayStation.

1996

EA becomes the leading independent publisher for 32-bit consoles.

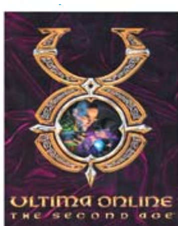
EA makes a strategic investment in Firaxis Software, Inc. and Tiburon Entertainment, developer of *Madden Football* products.

*Need for Speed* is released on the PlayStation. It is one of our top franchises, selling over 19 million units to date.


1997

EA acquires Maxis, the developer of SimCity, and later the creator of The Sims.

EA launches Ultima Online, the first massively multiplayer online game.



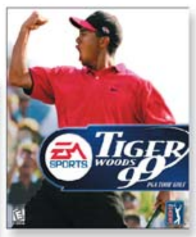

1998

EA acquires Tiburon Entertainment and Westwood Studios, developer of the best-selling *Command & Conquer* series.

ABC Software in Switzerland and Austria joins EA, furthering our strength in Europe.

EA creates EA Square and Square EA joint ventures with Square Company, Ltd.

EA signs an exclusive deal with Tiger Woods and the PGA TOUR.





1999

EA completes our first $1 billion year.

EA creates EA.com and forms a strategic partnership with AOL as the exclusive game provider.

EA signs an exclusive agreement with MGM and Danjaq to bring James Bond to the interactive entertainment market.

*SimCity 3000* is the #1 PC game of the year.



2000

EA releases our first products for the PlayStation 2 console and becomes the #1 publisher on that platform.

EA acquires the DreamWorks Interactive studio, developer of the best-selling *Medal of Honor* game.


EA is awarded the exclusive, worldwide interactive rights for Harry Potter.

*The Sims* is the #1 PC game of the year.

2001

EA releases its first products for the Nintendo GameCube and Xbox.

EA is the #1 publisher on next generation platforms and the PC.

*Harry Potter and the Sorcerer's Stone* becomes our largest launch title ever with over seven million units sold on four platforms in under two months.

*Madden NFL 2002* is the #1 console game in the U.S.

*The Sims* is the #1 PC game of the year for the second year.


2002

EA finishes fiscal 2002 with $1.7 billion in revenue.

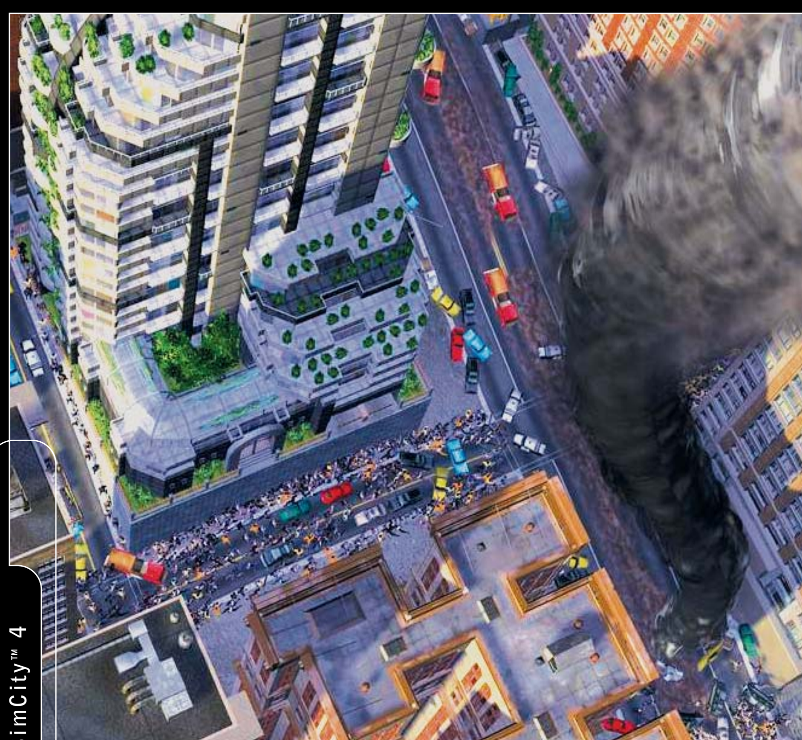
EA finishes fiscal 2002 as the #1 independent publisher on the PlayStation 2, Xbox and Nintendo GameCube.

*The Sims* becomes the #1 selling PC game of all time.


93 94 95 96 97 98 99 00 01 02

Medal of Honor Frontline™

NBA Live 2002



SimCity™ 4

Tiger Woods PGA TOUR® 2002

## FINANCIAL CONTENTS

# SELECTED FIVE-YEAR FINANCIAL DATA

| (In thousands, except per share data) YEARS ENDED MARCH 31, | 2002 | 2001 | 2000 | 1999 | 1998 |
|---|---|---|---|---|---|
| **Income Statement Data** | | | | | |
| Net revenues | $1,724,675 | $1,322,273 | $1,420,011 | $1,221,863 | $ 908,852 |
| Cost of goods sold | 807,611 | 652,242 | 704,702 | 627,589 | 481,233 |
| Gross profit | 917,064 | 670,031 | 715,309 | 594,274 | 427,619 |
| Operating expenses: | | | | | |
| Marketing and sales | 241,109 | 185,336 | 188,611 | 163,407 | 128,308 |
| General and administrative | 107,059 | 104,041 | 92,418 | 76,219 | 57,838 |
| Research and development | 387,736 | 388,928 | 261,966 | 199,375 | 145,732 |
| Amortization of intangibles | 25,418 | 19,323 | 11,989 | 5,880 | — |
| Charge for acquired in-process technology | — | 2,719 | 6,539 | 44,115 | 1,500 |
| Merger costs | — | — | — | — | 10,792 |
| Restructuring and asset impairment charges | 20,303 | — | — | — | — |
| Total operating expenses | 781,625 | 700,347 | 561,523 | 488,996 | 344,170 |
| Operating income (loss) | 135,439 | (30,316) | 153,786 | 105,278 | 83,449 |
| Interest and other income, net | 12,848 | 16,886 | 16,028 | 13,180 | 24,811 |
| Income (loss) before provision for (benefit from) income taxes and minority interest | 148,287 | (13,430) | 169,814 | 118,458 | 108,260 |
| Provision for (benefit from) income taxes | 45,969 | (4,163) | 52,642 | 45,414 | 35,726 |
| Income (loss) before minority interest | 102,318 | (9,267) | 117,172 | 73,044 | 72,534 |
| Minority interest in consolidated joint venture | (809) | (1,815) | (421) | (172) | 28 |
| Net income (loss) | $ 101,509[a] | $ (11,082)[b] | $ 116,751[c] | $ 72,872[d] | $ 72,562[e] |
| Net income per share: | | | | | |
| Basic | N/A | N/A | $ 0.93 | $ 0.60 | $ 0.62 |
| Diluted | N/A | N/A | $ 0.88 | $ 0.58 | $ 0.60 |
| Number of shares used in computation: | | | | | |
| Basic | N/A | N/A | 125,660 | 121,495 | 117,734 |
| Diluted | N/A | N/A | 132,742 | 126,545 | 121,917 |

| (In thousands, except per share data)<br>**YEARS ENDED MARCH 31,** | **2002** | **2001** | **2000** | **1999** | **1998** |
|---|---|---|---|---|---|
| Class A common stock: | | | | | |
| Net income (loss): | | | | | |
| Basic | $ 124,256 | $ 11,944 | N/A | N/A | N/A |
| Diluted | $ 101,509 | $ (11,082) | N/A | N/A | N/A |
| Net income (loss) per share: | | | | | |
| Basic | $ 0.91 | $ 0.09 | N/A | N/A | N/A |
| Diluted | $ 0.71 | $ (0.08) | N/A | N/A | N/A |
| Number of shares used in computation: | | | | | |
| Basic | 136,832 | 131,404 | N/A | N/A | N/A |
| Diluted | 143,142 | 132,056 | N/A | N/A | N/A |
| Class B common stock: | | | | | |
| Net loss, net of retained interest in EA.com | $ (22,747) | $ (23,026) | N/A | N/A | N/A |
| Net loss per share: | | | | | |
| Basic | $ (3.77) | $ (3.83) | N/A | N/A | N/A |
| Diluted | $ (3.77) | $ (3.83) | N/A | N/A | N/A |
| Number of shares used in computation: | | | | | |
| Basic | 6,026 | 6,015 | N/A | N/A | N/A |
| Diluted | 6,026 | 6,015 | N/A | N/A | N/A |

## Balance Sheet Data at Fiscal Year End

| | 2002 | 2001 | 2000 | 1999 | 1998 |
|---|---|---|---|---|---|
| Cash, cash equivalents and short-term investments | $ 796,936 | $ 466,492 | $ 339,804 | $ 312,822 | $ 374,560 |
| Marketable securities | 6,869 | 10,022 | 236 | 4,884 | 3,721 |
| Working capital | 699,561 | 478,701 | 440,021 | 333,256 | 408,098 |
| Long-term investments | — | 8,400 | 8,400 | 18,400 | 24,200 |
| Total assets | 1,699,374 | 1,378,918 | 1,192,312 | 901,873 | 745,681 |
| Total liabilities | 452,982 | 340,026 | 265,302 | 236,209 | 181,713 |
| Minority interest | 3,098 | 4,545 | 3,617 | 2,733 | — |
| Total stockholders' equity | 1,243,294 | 1,034,347 | 923,393 | 662,931 | 563,968 |

Note:
(a) Net income includes restructuring and asset impairment charges of $14.0 million, net of taxes and goodwill amortization of $17.5 million, net of taxes.
(b) Net loss includes one-time acquisition related charges of $1.9 million, net of taxes, incurred in connection with the acquisition of Pogo Corporation made during the year as well as goodwill amortization of $13.3 million, net of taxes.
(c) Net income includes one-time acquisition related charges of $4.5 million, net of taxes, incurred in connection with the acquisition of Kesmai and other business combinations made during the year as well as goodwill amortization of $8.3 million, net of taxes.
(d) Net income includes one-time acquisition related charges of $37.5 million, net of taxes, incurred in connection with the acquisition of Westwood Studios and other business combinations made during the year as well as goodwill amortization of $4.0 million, net of taxes.
(e) Net income includes one-time acquisition related charges of $1.0 million, net of taxes, incurred in connection with the acquisition of the remaining minority ownership interest in Electronic Arts Victor, Inc. as well as merger costs of $7.2 million, net of taxes, associated with the merger with Maxis, offset by a one-time gain on sale of Creative Wonders, LLC in the amount of $8.5 million, net of taxes.

Please refer to Management's Discussion and Analysis of Financial Condition and Results of Operations for discussions of EA Core and EA.com pro forma financial statements.

# MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

This Annual Report, including the "Letter to Stockholders" at pages 3 to 7 and the following "Management's Discussion and Analysis of Financial Condition and Results of Operations", contains forward-looking statements about circumstances that have not yet occurred. All statements, trend analysis and other information contained below relating to markets, our products and trends in revenue, as well as other statements including words such as "anticipate", "believe" or "expect" and statements in the future tense are forward-looking statements. These forward-looking statements are subject to business and economic risks and actual events or our actual future results could differ materially from those set forth in the forward-looking statements due to such risks and uncertainties. We will not necessarily update information if any forward-looking statement later turns out to be inaccurate. Risks and uncertainties that may affect our future results and performance include, but are not limited to, those listed under the heading "Risk Factors" at page 39 of this Annual Report and discussed under the same heading in our Annual Report on Form 10-K for the year ended March 31, 2002.

## CRITICAL ACCOUNTING POLICIES

Management's Discussion and Analysis of Financial Condition and Results of Operations discusses our consolidated financial statements, which have been prepared in accordance with accounting principles generally accepted in the United States of America. The preparation of these consolidated financial statements 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 date of the consolidated financial statements and the reported amounts of revenues and expenses during the reporting period. The policies discussed below are considered by management to be critical because they are both important to the portrayal of our financial condition and results of operations and their application places the most significant demands on management's judgment, with financial reporting results relying on estimates about the effect of matters that are inherently uncertain. Specific risks for these critical accounting policies are described in the following paragraphs. For all of these policies, management cautions that actual results may differ materially from these estimates under different assumptions or conditions.

### SALES ALLOWANCES AND BAD DEBT RESERVES

We derive revenues from sales of our packaged goods product, subscriptions of online service, sales of packaged goods through our online store and website advertising. Product revenue is recognized net of an allowance for returns. We also have stock-balancing programs for our personal computer products that, under certain circumstances and up to a specified amount, allow for the exchange of personal computer products by resellers. We may decide to provide price protection under certain circumstances for our personal computer and video game system products after we analyze: inventory remaining in the channel, the rate of inventory sell through in the channel, and our remaining inventory on hand. We maintain a policy of exchanging products or giving credits, but do not give cash refunds.

We estimate potential future product returns, price protection and stock-balancing programs related to current period product revenue. We analyze historical returns, current sell through of distributor and retailer inventory of our products, current trends in the video game market and the overall economy, changes in customer demand and acceptance of our products and other related factors when evaluating the adequacy of the sales returns and price protection allowances. In addition, management monitors and manages the volume of our sales to retailers and distributors and their inventories as substantial overstocking in the distribution channel can result in high returns or the requirement for substantial price protection in subsequent periods. In the past, actual returns have not generally exceeded our reserves. However, actual returns in any future period are inherently uncertain as unsold products in the distribution channels are exposed to rapid changes in consumer preferences, market conditions or technological obsolescence due to new platforms, product updates or competing products. For example, the risk of product returns for our products on mature platforms may increase as new hardware platforms, such as Xbox, Nintendo GameCube and PlayStation 2, become more popular. While management believes it can make reliable estimates for these matters, if we changed our assumptions and estimates, our returns reserves would change, which would impact the net revenue we report. In addition, if actual returns were significantly greater than the reserves we have established, the actual results would decrease our reported revenue. Conversely, if actual returns were significantly less than our reserves, this would increase our reported revenue.

Similarly, management must use significant judgment and make estimates in connection with establishing allowances for doubtful accounts in any accounting period. Management analyzes customer concentrations, customer credit-worthiness and current economic trends when evaluating the adequacy of the allowance for doubtful accounts. Material differences may result in the amount and timing of our bad debt expense for any period if management made different judgments or utilized different estimates. If our customers experience financial difficulties and are not able to meet their ongoing financial obligations to us, our results of operations may be adversely impacted. For example, in January 2002, one of our retail customers, Kmart, declared bankruptcy. We have adequately reserved for our exposure to Kmart. Our distribution channels have been characterized by change, including consolidations and financial difficulties of certain distributors and retailers.

Our gross accounts receivable balance was $306,365,000 and our allowance for product returns, pricing allowances and doubtful accounts was $115,870,000 as of March 31, 2002. As of March 31, 2001, our gross accounts receivable balance was $264,282,000 and our allowance for product returns, pricing allowances and doubtful accounts was $89,833,000.

## PREPAID ROYALTIES

Prepaid royalties consist primarily of prepayments for manufacturing royalties, co-publishing and/or distribution affiliates and license fees paid to celebrities, professional sports organizations and other organizations for use of their trade name and content. Also included in prepaid royalties are prepayments made to independent software developers under development arrangements that have alternative future uses. Prepaid royalties are expensed at the contractual or effective royalty rate as cost of goods sold based on actual net product sales. We evaluate the future realization of prepaid royalties quarterly and charge to research and development expense any amounts that we deem unlikely to be realized through product sales. We rely on forecasted revenue to evaluate the future realization of prepaid royalties. If actual revenues, or revised forecasted sales, fall below the initial forecasted sales, the charge to research and development expense may be larger than anticipated in any given quarter. Once the charge has been taken to research and development expense, that amount will not be expensed in future quarters when the product has shipped. The current portion of prepaid royalties, included in other current assets, was $65,484,000 at March 31, 2002 and $46,264,000 at March 31, 2001. The long-term portion of prepaid royalties, included in other assets, was $1,164,000 at March 31, 2002 and $9,664,000 at March 31, 2001.

## VALUATION OF LONG-LIVED ASSETS, INCLUDING GOODWILL AND OTHER INTANGIBLE ASSETS

Under current accounting standards, we make judgments about the remaining useful lives of goodwill, purchased intangible assets and other long-lived assets whenever events or changes in circumstances indicate an other than temporary impairment in the remaining value of the assets recorded on our balance sheet. In order to judge the remaining useful life of an asset, management makes various assumptions about the value of the asset in the future. This may include assumptions about future prospects for the business that the asset relates to and typically involves computations of the estimated future cash flows to be generated by these businesses. Please refer to the Operations by Segment discussion of the Management's Discussion and Analysis of Financial Condition and Results of Operations for discussions of EA Core and EA.com. For our EA Core division, our future net cash flows are primarily dependent on the sale of products for play on proprietary video game platforms. The success of our products is affected by the ability to accurately predict which platforms and which products we develop will be successful. Also, our revenues and earnings are dependent on our ability to meet our product release schedules. For our EA.com division, the future net cash flows are dependent on the success of online games. Offering games solely for online play is a substantial departure from our traditional business of selling packaged software games. Because of our inexperience in predicting usage patterns for our games, we may not be effective in achieving success that may otherwise be attainable from offering our games online. Due to these and other factors described in our Risk Factors, we may not realize the future net cash flows necessary to recover our long-lived assets. For example, our product *Majestic*™ and our Platinum offering, which contained certain browser-based entertainment games, were launched with a monthly subscription pricing model and obtained only limited commercial success. Accordingly, we did not realize our projected cash flows and discontinued these offerings as part of EA.com's restructuring plan.

Based on these judgments and assumptions, management determines whether we need to take an impairment charge to reduce the value of the asset stated on our balance sheet to reflect its estimated fair value. Judgments and assumptions about future values and remaining useful lives are complex and often subjective. They can be affected by a variety of factors, including but not limited to, significant negative industry or economic trends, significant changes in the manner or use of the acquired assets or the strategy of our overall business and significant underperformance relative to expected historical or projected future operating results. Although we believe the judgments and assumptions management has made in the past have been reasonable and appropriate, there is nonetheless a high degree of uncertainty and judgment involved. For example, as part of a restructuring plan to reduce EA.com's workforce and consolidate facilities in the fiscal year ended March 31, 2002, we recorded impairment charges to write down certain of EA.com's depreciable assets and certain intangibles to their estimated fair value and to write off certain assets which were abandoned. The impairment charges were based on management's projections regarding the assets' remaining useful lives and future values. The EA.com business is still in the growing stages, therefore evaluating its business and prospects is more difficult than would be the case for a more mature business. We continue to encounter the risks and difficulties faced with launching a new business. We continue to look for ways to streamline the business by consolidating systems and reducing infrastructure costs. Different judgments and assumptions could materially impact our reported financial results. More conservative assumptions of the anticipated future benefits from these businesses would result in greater impairment charges, which would decrease net income and result in lower asset values on our balance sheet. Conversely, less conservative assumptions would result in smaller impairment charges, higher net income and higher asset values. Impairment charges on long-lived assets amounted to $12,818,000 for the fiscal year ended March 31, 2002. There were no impairment charges on long-lived assets for the years ended March 31, 2001 and 2000.

On April 1, 2002, we adopted Statement of Financial Accounting Standards No. 142 ("SFAS 142"), *"Goodwill and Other Intangible Assets"*, which supersedes Accounting Principles Board Opinion No. 17 *"Intangible Assets"*. As a result of adopting this standard, we will continue to amortize finite-lived intangibles, but will no longer amortize certain other intangible assets, most notably goodwill and acquired workforce, which had a net book value at March 31, 2002 of $69,050,000. Amortization of goodwill and acquired workforce totaled approximately $13,125,000 for fiscal 2002, approximately $9,182,000 for fiscal 2001 and approximately $6,411,000 for fiscal 2000. Based on intangible assets as of March 31, 2002, we estimate that amortization of finite-lived intangibles will total approximately $8,700,000 for fiscal 2003. Following adoption of SFAS 142, we will continue to evaluate whether any event has occurred which might indicate that the carrying value of an intangible asset is not recoverable. In addition, SFAS 142 requires that goodwill be subject to at least an annual assessment for impairment by applying a fair value-based test.

## INCOME TAXES

As part of the process of preparing our consolidated financial statements we are required to estimate our income taxes in each of the jurisdictions in which we operate. This process involves estimating our current tax exposures in each jurisdiction including the impact, if any, of additional taxes resulting from tax examinations as well as making judgments regarding the recoverability of deferred tax assets. To the extent recovery of deferred tax assets is not likely based on our estimation of future taxable income in each jurisdiction, a valuation allowance is established. Tax exposures can involve complex issues and may require an extended period to resolve. To determine the quarterly tax rate, we are required to estimate full-year income and the related income tax expense in each jurisdiction. The estimated effective tax rate is adjusted for the tax related to significant unusual items. Changes in the geographic mix or estimated level of annual pre-tax income can effect the overall effective tax rate.

## RESULTS OF OPERATIONS

**Comparison of Fiscal 2002 to 2001:**

### REVENUES

We derive revenues primarily from shipments of entertainment software, which includes EA Studio products for dedicated entertainment systems (that we call video game systems or consoles such as PlayStation, PlayStation 2, Xbox and Nintendo GameCube, and handheld systems such as Game Boy® Advance), EA Studio personal computer products (or PC), Co-Publishing products that are co-published and distributed by us, and Affiliated Label (or AL) products that are published by third parties and distributed by us. We also derive revenues from licensing of EA Studio products and AL products through hardware companies (or OEM), selling subscriptions on our online gaming service, selling advertisements on our online web pages and selling our packaged goods through our online store.

Information about our net revenues for North America and foreign areas for fiscal 2002 and 2001 is summarized below (in thousands):

| | 2002 | 2001 | INCREASE | % CHANGE |
|---|---|---|---|---|
| North America | $ 1,093,244 | $ 831,924 | $ 261,320 | 31.4 % |
| Europe | 519,458 | 386,728 | 132,730 | 34.3 % |
| Asia Pacific | 53,376 | 51,039 | 2,337 | 4.6 % |
| Japan | 58,597 | 52,582 | 6,015 | 11.4 % |
| International | 631,431 | 490,349 | 141,082 | 28.8 % |
| Consolidated Net Revenues | $ 1,724,675 | $ 1,322,273 | $ 402,402 | 30.4 % |

#### North America Net Revenues

The increase in North America net revenues for fiscal 2002 compared to fiscal 2001 was primarily attributable to:

- A 111% increase in PlayStation 2 revenues for the year due to the shipment of key titles such as *Madden NFL 2002*, *James Bond 007 in... Agent Under Fire*, *NBA Street*, *NBA Live 2002* and *SSX Tricky*, a higher installed base of hardware and a strong catalogue business. PlayStation 2 launched in October 2000. Consequently, fiscal 2001 includes six months of revenues as compared to twelve months of revenues for the PlayStation 2 in fiscal 2002.
- The launch of the Xbox platform in North America in November 2001, which generated $73,609,000 in revenues from titles such as *Madden NFL 2002*, *NBA Live 2002*, *James Bond 007 in... Agent Under Fire*, *NASCAR Thunder™ 2002*, *NHL 2002* and *SSX Tricky*.
- The launch of Nintendo GameCube in North America in November 2001, which generated $48,744,000 for the year from key titles such as *Madden NFL 2002*, *James Bond 007 in... Agent Under Fire*, *SSX Tricky*, *NBA Street* and *FIFA Soccer 2002*.
- New revenues were generated by Game Boy Advance of $25,989,000 for the year from key titles including *Harry Potter and the Sorcerer's Stone*, *Madden NFL* 2002 and *NHL 2002*. Also, Game Boy Color generated new revenues of $16,870,000 for the year from titles such as *Harry Potter and the Sorcerer's Stone*, *Madden NFL 2002* and *The World Is Not Enough*.
- Advertising revenues increased by $31,849,000 for the twelve months ended March 31, 2002 as we commenced generating advertising revenues immediately following the launch of our gamesite on the world wide web in October 2000. In addition, advertising revenues were generated from Pogo Corporation's ("Pogo") websites subsequent to the February 2001 acquisition.
- These increases were partially offset by the continued expected decreases in Sony PlayStation and Nintendo 64® ("N64") revenues due to those declining markets and fewer titles shipping compared to the same period in the prior year.

### International Net Revenues

The increase in international net revenues for fiscal 2002 compared to fiscal 2001 was attributable to the following:

- Europe's net revenues increased by 34% compared to the prior year primarily due to higher PlayStation 2, AL and PC sales, partially offset by the expected decrease of revenues from Sony PlayStation. PlayStation 2 launched in November 2000. Consequently, fiscal 2001 includes five months of revenues as compared to twelve months of revenues from the PlayStation 2 in fiscal 2002, resulting in an 80% increase in PlayStation 2 revenues.
- Asia Pacific's net revenues increased by 5% compared to the prior year primarily due to higher PlayStation 2, Game Boy Color® and PC revenue, partially offset by the expected decrease in PlayStation and Nintendo 64 sales, and an unfavorable exchange rate comparison of approximately 10%. PlayStation 2 revenues increased by 46%, partially offset by a 34% decrease in PlayStation revenues in fiscal 2002 as compared to fiscal 2001.
- Japan's net revenues increased by 11% compared to the prior year primarily due to higher AL revenue and revenue generated from sales of PlayStation, Nintendo GameCube and Xbox products, offset by the strong sales of our first PlayStation 2 title, *FIFA Soccer World Championship*, in the prior year and weakness in the Yen currency during fiscal 2002 resulting in a rate decrease of approximately 14% from fiscal 2001. Also, Japan did not benefit from our primary PlayStation 2 releases during the current fiscal year, which have more appeal to the North American market. PlayStation 2 revenues decreased by 50% in fiscal 2002 as compared to fiscal 2001.

Information about our worldwide net revenues by product line for fiscal 2002 and 2001 is presented below (in thousands):

| | 2002 | 2001 | INCREASE/ (DECREASE) | % CHANGE |
|---|---|---|---|---|
| **EA STUDIO:** | | | | |
| PlayStation 2 | $ 482,882 | $ 258,988 | $ 223,894 | 86.4 % |
| PC | 456,292 | 405,256 | 51,036 | 12.6 % |
| PlayStation | 189,535 | 309,988 | (120,453) | (38.9 %) |
| Xbox | 78,363 | — | 78,363 | N/A |
| Nintendo GameCube | 51,740 | — | 51,740 | N/A |
| Game Boy Advance | 43,653 | — | 43,653 | N/A |
| Game Boy Color | 38,026 | — | 38,026 | N/A |
| Advertising | 38,024 | 6,175 | 31,849 | 515.8 % |
| Online Subscriptions | 30,940 | 28,878 | 2,062 | 7.1 % |
| License, OEM and Other | 24,762 | 20,468 | 4,294 | 21.0 % |
| N64 | 18,152 | 67,044 | (48,892) | (72.9 %) |
| Online Packaged Goods | 3,296 | 3,198 | 98 | 3.1 % |
| | 1,455,665 | 1,099,995 | 355,670 | 32.3 % |
| **AFFILIATED LABEL:** | 269,010 | 222,278 | 46,732 | 21.0 % |
| Consolidated Net Revenues | $ 1,724,675 | $ 1,322,273 | $ 402,402 | 30.4 % |

### PlayStation 2 Product Net Revenues

Revenues increased for the twelve months ended March 31, 2002 due to the higher installed base of PlayStation 2 hardware and more titles, including catalogue, available on the platform compared to the same period last year. Major releases for the fiscal year include titles such as *Madden NFL 2002*, *James Bond 007 in… Agent Under Fire*, *FIFA 2002*, *NBA Street*, *NBA Live 2002*, *NCAA Football 2002*, *SSX Tricky*, *NHL 2002* and *NASCAR Thunder 2002*. We released 18 PlayStation 2 titles in the current fiscal year compared to 15 in the same period last year. We expect revenues from PlayStation 2 products to continue to grow in fiscal 2003, but as revenues for these products increase, we do not expect to maintain these growth rates.

### Personal Computer Product Net Revenues

The increase in sales of PC products for the twelve months ended March 31, 2002 compared to the same period last year was primarily due to the continued strong sales of *The Sims*, which shipped over two years ago. Key current year releases were *Harry Potter and the Sorcerer's Stone*, *The Sims Hot Date Expansion Pack*, *Medal of Honor Allied Assault*, *Command & Conquer Renegade* and *Madden NFL 2002*. We released 16 PC titles in the twelve months ended March 31, 2002 compared to 18 in the same period last year. *The Sims* continues to be the number one PC title and has now sold over six million copies. Due to the sales of *The Sims* in fiscal 2002, we expect revenues from PC products to be flat or lower in fiscal 2003.

### PlayStation Product Net Revenues

We released five PlayStation titles in the twelve months ended March 31, 2002 compared to 17 titles in the same period last year. As expected, PlayStation sales decreased for the twelve months ended March 31, 2002 compared to the prior year primarily attributable to the transition to next generation console systems and fewer titles released for the product during the current year.

Although our PlayStation products are playable on the PlayStation 2 console, we expect sales of current PlayStation products to continue to decline significantly in fiscal 2003.

Under the terms of a licensing agreement entered into with Sony Computer Entertainment of America in July 1994 (the "Sony Agreement"), as amended, we are authorized to develop and distribute CD-based software products compatible with the PlayStation. Furthermore, under the terms of an additional licensing agreement entered into with Sony Computer Entertainment of America as of April 2000 (the "PlayStation 2 Agreement"), as amended, we are authorized to develop and distribute DVD-based software products compatible with the PlayStation 2. Pursuant to these agreements, we engage Sony to supply its PlayStation and PlayStation 2 CDs and DVDs for distribution by us. Accordingly, we have limited ability to control our supply of PlayStation and PlayStation 2 CD and DVD products or the timing of their delivery.

### Xbox Net Revenues

Following the launch of the Xbox platform in North America in November 2001, we released our first ten Xbox titles during fiscal 2002. Titles released included *Madden NFL 2002*, *NBA Live 2002*, *James Bond 007 in... Agent Under Fire*, *NASCAR Thunder 2002*, *NHL 2002*, *Triple Play™ 2002*, *SSX Tricky*, *Knockout Kings 2002* and *F1 2001*.

### Nintendo GameCube Net Revenues

We released our first five Nintendo GameCube titles, *Madden NFL 2002*, *James Bond 007 in... Agent Under Fire*, *SSX Tricky*, *NBA Street* and *FIFA Soccer 2002*, during fiscal 2002 following the platform's launch in Japan in September 2001 and in North America in November 2001.

### Game Boy Advance Net Revenues

We released our first three Game Boy Advance titles, *Harry Potter and the Sorcerer's Stone*, *Madden NFL 2002* and *NHL 2002* during fiscal 2002.

### Game Boy Color Net Revenues

We released three Game Boy Color titles, *Harry Potter and the Sorcerer's Stone*, *Madden NFL 2002* and *The World is Not Enough* during fiscal 2002.

### Advertising Revenues

We commenced generating advertising revenues in the third quarter of fiscal year 2001 following the launch of our gamesite on the world wide web and the AOL Games Channel in October 2000. In addition, we generated advertising revenue from Pogo's websites subsequent to the purchase of Pogo in February 2001. As a result of establishing our ad business in late fiscal 2001, we experienced significant revenue growth in fiscal 2002. Due to this and continuing uncertainties in the ad market, we will not be able to sustain the same annual growth rate as experienced in fiscal 2002.

### Online Subscription Net Revenues

The increase in online revenues for fiscal 2002 as compared to fiscal 2001 was primarily attributable to the following:

- An increase in the number of paying customers for *Ultima Online*™ to 207,000 as of March 31, 2002 as compared to 203,000 as of March 31, 2001. This increase was primarily due to the continued strong sales of *Ultima Online Third Dawn* and the release of *Ultima Online Lord Blackthorn's Revenge* in February 2002. In addition, the launch of *Motor City Online* in October 2001, which contributed $1,500,000 in subscription revenues for fiscal 2002.
- Offset by a decrease in subscription revenues of $5,000,000 for Gamestorm, Kesmai Corporation ("Kesmai") and Worldplay online games (most of which were transferred to our free service when the EA/AOL site went live in October 2000) in fiscal 2002 as compared to fiscal 2001.

### License, OEM and Other Revenues

The increase in license, OEM and other revenues for the twelve months ended March 31, 2002 was primarily due to a new OEM agreement with a customer in Europe and higher revenues in North America.

### Nintendo 64 Product Net Revenues

We released one N64 title in fiscal 2002 compared to three titles during fiscal 2001. The expected decrease in N64 revenues for the fiscal year, compared to the prior fiscal year, was primarily due to the declining market for N64 products and fewer titles released on this platform in the current fiscal year. We do not intend to release any new N64 products in fiscal 2003.

### Online Packaged Goods Net Revenues

Online Packaged Goods revenues for fiscal 2002 were slightly higher than fiscal 2001 primarily due to the release of *Motor City Online* in October 2001.

### Affiliated Label Product Net Revenues

AL product sales increased for fiscal 2002 compared to the prior fiscal year primarily due to strong sales of hit titles including *Devil May Cry* and *Resident Evil: Code Veronica* resulting from new distribution deals with Capcom as well as *The Simpsons*™ *Road Rage* in the current year. This was partially offset by lower revenues from shipment of Square EA products due to fewer titles released in fiscal 2002 compared to fiscal 2001.

## OPERATIONS BY SEGMENT

Management considers EA.com to be a separate reportable segment. We operate in two principal business segments globally (see Note 2 of the Notes to Consolidated Financial Statements):

- EA Core business segment: creation, marketing and distribution of entertainment software.
- EA.com business segment: creation, marketing and distribution of entertainment software which can be played or sold online, ongoing management of subscriptions of online games and website advertising.

EA.com represents Electronic Arts' online and e-Commerce businesses. EA.com's business includes subscription revenues collected for Internet game play on our websites, website advertising, sales of packaged goods for Internet-only based games and sales of Electronic Arts games sold through the EA.com web store. The Consolidated Statements of Operations includes all revenues and costs directly attributable to EA.com, including charges for shared facilities, functions and services used by EA.com and provided by EA Core. Certain costs and expenses have been allocated based on management's estimates of the cost of services provided to EA.com by EA Core.

Information about our operations by segment for fiscal 2002 and 2001 is presented below (in thousands):

| YEAR ENDED MARCH 31, 2002 | EA CORE (EXCLUDING EA.COM) | EA.COM | ADJUSTMENTS AND ELIMINATIONS | ELECTRONIC ARTS |
|---|---|---|---|---|
| Net revenues from unaffiliated customers | $ 1,647,502 | $ 77,173 | $ — | $ 1,724,675 |
| Group sales | 4,016 | — | (4,016)[a] | — |
| Total net revenues | 1,651,518 | 77,173 | (4,016) | 1,724,675 |
| Cost of goods sold from unaffiliated customers | 794,738 | 12,873 | — | 807,611 |
| Group cost of goods sold | — | 4,016 | (4,016)[a] | — |
| Total cost of goods sold | 794,738 | 16,889 | (4,016) | 807,611 |
| Gross profit | 856,780 | 60,284 | — | 917,064 |
| Operating expenses: | | | | |
| Marketing and sales | 202,749 | 20,496 | 17,864[c] | 241,109 |
| General and administrative | 96,919 | 10,140 | — | 107,059 |
| Research and development | 257,762 | 59,892 | 70,082[b] | 387,736 |
| Network development and support | — | 59,483 | (59,483)[b] | — |
| Customer relationship management | — | 10,599 | (10,599)[b] | — |
| Carriage fee | — | 17,864 | (17,864)[c] | — |
| Amortization of intangibles | 12,888 | 12,530 | — | 25,418 |
| Restructuring and asset impairment charges | — | 20,303 | — | 20,303 |
| Total operating expenses | 570,318 | 211,307 | — | 781,625 |
| Operating income (loss) | 286,462 | (151,023) | — | 135,439 |
| Interest and other income (expense), net | 13,472 | (624) | — | 12,848 |
| Income (loss) before provision for income taxes and minority interest | 299,934 | (151,647) | — | 148,287 |
| Provision for income taxes | 45,969 | — | — | 45,969 |
| Income (loss) before minority interest | 253,965 | (151,647) | — | 102,318 |
| Minority interest in consolidated joint venture | (809) | — | — | (809) |
| Net income (loss) before retained interest in EA.com | $ 253,156 | $ (151,647) | $ — | $ 101,509 |

Allocation of retained interest (in thousands):

| YEAR ENDED MARCH 31, 2002 | EA CORE (EXCLUDING EA.COM) | EA.COM | ADJUSTMENTS AND ELIMINATIONS | ELECTRONIC ARTS |
|---|---|---|---|---|
| Net income (loss) before retained interest in EA.com | $ 253,156 | $ (151,647) | $ — | $ 101,509 |
| Net loss related to retained interest in EA.com | (128,900) | 128,900 | — | — |
| Net income (loss) | $ 124,256 | $ (22,747) | $ — | $ 101,509 |

| YEAR ENDED MARCH 31, 2001 | EA CORE (EXCLUDING EA.COM) | EA.COM | ADJUSTMENTS AND ELIMINATIONS | ELECTRONIC ARTS |
|---|---|---|---|---|
| Net revenues from unaffiliated customers | $ 1,280,172 | $ 42,101 | $ — | $ 1,322,273 |
| Group sales | 2,658 | — | (2,658)[a] | — |
| Total net revenues | 1,282,830 | 42,101 | (2,658) | 1,322,273 |
| Cost of goods sold from unaffiliated customers | 640,239 | 12,003 | — | 652,242 |
| Group cost of goods sold | — | 2,658 | (2,658)[a] | — |
| Total cost of goods sold | 640,239 | 14,661 | (2,658) | 652,242 |
| Gross profit | 642,591 | 27,440 | — | 670,031 |
| Operating expenses: | | | | |
| Marketing and sales | 163,928 | 12,475 | 8,933[c] | 185,336 |
| General and administrative | 93,885 | 10,156 | — | 104,041 |
| Research and development | 248,534 | 77,243 | 63,151[b] | 388,928 |
| Network development and support | — | 51,794 | (51,794)[b] | — |
| Customer relationship management | — | 11,357 | (11,357)[b] | — |
| Carriage fee | — | 8,933 | (8,933)[c] | — |
| Amortization of intangibles | 12,829 | 6,494 | — | 19,323 |
| Charge for acquired in-process technology | — | 2,719 | — | 2,719 |
| Total operating expenses | 519,176 | 181,171 | — | 700,347 |
| Operating income (loss) | 123,415 | (153,731) | — | (30,316) |
| Interest and other income, net | 16,659 | 227 | — | 16,886 |
| Income (loss) before benefit from income taxes and minority interest | 140,074 | (153,504) | — | (13,430) |
| Benefit from income taxes | (4,163) | — | — | (4,163) |
| Income (loss) before minority interest | 144,237 | (153,504) | — | (9,267) |
| Minority interest in consolidated joint venture | (1,815) | — | — | (1,815) |
| Net income (loss) before retained interest in EA.com | $ 142,422 | $ (153,504) | $ — | $ (11,082) |

Allocation of retained interest (in thousands):

| YEAR ENDED MARCH 31, 2001 | EA CORE (EXCLUDING EA.COM) | EA.COM | ADJUSTMENTS AND ELIMINATIONS | ELECTRONIC ARTS |
|---|---|---|---|---|
| Net income (loss) before retained interest in EA.com | $ 142,422 | $ (153,504) | $ — | $ (11,082) |
| Net loss related to retained interest in EA.com | (130,478) | 130,478 | — | — |
| Net income (loss) | $ 11,944 | $ (23,026) | $ — | $ (11,082) |

(a) Represents elimination of intercompany sales of EA Core packaged goods products to EA.com, and represents elimination of royalties paid to EA Core by EA.com for intellectual property rights.
(b) Represents reclassification of Network Development and Support and Customer Relationship Management to Research and Development.
(c) Represents reclassification of amortization of the Carriage Fee to Marketing and Sales.

The following table shows our pro forma results reconciled to the Generally Accepted Accounting Principles ("GAAP") Consolidated Statements of Operations. Our pro forma results do not include unusual events or transactions, such as restructuring and asset impairment costs and charge for acquired in-process technology, and also excludes amortization of intangibles and non-cash stock compensation charges. In addition, income taxes are allocated to EA Core and EA.com at the consolidated effective tax rate (31%) on a pro rata basis. We believe the disclosure of the pro forma net income (loss) and operating profit (loss), which excludes the items noted in the table below, helps investors more meaningfully evaluate the results of our ongoing operations. However, we urge investors to carefully review the GAAP financial information included as part of this Annual Report and compare GAAP financial information with the pro forma financial results disclosed in this Annual Report.

Reconciliation of GAAP to Pro Forma net income (loss) (in thousands):

| FISCAL YEAR ENDED | MARCH 31, 2002 | | | MARCH 31, 2001 | | |
|---|---|---|---|---|---|---|
| | EA CORE (EXCLUDING EA.COM) | EA.COM | ELECTRONIC ARTS | EA CORE (EXCLUDING EA.COM) | EA.COM | ELECTRONIC ARTS |
| Net income (loss) - GAAP | $ 124,256 | $ (22,747) | $ 101,509 | $ 11,944 | $ (23,026) | $ (11,082) |
| Net loss related to retained interest in EA.com (note 1) | 128,900 | (128,900) | — | 130,478 | (130,478) | — |
| Pro forma allocation of income taxes (note 2) | (47,011) | 47,011 | — | (47,586) | 47,586 | — |
| Pro forma net income (loss) | 206,145 | (104,636) | 101,509 | 94,836 | (105,918) | (11,082) |
| Amortization of intangibles | 12,888 | 12,530 | 25,418 | 12,829 | 6,494 | 19,323 |
| Restructuring and asset impairment charges | — | 20,303 | 20,303 | — | — | — |
| Charge for acquired in-process technology | — | — | — | — | 2,719 | 2,719 |
| Non-cash stock compensation for non-employees (note 3) | 2,677 | 422 | 3,099 | 2,479 | 228 | 2,707 |
| Income tax effect on the above items | (4,825) | (10,309) | (15,134) | (4,745) | (2,927) | (7,672) |
| Pro forma net income (loss) excluding the items above | $ 216,885 | $ (81,690) | $ 135,195 | $ 105,399 | $ (99,404) | $ 5,995 |

1) EA Core maintains approximately 85% retained interest in EA.com and is reflected in the Net income - GAAP for EA Core. The pro forma statements exclude the retained interest allocation.
2) The provision for income taxes was allocated between EA Core and EA.com at the worldwide effective tax rate (31%) based on each segment's pro rata share of income or loss. The sum of tax provision for EA Core and EA.com is the same as consolidated tax provision.
3) Total non-cash stock compensation charges are included in Research and Development in GAAP financials, and excluded in the pro forma.

## COSTS AND EXPENSES, INTEREST AND OTHER INCOME, NET, INCOME TAXES AND NET INCOME (LOSS) FOR BOTH EA CORE AND EA.COM SEGMENTS

### COST OF GOODS SOLD

Cost of goods sold for our packaged goods business consists of actual product costs, royalties expense for celebrities, professional sports and other organizations and independent software developers, manufacturing royalties, expense for defective products and operations expense. Cost of goods sold for our subscription business consists primarily of data center and bandwidth costs associated with hosting our websites, credit card fees and royalties for use of EA and third party properties. Cost of goods sold for our advertising business consists primarily of ad serving costs.

### MARKETING AND SALES

Marketing and sales expenses consist of personnel related costs, advertising and marketing and promotional expenses. In addition, marketing and sales includes the amortization of the AOL carriage fee ("Carriage Fee"), which began with the launch of EA.com in October 2000. The Carriage Fee is being amortized straight-line over the term of the AOL agreement.

### GENERAL AND ADMINISTRATIVE

General and administrative expenses consist of personnel and related expenses of executive and administrative staff, fees for professional services such as legal and accounting and allowances for bad debts.

### RESEARCH AND DEVELOPMENT

Research and development expenses consist of personnel-related costs, consulting and equipment depreciation, customer relationship management expenses associated with Electronic Arts' product and online games and write-offs of prepaid royalties. EA.com has research and development expenses incurred by Electronic Arts' studios consisting of direct development costs and related overhead costs (facilities, network and development management and supervision) in connection with the development and production of EA.com online games. Research and development expenses also include product development expenses incurred directly by EA.com.

### NETWORK DEVELOPMENT AND SUPPORT

Network development and support costs consist of expenses associated with development of web content, depreciation on server equipment to support online games, network infrastructure direct expenses, software licenses and maintenance, and network and management overhead.

## Cost of Goods Sold

| | 2002 | % OF NET REVENUES | 2001 | % OF NET REVENUES | % CHANGE |
|---|---|---|---|---|---|
| | $ 807,611,000 | 46.8% | $ 652,242,000 | 49.3% | 23.8% |

Cost of goods sold as a percentage of revenues decreased in fiscal 2002 compared to fiscal 2001 due to:

- Revenues from the Xbox and Nintendo GameCube with lower cost of goods sold as a percentage of revenue.
- Higher mix of PlayStation 2 revenues in the current fiscal year.
- Higher advertising revenues with low cost of goods sold as a percentage of revenue.
- Lower revenue on N64 products with high cost of goods sold as a percentage of revenue.
- Higher AL margins due to a higher number of co-publishing titles with lower cost of goods sold as a percentage of revenue.
- Higher average margins on PC products.

These items were partially offset by:

- Higher cost of goods sold as a percentage of revenues on the PlayStation and PlayStation 2 products as compared to the prior year.
- Revenues from Nintendo Game Boy Advance and Game Boy Color with higher cost of goods sold as a percentage of revenue.
- Lower mix of high margin PC revenues in the current fiscal year.

## Marketing and Sales

| | 2002 | % OF NET REVENUES | 2001 | % OF NET REVENUES | % CHANGE |
|---|---|---|---|---|---|
| | $ 241,109,000 | 14.0% | $ 185,336,000 | 14.0% | 30.1% |

As a percent of revenue, marketing and sales expense in fiscal 2002 was comparable to fiscal 2001 at 14%. Marketing and sales expenses for fiscal 2002 increased 30.1%, primarily attributed to:

- Higher marketing and advertising in North America and Europe for programs to support *Madden NFL 2002*, *James Bond 007 in... Agent Under Fire* , *SSX Tricky*, *Harry Potter and the Sorcerer's Stone*, *FIFA Soccer 2002* and *NBA Live 2002*.
- Higher EA.com marketing and sales expenses due to increased consumer promotions and advertising media placement costs to promote new game offerings, particularly *Majestic* and *Motor City Online*, and higher expenditures associated with selling advertising on both EA.com and Pogo's gamesites.
- The amortization of the AOL Carriage Fee, which began with the launch of EA.com in October 2000.

## General and Administrative

| | 2002 | % OF NET REVENUES | 2001 | % OF NET REVENUES | % CHANGE |
|---|---|---|---|---|---|
| | $ 107,059,000 | 6.2% | $ 104,041,000 | 7.9% | 2.9% |

General and administrative expenses increased 2.9% for fiscal 2002, primarily attributed to:

- $1,000,000 contribution to charity organizations providing support for the September 11th tragedy.
- Increase in payroll and occupancy costs to support the increased growth in North America.
- Increase in bad debt expense of $1,820,000 due to higher product sales.

## Research and Development

| | 2002 | % OF NET REVENUES | 2001 | % OF NET REVENUES | % CHANGE |
|---|---|---|---|---|---|
| Research and development | $ 317,654,000 | 18.4% | $ 325,777,000 | 24.6% | (2.5%) |
| Network development and support | 59,483,000 | 3.5% | 51,794,000 | 3.9% | 14.8% |
| Customer relationship management | 10,599,000 | 0.6% | 11,357,000 | 0.9% | (6.7%) |
| Total research and development | $ 387,736,000 | 22.5% | $ 388,928,000 | 29.4% | (0.3%) |

### RESEARCH AND DEVELOPMENT EXPENSES (EXCLUDING NETWORK DEVELOPMENT AND SUPPORT AND CUSTOMER RELATIONSHIP MANAGEMENT)

Research and development expenses (excluding Network Development and Support and Customer Relationship Management) decreased in absolute dollars by 2.5% for fiscal 2002, primarily attributed to:

- Headcount reductions in EA.com in October 2001 (see Charge for Restructuring and Impairment discussion below).
- Replacement of EA.com's free games channel with Pogo free games.
- Offset by increased payroll costs due to higher headcount in EA studios, net of co-development arrangements.
- Offset by increased spending on EA.com online projects in development, primarily *The Sims Online* and *Earth & Beyond*.™

We expect research and development spending to increase in fiscal 2003 due to an increase in development spending for next generation console products including the PlayStation 2, Xbox and Nintendo GameCube, as well as extending our investment in the PC platform.

### NETWORK DEVELOPMENT AND SUPPORT

Network development and support expenses increased in absolute dollars by 14.8% for fiscal 2002 primarily due to:

- Increased depreciation related to both hardware and internally developed software that began when the site went live in October 2000.
- Increased headcount and network-related costs associated with Pogo.
- Partially offset by reduced consultant costs related to project and site enhancements.

The expense run rate has been reduced as a result of the restructuring. We do not expect expenses to increase in fiscal 2003.

### CUSTOMER RELATIONSHIP MANAGEMENT

Customer relationship management expenses decreased in absolute dollars by 6.7% for fiscal 2002 primarily due to headcount reductions in EA.com that occurred in October 2001 as part of the restructuring plan (see Charge for Restructuring and Impairment discussion below).

## Amortization of Intangibles

| | 2002 | % OF NET REVENUES | 2001 | % OF NET REVENUES | % CHANGE |
|---|---|---|---|---|---|
| | $ 25,418,000 | 1.5% | $ 19,323,000 | 1.5% | 31.5% |

The amortization of intangibles results primarily from the acquisitions of Westwood, Kesmai, DreamWorks Interactive, ABC Software, Pogo and other acquisitions. Amortization of intangibles was $12,888,000 for EA Core and $12,530,000 for EA.com for fiscal 2002. Amortization of intangibles was $12,829,000 for EA Core and $6,494,000 for EA.com for fiscal 2001. The increase in fiscal year 2002 for EA.com, compared to the prior year, was due to the acquisition of Pogo in February 2001.

With the implementation of new accounting pronouncements (see Impact of Recently Issued Accounting Standards on page 38) as of April 2002, we will continue to amortize finite-lived intangibles, but will no longer amortize goodwill and acquired workforce. Amortization of goodwill and acquired workforce totaled approximately $13,125,000 for fiscal 2002 and approximately $9,182,000 for fiscal 2001. Based on intangible assets as of March 31, 2002, we estimate that amortization of finite-lived intangibles will total approximately $8,700,000 for fiscal 2003. Following adoption of SFAS 142, we will continue to evaluate whether any event has occurred which might indicate that the carrying value of an intangible asset is not recoverable. In addition, SFAS 142 requires that goodwill be subject to at least an annual assessment for impairment by applying a fair value-based test. We are in the process of completing an evaluation for impairment of goodwill in accordance with SFAS 142. We believe the implementation of SFAS 142 will not have a material impact on our consolidated financial statements.

## Charge for Acquired In-Process Technology

| | 2002 | % OF NET REVENUES | 2001 | % OF NET REVENUES | % CHANGE |
|---|---|---|---|---|---|
| | $ — | N/A | $ 2,719,000 | 0.2% | (100.0%) |

In connection with the acquisition of Pogo in the fourth fiscal quarter of fiscal 2001, we allocated and expensed $2,719,000 of the $43,333,000 purchase price to acquired in-process technology. At the date of acquisition, this amount was expensed as a non-recurring charge as the in-process technology had not yet reached technological feasibility and had no alternative future uses. Pogo had various projects in progress at the time of the acquisition. As of the acquisition date, costs to complete Pogo projects acquired were expected to be approximately $1,200,000 in future periods. During fiscal 2002, all of these development projects were completed and launched on Pogo gamesites. In conjunction with the acquisition of Pogo, we accrued approximately $100,000 related to direct transaction and other related costs.

This charge was made after we concluded that the in-process technology had not reached technological feasibility and had no alternative future use after taking into consideration the potential for usage of the software in different products and resale of the software.

## Charge for Restructuring and Impairment

| | 2002 | % OF NET REVENUES | 2001 | % OF NET REVENUES | % CHANGE |
|---|---|---|---|---|---|
| | $ 20,303,000 | 1.2% | $ — | N/A | N/M |

During fiscal 2002, we announced a restructuring plan for EA.com to reduce its workforce and consolidate facilities. These restructuring and resulting asset impairment charges were necessary in order to focus on key online priorities and reduce EA.com's operating cost structure. A pre-tax charge of $20,303,000 was recorded in fiscal 2002, consisting of $4,173,000 for workforce reductions, $3,312,000 for consolidation of facilities and other administrative charges and $12,818,000 for the write-off of non-current assets as a direct result of the restructuring. The pre-tax charge of $20,303,000 consisted of $6,836,000 in cash outlays and $13,467,000 in non-cash charges related to the write-offs of non-current assets and facilities. As of March 31, 2002, an aggregate of $4,016,000 in cash had been paid out under the restructuring plan. Of the remaining cash outlay of $2,820,000, $1,590,000 is expected to occur in fiscal 2003 while the remaining $1,230,000 related to future lease payments will occur is fiscal years 2004 and beyond. Adjustments to the restructuring reserves will be made in future periods, if necessary, based upon current events and circumstances.

The restructuring plan resulted in the termination of approximately 270 personnel, or one third of EA.com's workforce, which affected all departments across the organization. The estimated costs for consolidation of facilities are comprised of contractual rental commitments under real estate leases for unutilized office space offset by estimated future sub-lease income. Included in these costs are estimated costs to close offices or consolidate facilities in various locations and costs to writeoff a portion of the assets from these facilities.

In addition, the restructuring efforts required an evaluation of asset impairment in accordance with Statement of Financial Accounting Standards No. 121 ("SFAS 121"), "*Accounting for the Impairment of Long-Lived Assets and for Long-Lived Assets to be Disposed Of*", to adjust these depreciable assets and certain intangibles to their estimated fair value. Management evaluated the impact of consolidating or abandoning certain EA.com technologies and processes and reviewed the effect of changes to EA.com's subscription product offerings in relation to EA.com's asset base. Impairment charges on long-lived assets amounted to $12,818,000 and included $11,177,000 relating to consolidated or abandoned technologies for the EA.com infrastructure and $1,641,000 of goodwill and intangibles impairment charges relating to the EA.com's San Diego and Kesmai studios. There are no assurances that the impairment factors evaluated by management will not change in subsequent periods and accordingly, this could result in additional impairment charges in future periods.

We will continue to evaluate the effectiveness of products, departments, technology and processes and look for ways to consolidate and streamline EA.com operations in an effort to further reduce operating expenses.

## Interest and Other Income, Net

| | 2002 | % OF NET REVENUES | 2001 | % OF NET REVENUES | % CHANGE |
|---|---|---|---|---|---|
| | $ 12,848,000 | 0.7% | $ 16,886,000 | 1.3% | (23.9%) |

Interest and other income, net, decreased in absolute dollars by 23.9% primarily due to lower interest income as a result of lower interest rates in the current year and an increase in the cost of utilizing foreign exchange hedge contracts.

## Income Taxes

| | 2002 | EFFECTIVE TAX RATE | 2001 | EFFECTIVE TAX RATE | % CHANGE |
|---|---|---|---|---|---|
| | $ 45,969,000 | 31.0% | $ (4,163,000) | 31.0% | N/M |

Our effective tax rate was 31.0% for fiscal 2002 and fiscal 2001. At March 31, 2002, we generated a federal income tax net operating loss. This loss will be carried forward to future tax years. At March 31, 2001, we also generated a federal income tax net operating loss. A substantial portion of this loss was utilized in a carryback claim with the remainder being carried forward. The net operating losses for both fiscal 2002 and fiscal 2001 resulted from losses from EA.com's operations as well as stock option deductions. A valuation allowance has not been established on these loss carryforwards or other net deferred tax assets as we believe it is more likely than not that the results of future operations will generate sufficient taxable income to realize them.

## Net Income (loss)

| | 2002 | % OF NET REVENUES | 2001 | % OF NET REVENUES | % CHANGE |
|---|---|---|---|---|---|
| | $ 101,509,000 | 5.9% | $ (11,082,000) | (0.8%) | N/M |

In absolute dollars, reported net income (loss) increased in fiscal 2002 primarily related to higher net revenues, partially offset by higher expenses compared to the same period last year. The increase in expenses was primarily due to increases in marketing and advertising costs to support a higher number of franchise titles. In addition, higher expenses were due to the charge for restructuring and impairment in fiscal 2002.

We believe the disclosure of pro forma net income (loss) and operating profit (loss), which does not include unusual events or transactions, such as restructuring and asset impairment costs and charge for acquired in-process technology, and also excludes amortization of intangibles and non-cash stock compensation charges, helps investors more meaningfully evaluate the results of our ongoing operations. However, we urge investors to carefully review the GAAP financial information included as part of this Annual Report and compare GAAP financial information with the pro forma financial results disclosed in this Annual Report.

Pro forma net income, excluding the items noted above, was $135,195,000 for the fiscal year ended March 31, 2002 and $5,995,000 for the fiscal year ended March 31, 2001. The increase in pro forma net income for the fiscal year ended March 31, 2002 was due to higher revenues and gross profits as compared to the same periods last year. This was partially offset by an increase in marketing and sales expenses to support programs for key titles shipped in the current year.

With the implementation of new accounting pronouncements relating to goodwill and intangible assets (see Impact of Recently Issued Accounting Standards on page 38) as of April 2002, we will continue to amortize finite-lived intangibles, but will no longer amortize goodwill and acquired workforce. Amortization of goodwill and acquired workforce totaled approximately $13,125,000 for fiscal 2002 and approximately $9,182,000 for fiscal 2001. Based on intangible assets as of March 31, 2002 we estimate that amortization of finite-lived intangibles will total approximately $8,700,000 for fiscal 2003. Following adoption of SFAS 142, we will continue to evaluate whether any event has occurred which might indicate that the carrying value of an intangible asset is not recoverable. In addition, SFAS 142 requires that goodwill be subject to at least an annual assessment for impairment by applying a fair value-based test. We are in the process of completing an evaluation for impairment of goodwill in accordance with SFAS 142. We believe the implementation of SFAS 142 will not have a material impact on our consolidated financial statements.

## Comparison of Fiscal 2001 to 2000:

### REVENUES

Information about our net revenues for North America and foreign areas for fiscal 2001 and 2000 is summarized below (in thousands):

| | 2001 | 2000 | INCREASE/ (DECREASE) | % CHANGE |
|---|---|---|---|---|
| North America | $ 831,924 | $ 846,637 | $ (14,713) | (1.7 %) |
| Europe | 386,728 | 486,816 | (100,088) | (20.6 %) |
| Asia Pacific | 51,039 | 53,187 | (2,148) | (4.0 %) |
| Japan | 52,582 | 33,371 | 19,211 | 57.6 % |
| International | 490,349 | 573,374 | (83,025) | (14.5 %) |
| Consolidated Net Revenues | $ 1,322,273 | $ 1,420,011 | $ (97,738) | (6.9 %) |

#### North America Net Revenues

The decrease in North America net revenues for fiscal 2001 compared to fiscal 2000 was primarily attributable to:

- Expected declines in sales of PlayStation and N64 titles due to the beginning of the transition to next generation consoles. PlayStation net revenues decreased 49% and N64 net revenues decreased 46% also due to fewer titles shipping in fiscal 2001 for both platforms.
- A 6% decrease in AL revenues primarily due to the acquisition of an affiliate, DreamWorks Interactive, by us in the fourth quarter of fiscal 2000.
- Offset partially by the launch of PlayStation 2 platform in North America which generated $171,034,000 in revenue for fiscal 2001 from titles such as *Madden NFL 2001*, *SSX*, *NBA Live 2001* and *NHL 2001*. PlayStation 2 revenues in fiscal 2001 did not offset the decrease in PlayStation revenues due to a reduced number of hardware units reaching the market due to hardware component shortages, according to Sony.
- Offset by a 21% increase in PC revenues due to the shipment of key releases including *Command & Conquer Red Alert™ 2* and *The Sims Livin' Large* and continued strong catalog sales of *The Sims* in fiscal 2001.

#### International Net Revenues

The decrease in international net revenues for fiscal 2001 compared to fiscal 2000 was attributable to the following:

- Europe's net revenues decreased 21% primarily due to the console transition, lower AL sales due to product release slips and fewer hit titles released in fiscal 2001, lower PC sales with fewer titles shipping in fiscal 2001, the strong sales of *Command & Conquer Tiberian Sun™* for the PC in fiscal 2000, and weakness in the Euro currency. In addition, PlayStation revenues decreased 43% due to fewer titles shipping during the console transition period in fiscal 2001 with most franchise titles showing significant decreases from fiscal 2000 releases. PlayStation 2 revenues did not offset the decrease in PlayStation revenues due to fewer hardware units reaching the market and the weighting of titles specifically appropriate for the North American market rather than the European market.

- Asia Pacific's net revenues decreased 4%, mainly due to the decrease in PlayStation revenues as there were no significant new titles released in fiscal 2001. This was offset by sales of PlayStation 2 titles such as *SSX* and *FIFA 2001*.
- Offset by Japan's net revenues which increased 58% compared to fiscal 2000 primarily due to the shipment of PlayStation 2 titles such as *FIFA Soccer World Championship*, *FIFA 2001* and *SSX* in fiscal 2001.

Information about our net revenues by product line for fiscal 2001 and 2000 is presented below (in thousands):

| | 2001 | 2000 | INCREASE/ (DECREASE) | % CHANGE |
|---|---|---|---|---|
| **EA STUDIO:** | | | | |
| PC | $ 405,256 | $ 395,522 | $ 9,734 | 2.5 % |
| PlayStation | 309,988 | 586,821 | (276,833) | (47.2 %) |
| PlayStation 2 | 258,988 | — | 258,988 | N/A |
| N64 | 67,044 | 120,415 | (53,371) | (44.3 %) |
| Online Subscriptions | 28,878 | 16,771 | 12,107 | 72.2 % |
| Online Packaged Goods | 3,198 | 2,255 | 943 | 41.8 % |
| License, OEM and Other | 20,468 | 22,894 | (2,426) | (10.6 %) |
| Advertising | 6,175 | — | 6,175 | N/A |
| | 1,099,995 | 1,144,678 | (44,683) | (3.9 %) |
| **AFFILIATED LABEL:** | 222,278 | 275,333 | (53,055) | (19.3 %) |
| Consolidated Net Revenues | $ 1,322,273 | $ 1,420,011 | $ (97,738) | (6.9 %) |

### Personal Computer Product Net Revenues

The increase in sales of PC products for fiscal 2001 was primarily attributable to the continued strong sales of *The Sims*, which shipped in fiscal 2000. Key fiscal 2001 releases were *Command & Conquer Red Alert 2* and *The Sims Livin' Large*. We released 20 PC titles in fiscal 2001 compared to 31 titles in fiscal 2000. *The Sims* continued to be the number one PC title.

### PlayStation Product Net Revenues

We released 17 PlayStation titles in fiscal 2001 compared to 30 in fiscal 2000. As expected, PlayStation sales decreased for fiscal 2001 compared to fiscal 2000 primarily attributable to the PlayStation 2 platform transition. With the exception of *Madden NFL*, all of our franchises experienced significant decreases from fiscal 2000 releases.

### PlayStation 2 Product Net Revenues

We released 15 titles worldwide in fiscal 2001 for the PlayStation 2. Key releases for fiscal 2001 included *Madden NFL 2001*, *SSX*, *FIFA 2001*, *NBA Live 2001* and *NHL 2001*. Revenue was lower than expected due to the shortage of PlayStation 2 hardware in fiscal 2001 resulting from component shortages which limited the number of units that could be manufactured, according to Sony.

### Affiliated Label Product Net Revenues

The decrease in Affiliated Label net revenues for fiscal 2001 compared to fiscal 2000 was primarily due to the strong sales of *Final Fantasy® VIII* in fiscal 2000, our acquisition of DreamWorks Interactive, formerly an AL, in the fourth quarter of fiscal 2000, fewer hit AL product releases and product release slips in Europe.

### N64 Product Net Revenues

We released three N64 titles in fiscal 2001 compared to eight titles during fiscal 2000. The expected decrease in N64 revenues for fiscal 2001, compared to fiscal 2000, was primarily due to fewer releases. The decrease was also due to the weaker market for N64 products in fiscal 2001. The key release for fiscal 2001 was *The World Is Not Enough*.

### Online Net Revenues

The increase in online revenues for fiscal 2001 as compared to fiscal 2000 was attributable to the following:

- The average number of paying customers for *Ultima Online* increased to approximately 200,000 for fiscal 2001 as compared to over 140,000 for fiscal 2000. This increase was due to continued strong sales of *Ultima Online*, the addition of new events and parties within the *Ultima*™ worlds and the release of *Ultima Online Renaissance*™ in April 2000.
- We generated over $5,100,000 in subscription revenues for Kesmai and Worldplay online games for fiscal 2001. These products were not part of EA.com in fiscal 2000 due to the Kesmai acquisition in the fourth quarter of fiscal 2000.

### License, OEM and Other Revenues

The decrease in license, OEM and other revenues for fiscal 2001 as compared to fiscal 2000 was primarily a result of lower license revenue of certain titles on the Game Boy platform.

### Advertising

Following the launch of EA.com on the worldwide web and the AOL Games Channel in October 2000, we began selling advertising on EA.com and AOL properties, including the *Slingo* game. In addition, we generated advertising revenue from Pogo's websites as a result of the purchase of Pogo in February 2001.

## OPERATIONS BY SEGMENT

Information about our operations by segment for fiscal 2001 and 2000 is presented below (in thousands):

| YEAR ENDED MARCH 31, 2001 | EA CORE (EXCLUDING EA.COM) | EA.COM | ADJUSTMENTS AND ELIMINATIONS | ELECTRONIC ARTS |
|---|---|---|---|---|
| Net revenues from unaffiliated customers | $ 1,280,172 | $ 42,101 | $ — | $ 1,322,273 |
| Group sales | 2,658 | — | (2,658)[a] | — |
| Total net revenues | 1,282,830 | 42,101 | (2,658) | 1,322,273 |
| Cost of goods sold from unaffiliated customers | 640,239 | 12,003 | — | 652,242 |
| Group cost of goods sold | — | 2,658 | (2,658)[a] | — |
| Total cost of goods sold | 640,239 | 14,661 | (2,658) | 652,242 |
| Gross profit | 642,591 | 27,440 | — | 670,031 |
| Operating expenses: | | | | |
| Marketing and sales | 163,928 | 12,475 | 8,933[c] | 185,336 |
| General and administrative | 93,885 | 10,156 | — | 104,041 |
| Research and development | 248,534 | 77,243 | 63,151[b] | 388,928 |
| Network development and support | — | 51,794 | (51,794)[b] | — |
| Customer relationship management | — | 11,357 | (11,357)[b] | — |
| Carriage fee | — | 8,933 | (8,933)[c] | — |
| Amortization of intangibles | 12,829 | 6,494 | — | 19,323 |
| Charge for acquired in-process technology | — | 2,719 | — | 2,719 |
| Total operating expenses | 519,176 | 181,171 | — | 700,347 |
| Operating income (loss) | 123,415 | (153,731) | — | (30,316) |
| Interest and other income, net | 16,659 | 227 | — | 16,886 |
| Income (loss) before benefit from income taxes and minority interest | 140,074 | (153,504) | — | (13,430) |
| Benefit from income taxes | (4,163) | — | — | (4,163) |
| Income (loss) before minority interest | 144,237 | (153,504) | — | (9,267) |
| Minority interest in consolidated joint venture | (1,815) | — | — | (1,815) |
| Net income (loss) before retained interest in EA.com | $ 142,422 | $ (153,504) | $ — | $ (11,082) |

Allocation of retained interest (in thousands):

| YEAR ENDED MARCH 31, 2001 | EA CORE (EXCLUDING EA.COM) | EA.COM | ADJUSTMENTS AND ELIMINATIONS | ELECTRONIC ARTS |
|---|---|---|---|---|
| Net income (loss) before retained interest in EA.com | $ 142,422 | $ (153,504) | $ — | $ (11,082) |
| Net loss related to retained interest in EA.com | (130,478) | 130,478 | — | — |
| Net income (loss) | $ 11,944 | $ (23,026) | $ — | $ (11,082) |

| YEAR ENDED MARCH 31, 2000 | EA CORE (EXCLUDING EA.COM) | EA.COM | ADJUSTMENTS AND ELIMINATIONS | ELECTRONIC ARTS |
|---|---|---|---|---|
| Net revenues from unaffiliated customers | $ 1,399,093 | $ 20,918 | $ — | $ 1,420,011 |
| Group sales | 2,014 | — | (2,014)[(a)] | — |
| Total net revenues | 1,401,107 | 20,918 | (2,014) | 1,420,011 |
| Cost of goods sold from unaffiliated customers | 700,024 | 4,678 | — | 704,702 |
| Group cost of goods sold | — | 2,014 | (2,014)[(a)] | — |
| Total cost of goods sold | 700,024 | 6,692 | (2,014) | 704,702 |
| Gross profit | 701,083 | 14,226 | — | 715,309 |
| Operating expenses: | | | | |
| Marketing and sales | 185,714 | 2,897 | — | 188,611 |
| General and administrative | 87,513 | 4,905 | — | 92,418 |
| Research and development | 205,933 | 34,716 | 21,317[(b)] | 261,966 |
| Network development and support | — | 17,993 | (17,993)[(b)] | — |
| Customer relationship management | — | 3,324 | (3,324)[(b)] | — |
| Amortization of intangibles | 10,866 | 1,123 | — | 11,989 |
| Charge for acquired in-process technology | 2,670 | 3,869 | — | 6,539 |
| Total operating expenses | 492,696 | 68,827 | — | 561,523 |
| Operating income (loss) | 208,387 | (54,601) | — | 153,786 |
| Interest and other income, net | 16,017 | 11 | — | 16,028 |
| Income (loss) before provision for income taxes and minority interest | 224,404 | (54,590) | — | 169,814 |
| Provision for income taxes | 52,642 | — | — | 52,642 |
| Income (loss) before minority interest | 171,762 | (54,590) | — | 117,172 |
| Minority interest in consolidated joint venture | (421) | — | — | (421) |
| Net income (loss) | $ 171,341 | $ (54,590) | $ — | $ 116,751 |

(a) Represents elimination of intercompany sales of EA Core packaged goods products to EA.com, and represents elimination of royalties paid to EA Core by EA.com for intellectual property rights.
(b) Represents reclassification of Network Development and Support and Customer Relationship Management to Research and Development.
(c) Represents reclassification of amortization of the Carriage Fee to Marketing and Sales.

The following table shows our pro forma results reconciled to the GAAP Consolidated Statements of Operations. Our pro forma results do not include unusual events or transactions, such as restructuring and asset impairment costs and charge for acquired in-process technology, and also excludes amortization of intangibles and non-cash stock compensation charges. In addition, income taxes are allocated to EA Core and EA.com at the consolidated effective tax rate (31%) on a pro rata basis. We believe the disclosure of the pro forma net income (loss) and operating profit (loss), which excludes the items noted in the table below, helps investors more meaningfully evaluate the results of our ongoing operations. However, we urge investors to carefully review the GAAP financial information included as part of this Annual Report and compare GAAP financial information with the pro forma financial results disclosed in this Annual Report.

Reconciliation of GAAP to Pro Forma net income (loss) (in thousands):

| FISCAL YEAR ENDED | MARCH 31, 2001 | | | MARCH 31, 2000 | | |
|---|---|---|---|---|---|---|
| | EA CORE (EXCLUDING EA.COM) | EA.COM | ELECTRONIC ARTS | EA CORE (EXCLUDING EA.COM) | EA.COM | ELECTRONIC ARTS |
| Net income (loss) - GAAP | $ 11,944 | $ (23,026) | $ (11,082) | $ 116,751 | $ – | $ 116,751 |
| Net loss related to retained interest in EA.com (note 1) | 130,478 | (130,478) | – | 54,590 | (54,590) | – |
| Pro forma allocation of income taxes (note 2) | (47,586) | 47,586 | – | (16,923) | 16,923 | – |
| Pro forma net income (loss) | 94,836 | (105,918) | (11,082) | 154,418 | (37,667) | 116,751 |
| Amortization of intangibles | 12,829 | 6,494 | 19,323 | 10,866 | 1,123 | 11,989 |
| Charge for acquired in-process technology | – | 2,719 | 2,719 | 2,670 | 3,869 | 6,539 |
| Non-cash stock compensation for non-employees (note 3) | 2,479 | 228 | 2,707 | 736 | – | 736 |
| Income tax effect on the above items | (4,745) | (2,927) | (7,672) | (4,424) | (1,548) | (5,972) |
| Pro forma net income (loss) excluding the items above | $ 105,399 | $ (99,404) | $ 5,995 | $ 164,266 | $ (34,223) | $ 130,043 |

1) EA Core maintains approximately 85% retained interest in EA.com and is reflected in the Net income - GAAP for EA Core. The pro forma statements exclude the retained interest allocation.
2) The provision for income taxes was allocated between EA Core and EA.com at the worldwide effective tax rate (31%) based on each segment's pro rata share of income or loss. The sum of tax provision for EA Core and EA.com is the same as consolidated tax provision.
3) Total non-cash stock compensation charges are included in Research and Development in GAAP financials, and excluded in the pro forma.

## COSTS AND EXPENSES, INTEREST AND OTHER INCOME, NET, INCOME TAXES AND NET INCOME (LOSS) FOR BOTH EA CORE AND EA.COM SEGMENTS

### Cost of Goods Sold

| 2001 | % OF NET REVENUES | 2000 | % OF NET REVENUES | % CHANGE |
|---|---|---|---|---|
| $ 652,242,000 | 49.3% | $ 704,702,000 | 49.6% | (7.4%) |

Cost of goods sold as a percentage of revenues decreased in fiscal 2001 due to:

- An increase in sales of higher margin PC titles as a percentage of revenues. Fiscal 2001 included sales on titles such as *The Sims*, *Command & Conquer Red Alert 2* and *The Sims Livin' Large*.
- The introduction of higher margin PlayStation 2 products in fiscal 2001.
- A decrease in sales of lower margin AL and N64 titles.
- An increase in higher margin Online and Advertising revenue.
- Offset by a decrease in sales of PlayStation titles combined with the decrease in average margins on PlayStation products due to a decrease in the average sales price on front line and catalog products.

## Marketing and Sales

| 2001 | % OF NET REVENUES | 2000 | % OF NET REVENUES | % CHANGE |
|---|---|---|---|---|
| $ 185,336,000 | 14.0% | $ 188,611,000 | 13.3% | (1.7%) |

Marketing and sales expenses for fiscal 2001 increased as a percentage of revenue, primarily attributed to:

- Higher EA.com marketing and sales expenses due to increased staff required to support the live game site and advertising campaigns run on the AOL service promoting the Games Channel.
- The amortization of the AOL Carriage Fee, which began with the launch of EA.com in October 2000.
- Offset by lower television and print advertising in North America and Europe due to fewer number of releases compared to fiscal 2000.

## General and Administrative

| 2001 | % OF NET REVENUES | 2000 | % OF NET REVENUES | % CHANGE |
|---|---|---|---|---|
| $ 104,041,000 | 7.9% | $ 92,418,000 | 6.5% | 12.6% |

General and administrative expenses increased 12.6% for fiscal 2001, primarily attributed to:

- The expansion of the EA.com staff and additional administrative-related costs required to support the growth of the EA.com business.
- Increase in bad debts due to a write off of a receivable as a result of the default of payment from a customer in Europe for approximately $1,000,000.
- Increase in depreciation expense for Europe due to the implementation of a new transaction processing system.

## Research and Development

| | | 2001 | % OF NET REVENUES | | 2000 | % OF NET REVENUES | % CHANGE |
|---|---|---|---|---|---|---|---|
| Research and development | $ | 325,777,000 | 24.6% | $ | 240,649,000 | 16.9% | 35.4% |
| Network development and support | | 51,794,000 | 3.9% | | 17,993,000 | 1.3% | 187.9% |
| Customer relationship management | | 11,357,000 | 0.9% | | 3,324,000 | 0.2% | 241.7% |
| Total research and development | $ | 388,928,000 | 29.4% | $ | 261,966,000 | 18.4% | 48.5% |

### RESEARCH AND DEVELOPMENT (EXCLUDING NETWORK DEVELOPMENT AND SUPPORT AND CUSTOMER RELATIONSHIP MANAGEMENT)

Research and development expenses (excluding Network Development and Support and Customer Relationship Management) increased in absolute dollars by 35.4% for fiscal 2001, primarily attributed to:

- Increase in research and development expenses by EA.com (including expenses incurred by EA Core on behalf of EA.com) due to an increase in the number of online projects in development and increased development staff to support these products.
- An increase in development spending for next generation console products including development for the PlayStation 2 console, Xbox and Nintendo GameCube.
- The increase is also due to research and development expenses related to the acquisition of DreamWorks Interactive, a software development company, in the fourth quarter of fiscal 2000.

We released a total of 55 new packaged goods products in fiscal 2001 compared to 69 new products in fiscal 2000. In addition, the EA.com website launched in October 2000, and had over 80 live games.

#### NETWORK DEVELOPMENT AND SUPPORT

The increase in network development and support expenses was primarily due to increased spending for the network infrastructure, and the Games Channel on the AOL service and the amortization of capitalized costs as required under Statement of Position 98-1, *"Accounting for the Costs of Computer Software Developed or Obtained for Internal Use"*, associated with the pre-launch network infrastructure build.

#### CUSTOMER RELATIONSHIP MANAGEMENT

Customer relationship management increased due to increased headcount-related costs associated with the formation of our customer relationship management organization for the live game site.

### Amortization of Intangibles

| | 2001 | % OF NET REVENUES | 2000 | % OF NET REVENUES | % CHANGE |
|---|---|---|---|---|---|
| | $ 19,323,000 | 1.5% | $ 11,989,000 | 0.8% | 61.2% |

The amortization of intangibles resulted primarily from the acquisitions of Westwood, Kesmai, DreamWorks Interactive, ABC Software, Pogo and other acquisitions. Amortization of intangibles was $12,829,000 for EA Core and $6,494,000 for EA.com for fiscal 2001. Amortization of intangibles was $10,866,000 for EA Core and $1,123,000 for EA.com for fiscal 2000.

### Charge for Acquired In-Process Technology

| | 2001 | % OF NET REVENUES | 2000 | % OF NET REVENUES | % CHANGE |
|---|---|---|---|---|---|
| | $ 2,719,000 | 0.2% | $ 6,539,000 | 0.5% | (58.4%) |

#### FISCAL 2001:

In connection with the acquisition of Pogo in the fourth quarter of fiscal 2001, we allocated and expensed $2,719,000 of the $43,333,000 purchase price to acquired in-process technology. At the date of acquisition, this amount was expensed as a non-recurring charge as the in-process technology had not yet reached technological feasibility and had no alternative future uses. Pogo had various projects in progress at the time of the acquisition. As of the acquisition date, costs to complete Pogo projects acquired were expected to be approximately $1,200,000 in future periods. During fiscal 2002, all of these development projects were completed and launched on Pogo gamesites. In conjunction with the acquisition of Pogo, we accrued approximately $100,000 related to direct transaction and other related costs.

#### FISCAL 2000:

- In connection with the acquisition of Kesmai by EA.com in the fourth quarter of fiscal 2000, we allocated and expensed $3,869,000 of the purchase price to acquired in-process technology.
- In connection with the acquisitions of two development companies by EA Core, made in the second and fourth quarters of fiscal 2000, we allocated and expensed $2,670,000 of the purchase price to acquired in-process technology.

These charges were made after we concluded that the in-process technology had not reached technological feasibility and had no alternative future use after taking into consideration the potential for usage of the software in different products and resale of the software.

### Interest and Other Income, Net

| | 2001 | % OF NET REVENUES | 2000 | % OF NET REVENUES | % CHANGE |
|---|---|---|---|---|---|
| | $ 16,886,000 | 1.3% | $ 16,028,000 | 1.1% | 5.4% |

Interest and other income, net, increased in absolute dollars primarily due to higher interest income as a result of higher average cash balances and investing in higher yielding taxable securities in fiscal 2001. Those gains were partially offset by realized gains on sales of marketable securities in fiscal 2000.

### Income Taxes

| | 2001 | EFFECTIVE TAX RATE | 2000 | EFFECTIVE TAX RATE | % CHANGE |
|---|---|---|---|---|---|
| | $ (4,163,000) | 31.0% | $ 52,642,000 | 31.0% | (107.9%) |

Our effective tax rate was 31.0% for fiscal 2001 and fiscal 2000. At March 31, 2001, we generated a federal income tax net operating loss. A substantial portion of this loss was utilized in a carryback claim with the remainder being carried forward. A valuation allowance was not established on this loss carryforward or other net deferred tax assets as we believed it was more likely than not that the results of future operations would generate sufficient taxable income to realize them.

### Net Income (loss)

| | 2001 | % OF NET REVENUES | 2000 | % OF NET REVENUES | % CHANGE |
|---|---|---|---|---|---|
| | $ (11,082,000) | (0.8%) | $ 116,751,000 | 8.2% | (109.5%) |

In absolute dollars, reported net income (loss) decreased in fiscal 2001 primarily related to lower revenues as well as higher costs and expenses compared to fiscal 2000. The decrease in revenues was primarily due to the beginning of the transition period to next generation console systems. The increase in expenses was primarily due to increases in development of next generation console products in the Core business and the investment in EA.com, including expenses to build network and online game products and to launch our game sites in October 2000.

Excluding goodwill, non-cash compensation and one-time charges in the amount of $17,077,000, net of taxes, for fiscal 2001, net income would have been $5,995,000. Excluding goodwill, non-cash compensation and one-time charges in the amount of $13,292,000, net of taxes, for fiscal 2000, net income would have been $130,043,000.

## LIQUIDITY AND CAPITAL RESOURCES

### EA CORE AND EA.COM

As of March 31, 2002, our working capital was $699,561,000 compared to $478,701,000 at March 31, 2001. Cash, cash equivalents and short-term investments increased by $330,444,000 in fiscal 2002. We generated $284,971,000 of cash from operations, $98,840,000 of cash through the sale of equity securities under our stock plans, offset by $51,518,000 of cash used in capital expenditures during fiscal 2002.

Reserves for bad debts and sales returns increased from $89,833,000 at March 31, 2001 to $115,870,000 at March 31, 2002. Reserves have been charged for returns of product and price protection credits issued for products sold in prior periods. Management believes these reserves are adequate based on historical experience and its current estimate of potential returns and allowances.

Our principal source of liquidity is $796,936,000 in cash, cash equivalents and short-term investments and $6,869,000 in marketable securities. We expect that for the foreseeable future, our operating expenses will constitute a significant use of our cash balances. Management believes the existing cash, cash equivalents, short-term investments, marketable securities and cash generated from operations will be sufficient to meet cash and investment requirements on both a short-term and long-term basis. However, our ability to maintain sufficient liquidity could be affected by various risks and uncertainties, including but not limited to, those related to customer demand and acceptance of titles on new platforms and new title versions on existing platforms, our ability to collect our accounts receivable as they become due, successfully achieving our product release schedules and attaining our forecasted sales objectives, the impact of competition, the economic conditions in the domestic and international markets, seasonality in operating results, risks of product returns and the other risks listed in the "Risk Factors" section.

## EA.COM

Included in the amounts above is the following for the EA.com business:

- With the exception of the proceeds from the sale of stock and warrant to AOL in fiscal 2000 in the amount of $20,000,000, to date, EA.com has been funded solely by Electronic Arts. This funding has been accounted for as capital contributions from Electronic Arts. Excess cash generated from operations is transferred to Electronic Arts, and has been accounted for as a return of capital. We anticipate these funding procedures will continue in the near-term. However, Electronic Arts may, at its discretion, provide funds to EA.com under a debt arrangement, instead of treating such funding as a capital contribution.
- During fiscal 2002, EA.com used $99,696,000 of cash in operations (including payments to AOL of approximately $11,250,000), $13,112,000 in capital expenditures for computer equipment, network infrastructure, internal use software and related third party software, offset by $114,837,000 provided through the capital contributions from Electronic Arts. As a result of the net operating loss generated, we realized a tax benefit of approximately $47,011,000.
- During fiscal 2001, EA.com used $132,210,000 of cash in operations (including payments to AOL of approximately $11,250,000), $68,887,000 in capital expenditures for computer equipment, network infrastructure, internal use software and related third party software, $43,333,000 for the acquisition of Pogo, excluding cash received of $762,000, offset by $245,141,000 provided through the capital contributions from Electronic Arts. As a result of the net operating loss generated, we realized a tax benefit of approximately $47,586,000.

Under the AOL agreement entered into in November 1999, EA.com is required to pay $81,000,000 to AOL over the life of the five-year agreement. Of this amount, $36,000,000 was paid upon signing the agreement with the remainder due in four equal annual installments beginning with the first anniversary of the initial payments. EA.com paid AOL $11,250,000 in both fiscal 2001 and 2002.

Future liquidity needs of EA.com will be met by Electronic Arts as Electronic Arts intends to continue to fund the cash requirements of EA.com for the foreseeable future.

## OTHER COMMITMENTS

### Advertising Commitments

We made a commitment to spend $15,000,000 in offline media advertisements promoting our online games, including those on the AOL service, prior to March 31, 2005. As of March 31, 2002, we have spent approximately $3,500,000 against this commitment.

On February 7, 2000, we acquired Kesmai from News America Corporation ("News Corp") in exchange for $22,500,000 in cash and approximately 206,000 shares of our existing common stock valued at $8,650,000. We agreed to spend $12,500,000 through the period ended June 1, 2002 in advertising with News Corp or any of its affiliates. In addition, if certain conditions are met, including that a qualified public offering of Class B common stock does not occur within twenty-four months of News Corp's purchase of such shares and all of the Class B outstanding shares have been converted to Class A common stock, then (1) News Corp has the right to (i) exchange Class B common stock for approximately 206,000 shares of Class A common stock, and (ii) receive cash from Electronic Arts in the amount of $9,650,000, and (2) we will agree to spend an additional $11,675,000 in advertising with News Corp and its affiliates.

### Lease Commitments

We lease certain of our current facilities and certain equipment under non-cancelable capital and operating lease agreements. We are required to pay property taxes, insurance and normal maintenance costs for certain of our facilities and will be required to pay any increases over the base year of these expenses on the remainder of our facilities.

In February of 1995, we entered into a build-to-suit lease with a financial institution on our headquarter's facility in Redwood City, California, which was extended in July of 2001 and runs through July of 2006. We accounted for this arrangement as an operating lease in accordance with Statement of Financial Accounting Standards No. 13 ("SFAS 13"), *"Accounting for Leases"*, as amended. Existing campus facilities developed in phase one comprise a total of 350,000 square feet and provide space for sales, marketing, administration and research and development functions. We have an option to purchase the property (land and facilities) for $145,000,000 or, at the end of the lease, to arrange for (1) an additional extension of the lease or (2) sale of the property to a third party with us retaining an obligation to the owner for the difference between the sale price and the guaranteed residual value of up to $128,900,000 if the sales price is less than this amount, subject to certain provisions of the lease.

In December 2000, we entered into a second build-to-suit lease with a financial institution for a five year term from December 2000 to expand our headquarter's facilities and develop adjacent property adding approximately 310,000 square feet to our campus. We expect to complete construction in June of 2002. We accounted for this arrangement as an operating lease in accordance with SFAS 13, as amended. The facilities will provide space for marketing, sales and research and development. We have an option to purchase the property for $127,000,000 or, at the end of the lease, to arrange for (1) an extension of the lease or (2) sale of the property to a third party with us retaining an obligation to the owner for the difference between the sale price and the guaranteed residual value of up to $118,800,000 if the sales price is less than this amount, subject to certain provisions of the lease.

Lease rates are based upon the Commercial Paper Rate. The two lease agreements described above require us to maintain certain financial covenants, all of which we were in compliance with as of March 31, 2002.

### Letters of Credit

In connection with our purchases of N64 cartridges and Nintendo GameCube optical disks for distribution in North America, Nintendo requires us to provide irrevocable letters of credit prior to Nintendo's acceptance of purchase orders from us for purchases of these cartridges and optical disks. For purchases of N64 cartridges and Nintendo GameCube optical disks for distribution in Japan and Europe, Nintendo requires us to make cash deposits.

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

The products published by EA Studios are designed and created by our in-house designers and artists and by independent software developers ("independent artists"). We typically pay the independent artists royalties based on the sales of the specific products, as defined in the related independent artist agreements. Advance payments on these royalties are paid to independent artists upon meeting deliverables as detailed in the contractual agreement. In addition, certain celebrity, league and content license contracts contain minimum guarantee payments and marketing commitments that are not dependent on any deliverables. Celebrities and organizations with whom we have contracts include: FIFA, NASCAR, John Madden, National Basketball Association, PGA TOUR, Tiger Woods, National Hockey League, Formula One, Warner Bros. (Harry Potter), MGM/Danjaq (James Bond) and National Football League. These minimum guarantee payments and marketing commitments are included in the table below.

Summary of minimum contractual obligations and commercial commitments as of March 31, 2002 (in thousands):

| | CONTRACTUAL OBLIGATIONS | | | | | COMMERCIAL COMMITMENTS | | |
|---|---|---|---|---|---|---|---|---|
| FISCAL YEAR ENDED MARCH 31, | LEASES | ADVERTISING | MINIMUM GUARANTEES | AOL | MARKETING | BANK AND OTHER GUARANTEES | LETTERS OF CREDIT | TOTAL |
| 2003 | $ 18,288 | $ 14,000 | $ 35,663 | $11,250 | $ 19,541 | $ 1,050 | $ 1,122 | $ 100,914 |
| 2004 | 15,011 | 3,500 | 22,812 | 11,250 | 16,554 | 171 | — | 69,298 |
| 2005 | 11,354 | 4,500 | 15,137 | — | 11,159 | 171 | — | 42,321 |
| 2006 | 10,810 | — | 16,483 | — | 4,572 | 171 | — | 32,036 |
| 2007 | 9,122 | — | 3,145 | — | 3,571 | 170 | — | 16,008 |
| Thereafter | 11,609 | — | 2,260 | — | 3,571 | 170 | — | 17,610 |
| | $ 76,194 | $ 22,000 | $ 95,500 | $22,500 | $ 58,968 | $ 1,903 | $ 1,122 | $ 278,187 |

## TRANSACTIONS WITH RELATED PARTIES

### Square EA

In May 1998, we completed the formation of a new joint venture with Square Co., Ltd. ("Square"), a leading developer and publisher of entertainment software in Japan. In North America, the companies formed Square Electronic Arts, LLC ("Square EA"), which has exclusive publishing rights in North America for future interactive entertainment titles created by Square. Additionally, we have the exclusive right to distribute in North America products published by this joint venture. Either party may terminate the existence of Square EA and the distribution agreement effective March 31, 2003. We own a 30% minority interest in this joint venture while Square owns 70%. This joint venture is accounted for under the equity method.

In March 2002, we announced a publishing and distribution partnership with Square for *Final Fantasy® X* in Asia Pacific. The deal grants us the rights to distribute *Final Fantasy X International* for the PlayStation 2 computer entertainment system in Taiwan, Hong Kong, Singapore, Thailand, Malaysia and Korea.

We generated $80,847,000 in net revenues from sales of Square EA products in fiscal 2002, $106,586,000 in net revenues from sales of Square EA products in fiscal 2001 and $83,657,000 in net revenues from sales of Square EA products in fiscal 2000.

## IMPACT OF RECENTLY ISSUED ACCOUNTING STANDARDS

In June 2001, the Financial Accounting Standards Board ("FASB") issued SFAS 142, "*Goodwill and Other Intangible Assets*", which supersedes Accounting Principles Board Opinion No. 17 ("APB 17"), "*Intangible Assets*". SFAS 142 addresses the accounting treatment for goodwill and other intangible assets acquired individually or with a group of other assets upon their acquisition, but not acquired in a business combination. This statement also addresses how goodwill and other intangible assets should be accounted for after they have been initially recognized in the financial statements. With the adoption of SFAS 142, goodwill is no longer subject to amortization over its estimated useful life; rather, goodwill will be subject to at least an annual assessment for impairment by applying a fair-value-based test. Also, if the benefit of an intangible asset is obtained through contractual or other legal rights, or if the intangible asset can be sold, transferred, licensed, rented or exchanged, an acquired intangible asset should be separately recognized. The terms of SFAS 142 are effective as of the beginning of the first quarter of the fiscal year beginning after December 15, 2001. Certain provisions of SFAS 142 shall be applied to goodwill and other acquired intangible assets for which the acquisition date is after June 30, 2001. On April 1, 2002, we adopted SFAS 142. As a result of adopting this standard, we will continue to amortize finite-lived intangibles, but will no longer amortize certain other intangible assets, most notably goodwill and acquired workforce, which had a net book value at March 31, 2002 of $69,050,000. Amortization of goodwill and acquired workforce totaled approximately $13,125,000 for fiscal 2002, approximately $9,182,000 for fiscal 2001 and approximately $6,411,000 for fiscal 2000. Based on intangible assets as of March 31, 2002, we estimate that amortization of finite-lived intangibles will total approximately $8,700,000 for fiscal 2003. Following adoption of SFAS 142, we will continue to evaluate whether any event has occurred which might indicate that the carrying value of an intangible asset is not recoverable. In addition, SFAS 142 requires that goodwill be subject to at least an annual assessment for impairment by applying a fair value-based test. We are in the process of completing an evaluation for impairment of goodwill in accordance with SFAS 142. We believe the implementation of SFAS 142 will not have a material impact on our consolidated financial statements.

In June 2001, the FASB issued Statement of Financial Accounting Standards No. 143 ("SFAS 143"), "*Accounting for Asset Retirement Obligations*". SFAS 143 addresses financial accounting and reporting for obligations associated with the retirement of tangible long-lived assets and the associated asset retirement costs. This statement applies to legal obligations associated with the retirement of long-lived assets that result from the acquisition, construction, development or normal use of the asset. SFAS 143 is effective for fiscal years beginning after June 15, 2002. We do not expect the adoption of SFAS 143 to have a material impact on our consolidated financial position or results of operations.

In October 2001, the FASB issued Statement of Financial Accounting Standards No. 144 ("SFAS 144"), "*Accounting for the Impairment or Disposal of Long-Lived Assets*", which addresses financial accounting and reporting for the impairment or disposal of long-lived assets. SFAS 144 supersedes SFAS 121, "*Accounting for the Impairment of Long-Lived Assets and for Long-Lived Assets to Be Disposed Of*", and also supersedes the accounting and reporting provisions of APB Opinion No. 30, "*Reporting the Results of Operations-Reporting the Effects of Disposal of a Segment of a Business, and Extraordinary, Unusual and Infrequently Occurring Events and Transactions*", for the disposal of a segment of a business. SFAS 144 is effective for fiscal years beginning after December 15, 2001 and interim periods within those fiscal years. We are in the process of determining the impact of this new accounting standard. We believe the implementation of SFAS 144 will not have a material impact to our consolidated financial statements.

## RISK FACTORS

Our business is subject to many risks and uncertainties which may affect our performance. Some of those risks and uncertainties are as follows:

- Our business is both seasonal and cyclical.
- Our significant investment in EA.com may not be successful or generate profits.
- Acceptance of our online products by paying subscribers is still unproven.
- The business models and technology for e-Commerce and online gaming are still unproven.
- Product development schedules are frequently unreliable, particularly for products for PC and for online play, and make predicting quarterly results difficult.
- Our business, our products and our distribution are subject to increasing regulation directed at content, consumer privacy and online delivery in key territories.
- Our platform licensors are our chief competitors and frequently control the manufacturing of our video game products.
- The current legislative and regulatory environment affecting generally accepted accounting principles is uncertain and volatile, and significant changes in current principles could affect our financial statements going forward.

For a discussion of these and other important risk factors, see the heading "Risk Factors" in our Annual Report on Form 10-K for the year ended March 31, 2002.

## QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

### MARKET RISK

We are exposed to various market risks, including the changes in foreign currency exchange rates and interest rates. Market risk is the potential loss arising from changes in market rates and prices. Foreign exchange contracts used to hedge foreign currency exposures and short-term investments are subject to market risk. We do not consider our cash and cash equivalents to be subject to interest rate risk due to their short maturities. We do not enter into derivatives or other financial instruments for trading or speculative purposes.

#### Foreign Currency Exchange Rate Risk

We utilize foreign exchange contracts to hedge foreign currency exposures of underlying assets and liabilities, primarily certain intercompany receivables that are denominated in foreign currencies, thereby, limiting our risk. Gains and losses on foreign exchange contracts are reflected in the Consolidated Statement of Operations. At March 31, 2002, we had foreign exchange contracts, all with maturities of less than three months to purchase and sell approximately $226,330,000 in foreign currencies, primarily British Pounds, European Currency Units ("Euro"), Canadian Dollars and other currencies.

Fair value represents the difference in value of the contracts at the spot rate and the forward rate. The counterparties to these contracts are substantial and creditworthy multinational commercial banks. The risks of counterparty nonperformance associated with these contracts are not considered to be material. Notwithstanding our efforts to manage foreign exchange risks, there can be no assurances that our hedging activities will adequately protect us against the risks associated with foreign currency fluctuations.

The following table below provides information about our foreign currency forward exchange contracts at March 31, 2002. The information is provided in U.S. dollar equivalents and presents the notional amount (forward amount), the weighted average contractual foreign currency exchange rates and fair value.

| | CONTRACT AMOUNT (In thousands) | WEIGHTED-AVERAGE CONTRACT RATE | FAIR VALUE (In thousands) |
|---|---|---|---|
| Foreign currency to be sold under contract: | | | |
| British Pound | $ 131,622 | 1.4229 | $ (52) |
| Euro | 41,121 | 0.8749 | 179 |
| Canadian Dollar | 16,986 | 1.5895 | 67 |
| Japanese Yen | 6,431 | 132.64 | (5) |
| Swedish Krona | 5,427 | 10.3189 | 43 |
| Australian Dollar | 4,206 | 0.5258 | (58) |
| South African Rand | 3,125 | 12.4801 | (281) |
| Norwegian Krone | 2,262 | 8.8409 | 13 |
| Danish Krone | 2,001 | 8.4965 | 10 |
| Swiss Franc | 1,199 | 1.6680 | 10 |
| Total | $ 214,380 | | $ (74) |
| Foreign currency to be purchased under contract: | | | |
| British Pound | $ 11,950 | 1.4253 | $ (207) |
| Total | $ 11,950 | | $ (207) |
| Grand total | $ 226,330 | | $ (281) |

While the contract amounts provide one measurement of the volume of these transactions, they do not represent the amount of our exposure to credit risk. The amounts (arising from the possible inabilities of counterparties to meet the terms of their contracts) are generally limited to the amounts, if any, by which the counterparties' obligations exceed our obligations as these contracts can be settled on a net basis at our option. We control credit risk through credit approvals, limits and monitoring procedures.

### Interest Rate Risk

Our exposure to market rate risk for changes in interest rates relates primarily to our investment portfolio. We do not use derivative financial instruments in our investment portfolio. We manage our interest rate risk by maintaining an investment portfolio primarily consisting of debt instruments of high credit quality and relatively short average maturities. We also manage our interest rate risk by maintaining sufficient cash and cash equivalent balances such that we are typically able to hold our investments to maturity. At March 31, 2002, our cash equivalents, short-term and long-term investments included debt securities of $662,359,000. Notwithstanding our efforts to manage interest rate risks, there can be no assurances that we will be adequately protected against the risks associated with interest rate fluctuations.

The table below presents the amounts and related weighted average interest rates of our investment portfolio at March 31, 2002:

| (Dollars in thousands) | AVERAGE INTEREST RATE | COST | FAIR VALUE |
|---|---|---|---|
| Cash equivalents(1) | | | |
| Fixed rate | 3.75% | $ 10,141 | $ 10,141 |
| Variable rate | 2.06% | $ 408,108 | $ 408,108 |
| Short-term investments(1)(2) | | | |
| Fixed rate | 3.61% | $ 235,769 | $ 235,710 |
| Variable rate | 6.35% | $ 8,400 | $ 8,653 |

(1) See definition in Note 1 of the Notes to Consolidated Financial Statements.
(2) Maturity dates for short-term investments range from 3 months to 31 months with call dates ranging from 3 months to 10 months.

# INDEPENDENT AUDITORS' REPORT

THE BOARD OF DIRECTORS AND STOCKHOLDERS
ELECTRONIC ARTS INC. AND SUBSIDIARIES:

We have audited the accompanying consolidated balance sheets of Electronic Arts Inc. and subsidiaries as of March 31, 2002 and 2001, and the related consolidated statements of operations, stockholders' equity and comprehensive income, and cash flows for each of the years in the three-year period ended March 31, 2002. These consolidated financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these consolidated financial statements based on our audits.

We conducted our audits in accordance with auditing standards generally accepted in the United States of America. Those standards 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. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the financial position of Electronic Arts Inc. and subsidiaries as of March 31, 2002 and 2001, and the results of their operations and their cash flows for each of the years in the three-year period ended March 31, 2002, in conformity with accounting principles generally accepted in the United States of America.

KPMG LLP

KPMG LLP
Mountain View, California
May 3, 2002

ELECTRONIC ARTS AND SUBSIDIARIES

# CONSOLIDATED BALANCE SHEETS

| (In thousands, except share data) AS OF MARCH 31, | 2002 | 2001 |
|---|---|---|
| **Assets** | | |
| Current assets: | | |
| Cash, cash equivalents and short-term investments | $ 796,936 | $ 466,492 |
| Marketable securities | 6,869 | 10,022 |
| Receivables, less allowances of $115,870 and $89,833, respectively | 190,495 | 174,449 |
| Inventories, net | 23,780 | 15,686 |
| Other current assets | 134,463 | 152,078 |
| Total current assets | 1,152,543 | 818,727 |
| Property and equipment, net | 308,827 | 337,199 |
| Long-term investments | — | 8,400 |
| Investment in affiliates | 19,077 | 19,052 |
| Goodwill and other intangibles, net | 110,512 | 136,764 |
| Other assets | 108,415 | 58,776 |
| | $ 1,699,374 | $ 1,378,918 |
| **Liabilities, Minority Interest and Stockholders' Equity** | | |
| Current liabilities: | | |
| Accounts payable | $ 88,563 | $ 73,061 |
| Accrued and other liabilities | 364,419 | 266,965 |
| Total current liabilities | 452,982 | 340,026 |
| Minority interest in consolidated joint venture | 3,098 | 4,545 |
| Stockholders' equity: | | |
| Preferred stock, $0.01 par value. Authorized 10,000,000 shares | — | — |
| Common stock | | |
| Class A common stock, $0.01 par value. Authorized 400,000,000 shares; issued and outstanding 138,429,269 and 134,714,464 shares, respectively | 1,384 | 1,347 |
| Class B common stock, $0.01 par value. Authorized 100,000,000 shares; issued and outstanding 6,233,413 and 6,250,000 shares, respectively | 62 | 63 |
| Paid-in capital | 649,777 | 540,354 |
| Retained earnings | 606,795 | 505,286 |
| Accumulated other comprehensive loss | (14,724) | (12,703) |
| Total stockholders' equity | 1,243,294 | 1,034,347 |
| | $ 1,699,374 | $ 1,378,918 |

See accompanying Notes to Consolidated Financial Statements.

ELECTRONIC ARTS AND SUBSIDIARIES

# CONSOLIDATED STATEMENTS OF OPERATIONS

| (In thousands, except per share data) YEARS ENDED MARCH 31, | 2002 | 2001 | 2000 |
|---|---|---|---|
| Net revenues | $ 1,724,675 | $ 1,322,273 | $ 1,420,011 |
| Cost of goods sold | 807,611 | 652,242 | 704,702 |
| Gross profit | 917,064 | 670,031 | 715,309 |
| Operating expenses: | | | |
| Marketing and sales | 241,109 | 185,336 | 188,611 |
| General and administrative | 107,059 | 104,041 | 92,418 |
| Research and development | 387,736 | 388,928 | 261,966 |
| Amortization of intangibles | 25,418 | 19,323 | 11,989 |
| Charge for acquired in-process technology | — | 2,719 | 6,539 |
| Restructuring and asset impairment charges | 20,303 | — | — |
| Total operating expenses | 781,625 | 700,347 | 561,523 |
| Operating income (loss) | 135,439 | (30,316) | 153,786 |
| Interest and other income, net | 12,848 | 16,886 | 16,028 |
| Income (loss) before provision for (benefit from) income taxes and minority interest | 148,287 | (13,430) | 169,814 |
| Provision for (benefit from) income taxes | 45,969 | (4,163) | 52,642 |
| Income (loss) before minority interest | 102,318 | (9,267) | 117,172 |
| Minority interest in consolidated joint venture | (809) | (1,815) | (421) |
| Net income (loss) | $ 101,509 | $ (11,082) | $ 116,751 |
| Net income per share: | | | |
| Basic | N/A | N/A | $ 0.93 |
| Diluted | N/A | N/A | $ 0.88 |
| Number of shares used in computation: | | | |
| Basic | N/A | N/A | 125,660 |
| Diluted | N/A | N/A | 132,742 |
| Class A common stock: | | | |
| Net income (loss): | | | |
| Basic | $ 124,256 | $ 11,944 | N/A |
| Diluted | $ 101,509 | $ (11,082) | N/A |
| Net income (loss) per share: | | | |
| Basic | $ 0.91 | $ 0.09 | N/A |
| Diluted | $ 0.71 | $ (0.08) | N/A |
| Number of shares used in computation: | | | |
| Basic | 136,832 | 131,404 | N/A |
| Diluted | 143,142 | 132,056 | N/A |
| Class B common stock: | | | |
| Net loss, net of retained interest in EA.com | $ (22,747) | $ (23,026) | N/A |
| Net loss per share: | | | |
| Basic | $ (3.77) | $ (3.83) | N/A |
| Diluted | $ (3.77) | $ (3.83) | N/A |
| Number of shares used in computation: | | | |
| Basic | 6,026 | 6,015 | N/A |
| Diluted | 6,026 | 6,015 | N/A |

See accompanying Notes to Consolidated Financial Statements, including segment information in Note 18.

# CONSOLIDATED STATEMENTS OF STOCKHOLDERS' EQUITY

| (In thousands) YEARS ENDED MARCH 31, 2002, 2001 AND 2000 | CLASS A COMMON STOCK | | CLASS B COMMON STOCK | | PAID-IN | RETAINED | ACCUMULATED OTHER COMPRE- | TREASURY STOCK | | |
|---|---|---|---|---|---|---|---|---|---|---|
| | SHARES | AMOUNT | SHARES | AMOUNT | CAPITAL | EARNINGS | HENSIVE LOSS | SHARES | AMOUNT | TOTAL |
| Balances at March 31, 1999 | 122,584 | $1,226 | — | $ — | $267,086 | $402,112 | $(2,567) | (246) | $(4,926) | $662,931 |
| Net income | | | | | | 116,751 | | | | 116,751 |
| Change in unrealized appreciation of investments, net | | | | | | | 1,739 | | | 1,739 |
| Reclassification adjustment for gains realized in net income, net | | | | | | | (5,194) | | | (5,194) |
| Translation adjustment | | | | | | | (339) | | | (339) |
| Comprehensive income | | | | | | | | | | 112,957 |
| Proceeds from sales of shares through stock plans | 6,285 | 62 | | | 83,096 | (2,495) | | 246 | 4,926 | 85,589 |
| Issuance of Class B common stock | | | 6,000 | 60 | 27,993 | | | | | 28,053 |
| Issuance of Class B stock warrant | | | | | 1,300 | | | | | 1,300 |
| Tax benefit related to stock options | | | | | 32,563 | | | | | 32,563 |
| Balances at March 31, 2000 | 128,869 | 1,288 | 6,000 | 60 | 412,038 | 516,368 | (6,361) | — | — | 923,393 |
| Net loss | | | | | | (11,082) | | | | (11,082) |
| Change in unrealized appreciation of investments, net | | | | | | | 3,097 | | | 3,097 |
| Translation adjustment | | | | | | | (9,439) | | | (9,439) |
| Comprehensive loss | | | | | | | | | | (17,424) |
| Proceeds from sales of shares through stock plans | 5,845 | 59 | | | 101,937 | | | | | 101,996 |
| Issuance of Class B common stock | | | 250 | 3 | 2,247 | | | | | 2,250 |
| Notes receivable in connection with issuance of Class B stock | | | | | (1,618) | | | | | (1,618) |
| Tax benefit related to stock options | | | | | 25,750 | | | | | 25,750 |
| Balances at March 31, 2001 | 134,714 | 1,347 | 6,250 | 63 | 540,354 | 505,286 | (12,703) | — | — | 1,034,347 |

| (In thousands) YEARS ENDED MARCH 31, 2002, 2001 AND 2000 | CLASS A COMMON STOCK SHARES | CLASS A COMMON STOCK AMOUNT | CLASS B COMMON STOCK SHARES | CLASS B COMMON STOCK AMOUNT | PAID-IN CAPITAL | RETAINED EARNINGS | ACCUMULATED OTHER COMPREHENSIVE LOSS | TREASURY STOCK SHARES | TREASURY STOCK AMOUNT | TOTAL |
|---|---|---|---|---|---|---|---|---|---|---|
| Balances at March 31, 2001 | 134,714 | 1,347 | 6,250 | 63 | 540,354 | 505,286 | (12,703) | — | — | 1,034,347 |
| Net income | | | | | | 101,509 | | | | 101,509 |
| Change in unrealized depreciation of investments, net | | | | | | | (3,540) | | | (3,540) |
| Reclassification adjustment for losses realized in net income, net | | | | | | | 66 | | | 66 |
| Translation adjustment | | | | | | | 1,453 | | | 1,453 |
| Comprehensive income | | | | | | | | | | 99,488 |
| Proceeds from sales of shares through stock plans | 3,995 | 40 | — | — | 98,701 | | | | | 98,741 |
| Sale of stock under stock purchase agreement | | | 8 | — | 100 | | | | | 100 |
| Purchase of treasury stock | | | | | | | | (280) | (11,922) | (11,922) |
| Retirement of treasury stock | (280) | (3) | | | (11,919) | | | 280 | 11,922 | — |
| Other | | | (25) | (1) | | | | | | (1) |
| Tax benefit related to stock options | | | | | 22,541 | | | | | 22,541 |
| Balances at March 31, 2002 | 138,429 | $1,384 | 6,233 | $62 | $649,777 | $606,795 | $(14,724) | — | $ — | $1,243,294 |

See accompanying Notes to Consolidated Financial Statements.

ELECTRONIC ARTS AND SUBSIDIARIES

# CONSOLIDATED STATEMENTS OF CASH FLOWS

| (In thousands) YEARS ENDED MARCH 31, | 2002 | 2001 | 2000 |
|---|---|---|---|
| **Operating Activities** | | | |
| Net income (loss) | $ 101,509 | $ (11,082) | $ 116,751 |
| Adjustments to reconcile net income (loss) to net cash provided by operating activities: | | | |
| Minority interest in consolidated joint venture | 809 | 1,815 | 421 |
| Equity in net income of affiliates | (2,999) | (820) | (1,138) |
| Gain on sale of affiliate | (200) | (214) | (842) |
| Depreciation and amortization | 110,901 | 78,601 | 46,725 |
| Non-cash restructuring and asset impairment charges | 13,399 | — | — |
| Loss on sale of fixed assets | 331 | 1,992 | 31 |
| (Gain) loss on marketable securities | 96 | — | (7,528) |
| Bad debt expense | 9,361 | 7,541 | 6,714 |
| Charge for acquired in-process technology | — | 2,719 | 6,539 |
| Tax benefit from exercise of stock options | 22,541 | 25,750 | 32,563 |
| Change in assets and liabilities, net of acquisitions: | | | |
| Receivables | (25,407) | 53,775 | (77,779) |
| Inventories | (8,094) | 7,300 | (579) |
| Other assets | (1,718) | (4,238) | (69,727) |
| Accounts payable | 15,502 | (27,476) | 29,673 |
| Accrued and other liabilities | 90,996 | 91,356 | (6,919) |
| Deferred income taxes | (42,056) | (33,080) | 2,994 |
| Net cash provided by operating activities | 284,971 | 193,939 | 77,899 |
| **Investing Activities** | | | |
| Proceeds from sale of property and equipment | 299 | 4,134 | 444 |
| Proceeds from sales of marketable securities, net | — | — | 8,598 |
| Proceeds from sale of affiliate | 570 | — | 8,842 |
| Capital expenditures | (51,518) | (120,347) | (134,884) |
| Investment in affiliates, net | 2,919 | 1,662 | (4,099) |
| Purchase of marketable securities | — | (2,479) | — |
| Dividend to joint venture | (2,481) | — | — |
| Change in short-term investments, net | (190,342) | 46,907 | (13,860) |
| Acquisition of Pogo Corporation, net of cash acquired | — | (42,571) | — |
| Acquisition of Kesmai | — | — | (22,500) |
| Acquisition of other subsidiaries, net of cash acquired | — | — | (22,096) |
| Net cash used in investing activities | (240,553) | (112,694) | (179,555) |
| **Financing Activities** | | | |
| Proceeds from sales of Class A shares through employee stock plans and other plans | 98,741 | 101,996 | 85,589 |
| Proceeds from sales of Class B shares and stock warrants | 99 | 632 | 20,000 |
| Purchase of treasury shares | (11,922) | — | — |
| Net cash provided by financing activities | 86,918 | 102,628 | 105,589 |
| Translation adjustment | 1,678 | (10,326) | 124 |
| Increase in cash and cash equivalents | 133,014 | 173,547 | 4,057 |
| Beginning cash and cash equivalents | 419,812 | 246,265 | 242,208 |
| Ending cash and cash equivalents | 552,826 | 419,812 | 246,265 |
| Short-term investments | 244,110 | 46,680 | 93,539 |
| Ending cash, cash equivalents and short-term investments | $ 796,936 | $ 466,492 | $ 339,804 |
| Supplemental cash flow information: | | | |
| Cash paid during the year for income taxes | $ 9,955 | $ 13,556 | $ 15,525 |
| Non-cash investing activities: | | | |
| Class B common stock issued in connection with the Kesmai acquisition | $ — | $ — | $ 9,353 |
| Change in unrealized appreciation (depreciation) of investments and marketable securities | $ (5,035) | $ 4,488 | $ (5,008) |

See accompanying Notes to Consolidated Financial Statements.

# NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

March 31, 2002, 2001 and 2000

## (1) SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

A summary of the significant accounting policies applied in the preparation of the accompanying consolidated financial statements of Electronic Arts Inc. and its wholly-owned and majority-owned subsidiaries (the "Company") follows:

### (a) Consolidation

The accompanying consolidated financial statements include the accounts of the Company. All significant intercompany balances and transactions have been eliminated in consolidation.

### (b) Fiscal Year

The Company's fiscal year is reported on a 52/53-week period that ends on the Saturday nearest to March 31 in each year. The results of operations for fiscal 2002 contain 52 weeks. The results of operations for fiscal 2001 and 2000 contain 53 and 52 weeks, respectively. For clarity of presentation herein, all fiscal periods are treated as ending on a calendar month end.

### (c) Revenue Recognition

The Company's revenue recognition policies are in compliance with American Institute of Certified Public Accountants 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*", which provide guidance on generally accepted accounting principles for recognizing revenue on software transactions.

In December 1999, the Securities and Exchange Commission ("SEC") issued Staff Accounting Bulletin No. 101("SAB 101"), "*Revenue Recognition in Financial Statements*", which outlines the basic criteria that must be met to recognize revenue and provides guidance for presentation of revenue and for disclosure related to revenue recognition policies in financial statements filed with the SEC. The adoption of SAB 101 did not have a material impact on the Company's consolidated financial position and results of operations.

#### PRODUCT SALES:

The Company recognizes revenue upon shipment of its packaged goods products based on "FOB Shipping" terms. Under FOB Shipping terms, title and risk of loss are transferred when the products are delivered to the customer. In order to recognize revenue, the Company must not have any continuing obligations and it must also be probable that the Company will collect the accounts receivable. Subject to certain limitations, the Company permits customers to obtain exchanges within certain specified periods and provides price protection on certain unsold merchandise. Revenue is recognized net of an allowance for returns and price protection.

#### ONLINE SUBSCRIPTION REVENUES:

Online subscription revenues are derived principally from subscription revenues collected from customers for online play, who are only contractually obligated to pay on a month-to-month basis. Prepaid monthly subscription revenues, including revenues collected from credit card sales as well as sales of *Gametime* subscription cards, are deferred and subsequently recognized ratably over the period for which the hosting services are provided.

#### ADVERTISING REVENUES:

Advertising revenues are derived principally from the sale of banner and in-game advertisements. Banner and in-game advertising is typically generated from contracts in which either the Company or AOL provides a minimum number of impressions over the term of the agreed upon commitment. Revenue is recognized as the impressions are delivered, provided that no significant obligations remain and collection of the related receivable is probable. Advertising revenue generated on the AOL Games Channel is recorded net of the applicable revenue share owed to AOL under the AOL agreement (see Note 5 of the Notes to Consolidated Financial Statements).

#### SOFTWARE LICENSES:

For those agreements which provide the customers the right to multiple copies in exchange for guaranteed minimum royalty amounts, revenue is recognized at delivery of the product master or the first copy. Per copy royalties on sales that exceed the guarantee are recognized as earned.

Revenue from the licensing of software was $23,291,000, $18,944,000 and $21,704,000 for the fiscal years ended March 31, 2002, 2001 and 2000, respectively.

### (d) Sales Returns and Other Reserves

The Company estimates potential future product returns and price protection related to current period product revenue. The Company analyzes historical returns, current sell through of distributor and retailer inventory of the Company's products, current trends in the video game market and the overall economy, changes in customer demand and acceptance of the Company's products and other related factors when evaluating the adequacy of the sales returns and price protection allowances. In addition, the Company monitors and manages the volume of sales to retailers and distributors and their inventories as substantial overstocking in the distribution channel can result in high returns or the requirement for substantial price protection in subsequent periods.

Similarly, the Company must use significant judgment and make estimates in connection with establishing allowances for doubtful accounts in any accounting period. The Company analyzes customer concentrations, customer credit-worthiness and current economic trends when evaluating the adequacy of the allowance for doubtful accounts.

### (e) Cash and Investments

Cash equivalents consist of highly liquid investments with insignificant rate risk and with maturities of three months or less at the date of purchase. Short-term investments include securities with maturities greater than three months and less than one year, except for certain investments with stated maturities greater than one year. Long-term investments consist of securities with maturities greater than one year.

The Company accounts for investments under Statement of Financial Accounting Standards No. 115 ("SFAS 115"), "*Accounting for Certain Investments in Debt and Equity Securities*". The Company's policy is to protect the value of its investment portfolio and to minimize principal risk by earning returns based on current interest rates. Management determines the appropriate classification of its debt and equity securities at the time of purchase and reevaluates such designation as of each balance sheet date. Debt securities are classified as held-to-maturity when the Company has the positive intent and ability to hold the securities to maturity. Securities classified as held-to-maturity are carried at amortized cost, which is adjusted for amortization of premiums and accretion of discounts to maturity. Such amortization is included in interest income. Debt securities, not classified as held-to-maturity, are classified as available-for-sale and are stated at fair value. Securities sold are based on the specific identification method.

### (f) Prepaid Royalties

Prepaid royalties consist primarily of prepayments for manufacturing royalties, co-publishing and/or distribution affiliates and license fees paid to celebrities, professional sports organizations and other organizations for use of their trade name and content. Also included in prepaid royalties are prepayments made to independent software developers under development arrangements that have alternative future uses. Prepaid royalties are expensed at the contractual or effective royalty rate as cost of goods sold based on actual net product sales. Management evaluates the future realization of prepaid royalties quarterly and charges to research and development expense any amounts that management deems unlikely to be realized through product sales. Royalty advances are classified as current and non-current assets based upon estimated net product sales for the following year. The current portion of prepaid royalties, included in other current assets, was $65,484,000 and $46,264,000 at March 31, 2002 and 2001, respectively. The long-term portion of prepaid royalties, included in other assets, was $1,164,000 and $9,664,000 at March 31, 2002 and 2001, respectively.

### (g) Software Development Costs

Research and development costs, which consist primarily of software development costs, are expensed as incurred. Statement of Financial Accounting Standards No. 86 ("SFAS 86"), "*Accounting for the Cost of Computer Software to be Sold, Leased, or Otherwise Marketed*", provides for the capitalization of certain software development costs incurred after technological feasibility of the software is established or for development costs that have alternative future uses. Under the Company's current practice of developing new products, the technological feasibility of the underlying software is not established until substantially all product development is complete, which generally includes the development of a working model. The software development costs that have been capitalized to date have been insignificant.

### (h) Inventories

Inventories are stated at the lower of cost or market. Inventories at March 31, 2002 and 2001 consisted of:

| (In thousands) | 2002 | 2001 |
|---|---|---|
| Raw materials and work in process | $ 1,025 | $ 976 |
| Finished goods | 22,755 | 14,710 |
| | $ 23,780 | $ 15,686 |

### (i) Advertising Costs

The Company generally expenses advertising costs as incurred, except for production costs associated with media campaigns which are deferred and charged to expense at the first run of the ad. Cooperative advertising with distributors and retailers is accrued when revenue is recognized. Cooperative advertising credits are reimbursed when qualifying claims are submitted. The Company has adopted the provisions of Emerging Issues Task Force issue No. 01-09 ("EITF 01-09"), *"Accounting for Consideration Given by a Vendor to a Customer or a Reseller of the Vendor's Products"*. The adoption of EITF 01-09 did not have a material impact in the Company's consolidated financial position or results of operations. For the fiscal years ended March 31, 2002, 2001 and 2000, advertising expenses totaled approximately $105,712,000, $75,429,000 and $87,377,000, respectively.

### (j) Property and Equipment

Property and equipment are stated at cost. Depreciation is calculated using the accelerated and straight-line methods over the following useful lives:

| | |
|---|---|
| Buildings | 20 to 25 years |
| Computer equipment and software | 3 to 7 years |
| Furniture and equipment | 3 to 7 years |
| Leasehold improvements | Lesser of the lease terms or the estimated useful lives of the improvements |

Under the provisions of SOP 98-1, *"Accounting for the Costs of Computer Software Developed or Obtained for Internal Use"*, the Company capitalizes costs associated with customized internal-use software systems that have reached the application stage and meet recoverability tests. Such capitalized costs include external direct costs utilized in developing or obtaining the applications and payroll and payroll-related expenses for employees who are directly associated with the applications. Capitalization of such costs begins when the preliminary project stage is complete and ceases at the point in which the project is substantially complete and ready for its intended purpose. Capitalized costs associated with internal-use software amounted to $121,002,000 at March 31, 2002, and are being depreciated on a straight-line basis over each project's estimated useful life.

### (k) Intangible Assets

Intangible assets net of accumulated amortization at March 31, 2002 and 2001, of $110,512,000 and $136,764,000, respectively, include goodwill, costs of obtaining product technology and noncompete covenants which are amortized using the straight-line method over the lesser of their estimated useful lives or the agreement terms, typically from two to twelve years. Amortization expense for fiscal years ended March 31, 2002, 2001 and 2000 was $25,418,000, $19,323,000 and $11,989,000, respectively. The Company assesses the recoverability of goodwill by determining whether the carried value of the assets may be recovered through estimated future undiscounted net cash flows.

On April 1, 2002, the Company adopted Statement of Financial Accounting Standards No. 142 ("SFAS 142"), *"Goodwill and Other Intangible Assets"*, which supersedes Accounting Principles Board Opinion No. 17 *"Intangible Assets"*. As a result of adopting this standard, the Company will continue to amortize finite-lived intangibles, but will no longer amortize certain other intangible assets, most notably goodwill and acquired workforce, which had a net book value at March 31, 2002 of $69,050,000. Amortization of goodwill and acquired workforce totaled approximately $13,125,000 for fiscal 2002, approximately $9,182,000 for fiscal 2001 and approximately $6,411,000 for fiscal 2000. Based on intangible assets as of March 31, 2002, the Company estimates that amortization of finite-lived intangibles will total approximately $8,700,000 for fiscal 2003. Following adoption of SFAS 142, the Company will continue to evaluate whether any event has occurred which might indicate that the carrying value of an intangible asset is not recoverable. In addition, SFAS 142 requires that goodwill be subject to at least an annual assessment for impairment by applying a fair value-based test. The Company is in the process of completing an evaluation for impairment of goodwill in accordance with SFAS 142. The Company believes the implementation of SFAS 142 will not have a material impact on its consolidated financial statements.

### (l) Long-Lived Assets

The Company evaluates long-lived assets and certain identifiable intangibles for impairment whenever events or changes in circumstances indicate that the carrying amount of an asset may not be recoverable. Recoverability of assets is measured by a comparison of the carrying amount of an asset to future undiscounted net cash flows expected to be generated by the asset. This may include assumptions about future prospects for the business that the asset relates to and typically involves computations of the estimated future cash flows to be generated by these businesses. Based on these judgments and assumptions, the Company determines whether it needs to take an impairment charge to reduce the value of the asset stated on the balance sheet to reflect its actual fair value. Judgments and assumptions about future values and remaining useful lives are complex and often subjective. They can be affected by a variety of factors, including but not limited to, significant negative industry or economic trends, significant changes in the manner or the Company's use of the acquired assets or the strategy of the Company's overall business and significant underperformance relative to expected historical or projected future operating results. If such assets are considered to be impaired, the impairment to be recognized is measured by the amount by which the carrying amount of the asset exceeds its fair value.

In April 2002, the Company adopted Statement of Financial Accounting Standards No. 144 ("SFAS 144"), *"Accounting for the Impairment or Disposal of Long-Lived Assets"*, which addresses financial accounting and reporting for the impairment or disposal of long-lived assets. The Company is in the process of determining the impact of this new accounting standard. The Company believes the implementation of SFAS 144 will not have a material impact to its consolidated financial statements.

### (m) Income Taxes

The Company uses the asset and liability method of accounting for income taxes. Under the asset and liability method, the Company recognizes deferred tax assets and liabilities for the future tax consequences attributable to differences between the financial statement carrying amounts and the tax basis of existing assets and liabilities. Deferred tax assets and liabilities are based on temporary differences resulting from differing treatment of items for tax and accounting purposes. The Company records a valuation allowance to reduce tax assets to an amount whose realization is more likely than not. The valuation allowance is based on the Company's estimates of taxable income by jurisdiction in which the Company operates and the period over which the Company's deferred tax assets will be recoverable.

### (n) Foreign Currency Translation

For each of the Company's foreign subsidiaries the functional currency is its local currency. Assets and liabilities of foreign operations are translated into U.S. dollars using current exchange rates, and revenues and expenses are translated into U.S. dollars using average exchange rates. The effects of foreign currency translation adjustments are included as a component of accumulated other comprehensive income (loss) in stockholders' equity.

Foreign currency transaction gains and losses are a result of the effect of exchange rate changes on transactions denominated in currencies other than the functional currency. Included in interest and other income in the statements of operations are foreign currency transaction losses of $412,000, $888,000 and $1,781,000, for the fiscal years ended March 31, 2002, 2001 and 2000, respectively.

On April 1, 2001, the Company adopted Statement of Financial Accounting Standards No. 133 ("SFAS 133"), *"Accounting for Derivative Instruments and Hedging Activities"*. SFAS 133 establishes accounting and reporting standards for derivative instruments and hedging activities and requires us to recognize these as either assets or liabilities on the balance sheet and measure them at fair value. As described in Note 3 of the Notes to Consolidated Financial Statements, gains and losses resulting from changes in fair value are accounted for depending on the use of the derivative and whether it is designated and qualifies for hedge accounting. The adoption of this accounting standard did not have a material impact on the Company's consolidated financial position or results of operations.

### (o) Net Income (Loss) Per Share

The following summarizes the computations of Basic Earnings Per Share ("EPS") and Diluted EPS. Basic EPS is computed as net earnings divided by the weighted-average number of common shares outstanding for the period. Diluted EPS reflects the potential dilution that could occur from common shares issuable through stock-based compensation plans including stock options, restricted stock awards, warrants and other convertible securities using the treasury stock method.

Net income (loss) per share was calculated on a consolidated basis until Class A common stock and Class B common stock were created as a result of the approval of the Tracking Stock Proposal (see Note 2 of the Notes to Consolidated Financial Statements). Net income (loss) per share is computed individually for Class A common stock and Class B common stock. Please see the discussion regarding segment reporting in the Management's Discussion and Analysis of Financial Condition and Results of Operations.

| (In thousands, except for per share amounts):<br>**YEAR ENDED MARCH 31, 2002** | **CLASS A COMMON STOCK-BASIC** | **CLASS A COMMON STOCK-DILUTED** | **CLASS B COMMON STOCK** |
|---|---|---|---|
| Net income (loss) before retained interest in EA.com | $ 253,156 | $ 101,509 | $ (151,647) |
| Net loss related to retained interest in EA.com | (128,900) | — | 128,900 |
| Net income (loss) | $ 124,256 | $ 101,509 | $ (22,747) |
| Shares used to compute net income (loss) per share: | | | |
| Weighted-average common shares | 136,832 | 136,832 | 6,026 |
| Dilutive stock equivalents | — | 6,310 | — |
| Dilutive potential common shares | 136,832 | 143,142 | 6,026 |
| Net income (loss) per share: | | | |
| Basic | $ 0.91 | N/A | $ (3.77) |
| Diluted | N/A | $ 0.71 | $ (3.77) |

| (In thousands, except for per share amounts):<br>**YEAR ENDED MARCH 31, 2001** | **CLASS A COMMON STOCK-BASIC** | **CLASS A COMMON STOCK-DILUTED** | **CLASS B COMMON STOCK** |
|---|---|---|---|
| Net income (loss) before retained interest in EA.com | $ 142,422 | $ (11,082) | $ (153,504) |
| Net loss related to retained interest in EA.com | (130,478) | — | 130,478 |
| Net income (loss) | $ 11,944 | $ (11,082) | $ (23,026) |
| Shares used to compute net income (loss) per share: | | | |
| Weighted-average common shares | 131,404 | 131,404 | 6,015 |
| Dilutive stock equivalents | — | 652 | — |
| Dilutive potential common shares | 131,404 | 132,056 | 6,015 |
| Net income (loss) per share: | | | |
| Basic | $ 0.09 | N/A | $ (3.83) |
| Diluted | N/A | $ (0.08) | $ (3.83) |

| (In thousands, except for per share amounts):<br>**YEAR ENDED MARCH 31, 2000** | |
|---|---|
| Net income | $ 116,751 |
| Shares used to compute net income per share: | |
| Weighted-average common shares | 125,660 |
| Dilutive stock equivalents | 7,082 |
| Dilutive potential common shares | 132,742 |
| Net income per share: | |
| Basic | $ 0.93 |
| Diluted | $ 0.88 |

The Diluted EPS calculation for Class A common stock, presented above, includes the potential dilution from the conversion of Class B common stock to Class A common stock in the event that the initial public offering for Class B common stock does not occur. Net income used for the calculation of Diluted EPS for Class A common stock is $101,509,000 for the fiscal year ended March 31, 2002. This net income includes the remaining 15% interest in EA.com, which is directly attributable to outstanding Class B shares owned by third parties, which would be included in the Class A common stock EPS calculation in the event that the initial public offering for Class B common stock does not occur.

Due to the net loss attributable for the twelve months ended March 31, 2001 on a diluted basis to Class A Stockholders, stock options have been excluded from the Diluted EPS calculation. Had net income been reported for this period, an additional 5,971,000 shares would have been added to diluted potential common shares for Class A common stock for the twelve months ended March 31, 2001.

Due to the net loss attributable for the twelve months ended March 31, 2002 and 2001 on a diluted basis to Class B Stockholders, stock options have been excluded from the Diluted EPS calculation. Had net income been reported for these periods, an additional 842,000 and 472,000 shares, respectively, would have been added to diluted potential common shares for Class B common stock for the twelve months ended March 31, 2002 and 2001.

Excluded from the above computation of weighted-average shares for Class A diluted EPS for the fiscal years ended March 31, 2002, 2001 and 2000 were options to purchase 1,515,000, 2,705,000 and 229,000 shares of common stock, respectively, as the options' exercise price was greater than the average market price of the common shares. Class B common stock, authorized on March 22, 2000, was excluded from the Company's calculations of basic and diluted EPS for the fiscal year ended March 31, 2000 because its impact on the calculations was immaterial.

### (p) Employee Benefits

The Company has a 401(k) Plan covering substantially all of its U.S. employees. The 401(k) Plan permits the Company to make discretionary contributions to employees' accounts based on the Company's financial performance. The Company contributed $4,811,000, $1,127,000 and $1,799,000 to the Plan in fiscal 2002, fiscal 2001 and fiscal 2000, respectively.

### (q) Stock-based Compensation

The Company accounts for stock-based awards to employees using the intrinsic value method in accordance with Accounting Principles Board Opinion No. 25 ("APB 25"), *"Accounting for Stock Issued to Employees"* and Financial Accounting Standards Board issued Interpretation No. 44 ("FIN 44"), *"Accounting for Certain Transactions Involving Stock Compensation (an interpretation of APB Opinion No. 25)"*. The Company has adopted the disclosure-only provisions of Statement of Financial Accounting Standards No. 123 ("SFAS 123"), *"Accounting for Stock-Based Compensation"*.

### (r) Use of Estimates

The preparation of financial statements in conformity with accounting principles generally accepted in the United States 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 date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Such estimates include provisions for doubtful accounts, sales returns and allowances, long-lived assets, deferred income taxes, warranty provisions, and estimates regarding the recoverability of prepaid royalty advances and inventories. Actual results could differ from those estimates.

### (s) Reclassifications

Certain amounts have been reclassified to conform to fiscal 2002 presentation.

## (2) TRACKING STOCK

On March 22, 2000, the stockholders of Electronic Arts authorized the issuance of a new series of common stock, designated as Class B common stock ("Tracking Stock"). The Tracking Stock is intended to reflect the performance of Electronic Arts' online and e-Commerce division, EA.com. As a result of the approval of the Tracking Stock Proposal, Electronic Arts' existing common stock has been re-classified as Class A common stock ("Class A Stock") and that stock reflects the performance of Electronic Arts' other businesses, EA Core.

## (3) FINANCIAL INSTRUMENTS

### (a) Cash and Investments

| (In thousands)<br>**AS OF MARCH 31,** | **2002** | **2001** |
|---|---|---|
| Cash and cash equivalents: | | |
| Cash | $ 134,577 | $ 70,196 |
| Money market funds | 380,632 | 250,182 |
| Municipal securities | 27,189 | 91,879 |
| Commercial paper | 10,428 | 7,555 |
| Cash and cash equivalents | 552,826 | 419,812 |
| Short-term investments: | | |
| Available-for-sale | | |
| U.S. Agency bonds | 222,985 | — |
| Corporate bonds | 8,236 | 4,076 |
| Municipal securities | 4,489 | 42,604 |
| Held-to-maturity | | |
| U.S. Treasury securities | 8,400 | — |
| Short-term investments | 244,110 | 46,680 |
| Cash, cash equivalents and short-term investments | $ 796,936 | $ 466,492 |
| Long-term investments: | | |
| U.S. Treasury securities | $ — | $ 8,400 |

Long-term and short-term held-to-maturity investments include commercial notes with original maturities of five to eight years secured by U.S. Treasury Notes which enable the Company to take advantage of certain tax incentives from its Puerto Rico operation. These investments are treated as held-to-maturity for financial reporting purposes.

The fair value of held-to-maturity securities at March 31, 2002 was $8,653,000 which included gross unrealized gains of $253,000. The fair value of held-to-maturity securities at March 31, 2001 was $8,601,000 which included gross unrealized gains of $201,000.

### (b) Marketable Securities

Marketable securities are comprised of equity securities. The Company has accounted for investments in equity securities as "available-for-sale" and has stated applicable investments at fair value, with net unrealized appreciation (depreciation) reported as a separate component of accumulated other comprehensive loss in stockholders' equity. Marketable securities had an aggregate cost of $6,954,000 and $7,066,000 at March 31, 2002 and 2001, respectively. At March 31, 2002, marketable securities included gross unrealized losses of $85,000. At March 31, 2001, marketable securities included gross unrealized gains of $2,956,000. There were no sales of marketable securities in fiscal years 2002 and 2001.

### (c) Foreign Currency Forward Exchange Contracts

The Company utilizes foreign exchange contracts to hedge foreign currency exposures of underlying assets and liabilities, primarily certain intercompany receivables that are denominated in foreign currencies, thereby limiting its risk. The Company does not use forward exchange contracts for speculative or trading purposes. The Company's accounting policies for these instruments are based on the Company's designation of such instruments as hedging transactions. The criteria the Company uses for designating an instrument as a hedge include the instrument's effectiveness in risk reduction and one-to-one matching of forward exchange contracts to underlying transactions. Gains and losses on currency forward contracts that are designated and effective as hedges of existing transactions are recognized in income in the same period as losses and gains on the underlying transactions are recognized and generally offset.

Net Loss Recognized in Other Income Relating to Fair Value Hedging of the Balance Sheet:

| (In thousands)<br>**YEAR ENDED MARCH 31,** | **2002** | **2001** |
|---|---|---|
| Gain (loss) on foreign currency assets and liabilities | $ 991 | $ (26,104) |
| Gain (loss) on hedges of foreign currency assets and liabilities | (1,403) | 25,216 |
| Net loss recognized in other income | $ (412) | $ (888) |

The Company transacts business in various foreign currencies. At March 31, 2002, the Company had foreign exchange contracts, all with maturities of less than three months, to purchase and sell approximately $226,330,000 in foreign currencies, primarily in British Pounds, European Currency Units ("Euros"), Canadian Dollars, and other currencies.

Fair value represents the difference in value of the contracts at the spot rate and the forward rate, plus the unamortized premium or discount. At March 31, 2002, fair value of these contracts is not significant. The counterparties to these contracts are substantial and creditworthy multinational commercial banks. The risks of counterparty nonperformance associated with these contracts are not considered to be material. Notwithstanding the Company's efforts to manage foreign exchange risk, there can be no assurances that it's hedging activities will adequately protect against the risks associated with foreign currency fluctuations.

## (4) LEASE COMMITMENTS

The Company leases certain of its current facilities and certain equipment under non-cancelable capital and operating lease agreements. The Company is required to pay property taxes, insurance and normal maintenance costs for certain of its facilities and will be required to pay any increases over the base year of these expenses on the remainder of the Company's facilities.

In February of 1995, the Company entered into a build-to-suit lease with a financial institution on its headquarter's facility in Redwood City, California, which was extended in July of 2001 and runs through July of 2006. The Company accounted for this arrangement as an operating lease in accordance with Statement of Financial Accounting Standards No. 13 ("SFAS 13"), "*Accounting for Leases*", as amended. Existing campus facilities developed in phase one comprise a total of 350,000 square feet and provide space for sales, marketing, administration and research and development functions. The Company has an option to purchase the property (land and facilities) for $145,000,000 or, at the end of the lease, to arrange for (1) an additional extension of the lease or (2) sale of the property to a third party with the Company retaining an obligation to the owner for the difference between the sale price and the guaranteed residual value of up to $128,900,000 if the sales price is less than this amount, subject to certain provisions of the lease.

In December 2000, the Company entered into a second build-to-suit lease with a financial institution for a five year term from December 2000 to expand its headquarter's facilities and develop adjacent property adding approximately 310,000 square feet to its campus. The Company expects to complete construction in June of 2002. The Company accounted for this arrangement as an operating lease in accordance with SFAS 13, as amended. The facilities will provide space for marketing, sales and research and development. The Company has an option to purchase the property for $127,000,000 or, at the end of the lease, to arrange for (1) an extension of the lease or (2) sale of the property to a third party with the Company retaining an obligation to the owner for the difference between the sale price and the guaranteed residual value of up to $118,800,000 if the sales price is less than this amount, subject to certain provisions of the lease.

Lease rates are based upon the Commercial Paper Rate. The two lease agreements described above require the Company to maintain certain financial covenants, all of which the Company was in compliance with as of March 31, 2002.

Total future minimum lease commitments as of March 31, 2002 are:

| (In thousands) | YEAR ENDED MARCH 31, | |
|---|---|---|
| | 2003 | $ 18,288 |
| | 2004 | 15,011 |
| | 2005 | 11,354 |
| | 2006 | 10,810 |
| | 2007 | 9,122 |
| | Thereafter | 11,609 |
| | | $ 76,194 |

Total rent expense for all operating leases was $25,177,000, $27,526,000 and $23,591,000, for the fiscal years ended March 31, 2002, 2001 and 2000, respectively.

## (5) AMERICA ONLINE, INC. ("AOL") AGREEMENT

In November 1999, Electronic Arts Inc., EA.com and AOL entered into a five-year agreement which establishes the basis for EA.com's production of a games site on the world wide web that will be available to AOL subscribers and to users of other branded AOL properties.

The Company is required to pay to AOL $81,000,000 over the life of the five-year agreement. Of this amount, $36,000,000 was paid upon signing the agreement with the remainder due in four equal installments on the first four anniversaries of the initial payment. The Company paid AOL $11,250,000 in both fiscal 2002 and 2001. The fair value of the payments made under the AOL agreement was determined by an independent valuation and the resulting amounts are being amortized using the straight-line method (beginning with the site launch) over the remaining term of the five-year agreement. Advances of $38,597,000 and $41,462,000 are included in other long-term assets as of March 31, 2002 and 2001, respectively.

The Company made a commitment to spend $15,000,000 in offline media advertisements promoting their online games, including those on the AOL service, prior to March 31, 2005. As of March 31, 2002, the Company has spent approximately $3,500,000 against this commitment.

### Sale of Class B Common Stock and Warrant to AOL

In connection with the agreement with AOL, the Company sold shares of Class B common stock to AOL (the "AOL Shares") representing 10 percent of the initial equity value attributable to EA.com valued at $18,700,000.

In addition to the AOL Shares, the Company sold AOL a warrant (the "AOL Warrant") to purchase shares of Class B common stock representing an additional 5 percent of the initial equity value attributable to EA.com for $1,300,000. The aggregate exercise price of the AOL Warrant will be $40,000,000. The AOL Warrant expires at the latest at the fifth anniversary of its date of issuance, and under certain conditions may expire at an earlier date.

### AOL Exchange Rights

AOL may exchange their Class B common stock shares for a number of Class A common stock based on the ratio of per share price paid by AOL for the Class B stock relative to $41.89. As of March 31, 2002, none of the AOL shares have been exchanged for Class A common stock.

## (6) CONCENTRATION OF CREDIT RISK

The Company extends credit to various companies in the retail and mass merchandising industry. Collection of trade receivables may be affected by changes in economic or other industry conditions and may, accordingly, impact the Company's overall credit risk. Although the Company generally does not require collateral, the Company performs ongoing credit evaluations of its customers and reserves for potential credit losses are maintained. For the fiscal year ended March 31, 2002, the Company had receivable balances from one customer which represented 13% of total gross accounts receivables. For the fiscal years ended March 31, 2001 and 2000, there were no customers with receivable balances greater than 10% of total gross accounts receivables.

Short-term investments are placed with high credit-quality financial institutions or in short-duration high quality securities. The Company limits the amount of credit exposure in any one institution or type of investment instrument.

## (7) LITIGATION

The Company is subject to pending claims and litigation. Management, after review and consultation with counsel, considers that any liability from the disposition of such lawsuits would not have a material adverse effect upon the consolidated financial condition or results of operations of the Company.

## (8) PREFERRED STOCK

At March 31, 2002 and 2001, the Company had 10,000,000 shares of Preferred Stock authorized but unissued. The rights, preferences, and restrictions of the Preferred Stock may be designated by the Board of Directors without further action by the Company's stockholders.

## (9) TREASURY STOCK

In September 2001, the Board of Directors approved a plan to purchase up to two million shares of the Company's Class A common stock. For the fiscal year ended March 31, 2002, the Company repurchased 280,000 shares for approximately $11,922,000 under the program. In February 2002, all of the 280,000 shares were retired.

## (10) STOCK PLANS

### (a) Employee Stock Purchase Plan

The Company has an Employee Stock Purchase Plan program whereby eligible employees may authorize payroll deductions of up to 10% of their compensation to purchase shares at 85% of the lower of the fair market value of the Class A Common Stock on the date of commencement of the offering or on the last day of the six-month purchase period. The program commenced in September 1991. A new Employee Stock Purchase Plan program was approved by the Board of Directors in May 2000 and commenced in August 2000. In fiscal 2002, 313,240 shares were purchased by the Company and distributed to employees at prices ranging from $42.45 to $45.05. In fiscal 2001, 350,164 shares were purchased by the Company and distributed to employees at prices ranging from $29.14 to $42.50. In fiscal 2000, 491,046 shares were purchased by the Company and distributed to employees at prices ranging from $16.21 to $29.14. The weighted average fair value of the fiscal 2002, fiscal 2001 and fiscal 2000 awards was $18.88, $18.31 and $10.00, respectively. At March 31, 2002, the Company had 1,009,673 shares of Class A Common Stock reserved for future issuance under the Plans.

## (b) Stock Option Plans

The Company's 2000 Class A Equity Incentive Plan, 1995 Stock Option Plan, and Directors' Plan ("Option Plans") provide options for employees, officers and directors to purchase the Company's Class A common stock. Pursuant to these Option Plans, the Board of Directors may grant non-qualified and incentive stock options to employees and officers and non-qualified options to directors, at not less than the fair market value on the date of grant.

At the Company's Annual Meeting of Stockholders, held on August 1, 2001, the stockholders elected to amend the 2000 Class A Equity Incentive Plan to increase by 6,000,000 the number of shares of the Company's Class A common stock reserved for issuance under the Plan.

Under the Company's stock option plans, 246,000 shares were reissued from treasury stock in fiscal 2000. No shares were distributed from reissued treasury stock in fiscal 2002 or 2001.

Together with the Tracking Stock Proposal, the stockholders approved the Electronic Arts Inc. 2000 Class B Equity Incentive Plan. The Class B equity plan allows the award of stock options or restricted stock for up to an aggregate of 6,000,000 shares of Class B common stock. The Class B plan includes a provision for automatic option grants to the Company's outside directors. As of March 31, 2002 there were 225,000 restricted shares issued under the Class B equity plan.

The options generally expire ten years from the date of grant and are generally exercisable in monthly increments over 50 months. Class B common stock grants will generally vest over 50 months with 2% vesting per month.

In the fiscal year 2001, the Board of Directors approved the Key Partner Class B Equity Incentive Program which allows for the issuance of warrants to key business partners to purchase up to 750,000 shares of Class B common stock. As of March 31, 2002, there were 121,000 warrants outstanding under this program. These warrants expire not later than five years from issuance.

The Company has adopted the disclosure-only provisions of SFAS 123, "*Accounting for Stock Based Compensation*". Accordingly, no compensation expense has been recognized for options granted under the Company's employee-based stock option plans. Had compensation expense been determined based on the fair value at the grant dates for awards under those plans in accordance with the provisions of SFAS 123, the Company's pro forma net income (loss) and net income (loss) per share for fiscal 2002, 2001 and 2000 would have been:

| (In thousands, except per share data) | 2002 | 2001 | 2000 |
|---|---|---|---|
| **CONSOLIDATED** | | | |
| Net income (loss): | | | |
| As reported | $ 101,509 | $ (11,082) | $ 116,751 |
| Pro forma | $ 27,913 | $ (69,350) | $ 78,380 |
| Earnings per share: | | | |
| As reported – basic | N/A | N/A | $ 0.93 |
| Pro forma – basic | N/A | N/A | $ 0.62 |
| As reported – diluted | N/A | N/A | $ 0.88 |
| Pro forma – diluted | N/A | N/A | $ 0.60 |
| **CLASS A COMMON STOCK** | | | |
| Net income (loss): | | | |
| As reported – basic | $ 124,256 | $ 11,944 | N/A |
| Pro forma – basic | $ 51,505 | $ (45,493) | N/A |
| As reported – diluted | $ 101,509 | $ (11,082) | N/A |
| Pro forma – diluted | $ 27,913 | $ (69,350) | N/A |
| Earnings (loss) per share: | | | |
| As reported – basic | $ 0.91 | $ 0.09 | N/A |
| Pro forma – basic | $ 0.38 | $ (0.35) | N/A |
| As reported – diluted | $ 0.71 | $ (0.08) | N/A |
| Pro forma – diluted | $ 0.20 | $ (0.53) | N/A |

The fair value of each option grant is estimated on the date of grant using the Black-Scholes option-pricing model. The following weighted-average assumptions are used for grants made in 2002, 2001 and 2000 under the stock plans: risk-free interest rates of 2.22% to 4.51% in 2002; 4.59% to 6.55% in 2001; and 4.93% to 6.54% in 2000; expected volatility of 72% in fiscal 2002, 74% in fiscal 2001 and 65% in fiscal 2000; expected lives of 2.25 years in fiscal 2002, 2.32 years in fiscal 2001 and 2.29 years in fiscal 2000 under the Option Plans and one year for the Employee Stock Purchase Plan. No dividends are assumed in the expected term. The Company's calculations are based on a multiple option valuation approach and forfeitures are recognized when they occur.

| (In thousands, except per share data) | 2002 | 2001 | 2000 |
|---|---|---|---|
| **CLASS B COMMON STOCK** | | | |
| Net loss: | | | |
| As reported | $ (22,747) | $ (23,026) | N/A |
| Pro forma | $ (23,592) | $ (23,857) | N/A |
| Loss per share: | | | |
| As reported – basic | $ (3.77) | $ (3.83) | N/A |
| Pro forma – basic | $ (3.92) | $ (3.97) | N/A |
| As reported – diluted | $ (3.77) | $ (3.83) | N/A |
| Pro forma – diluted | $ (3.92) | $ (3.97) | N/A |

The fair value of each Class B option grant is estimated on the date of grant using the Black-Scholes option-pricing model. The assumptions used were the same as those for Class A.

Additional information regarding options outstanding for Class A as of March 31, 2002 is as follows:

| | OPTIONS OUTSTANDING | | | OPTIONS EXERCISABLE | |
|---|---|---|---|---|---|
| RANGE OF EXERCISE PRICES | NUMBER OF SHARES | WEIGHTED-AVERAGE REMAINING CONTRACTUAL LIFE | WEIGHTED-AVERAGE EXERCISE PRICE | NUMBER OF SHARES | WEIGHTED-AVERAGE EXERCISE PRICE |
| $ 0.995 – $14.938 | 2,467,771 | 3.72 | $ 11.88 | 2,460,911 | $ 11.88 |
| 15.000 – 18.563 | 2,320,347 | 5.05 | 17.34 | 1,444,878 | 17.00 |
| 19.000 – 23.563 | 2,582,951 | 6.41 | 21.81 | 1,960,239 | 21.82 |
| 23.625 – 28.500 | 503,344 | 6.97 | 26.25 | 328,980 | 26.17 |
| 28.969 – 29.875 | 2,848,273 | 7.40 | 29.82 | 1,490,328 | 29.82 |
| 30.844 – 44.500 | 2,586,540 | 8.32 | 39.55 | 854,492 | 38.48 |
| 44.688 – 46.540 | 2,796,244 | 9.33 | 46.47 | 377,795 | 46.33 |
| 46.938 – 49.500 | 3,153,199 | 8.51 | 49.30 | 1,009,540 | 49.32 |
| 49.688 – 57.040 | 2,888,196 | 9.17 | 54.94 | 215,854 | 53.91 |
| 57.170 – 63.130 | 670,795 | 9.39 | 59.35 | 81,056 | 59.23 |
| $ 0.995 – $63.130 | 22,817,660 | 7.42 | $ 35.51 | 10,224,073 | $ 26.04 |

Additional information regarding options outstanding for Class B as of March 31, 2002 is as follows:

| | OPTIONS OUTSTANDING | | | OPTIONS EXERCISABLE | |
|---|---|---|---|---|---|
| RANGE OF EXERCISE PRICES | NUMBER OF SHARES | WEIGHTED-AVERAGE REMAINING CONTRACTUAL LIFE | WEIGHTED-AVERAGE EXERCISE PRICE | NUMBER OF SHARES | WEIGHTED-AVERAGE EXERCISE PRICE |
| $ 9.000 | 2,611,719 | 8.00 | $ 9.00 | 1,553,510 | $ 9.00 |
| 10.000 | 65,275 | 8.34 | 10.00 | 27,952 | 10.00 |
| 12.000 | 1,484,171 | 8.96 | 12.00 | 425,937 | 12.00 |
| $ 9.000 – $12.000 | 4,161,165 | 8.35 | $ 10.09 | 2,007,399 | $ 9.65 |

The following summarizes the activity under the Company's Class A stock option plans during the fiscal years ended March 31, 2002, 2001 and 2000:

| | OPTIONS OUTSTANDING | |
|---|---|---|
| | SHARES | WEIGHTED-AVERAGE EXERCISE PRICE |
| Balance at March 31, 1999 | 22,878,518 | $ 15.33 |
| Granted | 7,815,952 | 31.92 |
| Canceled | (1,721,172) | 21.68 |
| Exercised | (6,039,390) | 12.42 |
| Balance at March 31, 2000 (8,907,324 shares were exercisable at a weighted average price of $14.93) | 22,933,908 | 21.30 |
| Granted | 5,851,961 | 46.05 |
| Canceled | (1,746,449) | 15.71 |
| Exercised | (5,495,281) | 31.15 |
| Balance at March 31, 2001 (8,902,789 shares were exercisable at a weighted average price of $20.55) | 21,544,139 | 28.66 |
| Granted | 6,313,776 | 51.29 |
| Canceled | (1,358,690) | 36.14 |
| Exercised | (3,681,565) | 22.27 |
| Balance at March 31, 2002 | 22,817,660 | $ 35.51 |
| Options available for grant at March 31, 2002 | 3,510,216 | |

The following summarizes the activity under the Company's Class B stock option plan during the fiscal years ended March 31, 2002 and 2001:

| | OPTIONS OUTSTANDING | |
|---|---|---|
| | SHARES | WEIGHTED-AVERAGE EXERCISE PRICE |
| Balance at March 31, 2000 | — | $ — |
| Granted | 5,785,792 | 9.62 |
| Canceled | (429,310) | 9.28 |
| Exercised | (250,000) | 9.00 |
| Balance at March 31, 2001 (21,990 shares were exercisable at a weighted average price of $9.57) | 5,106,482 | 9.68 |
| Granted | 977,983 | 12.00 |
| Canceled | (1,923,220) | 9.99 |
| Exercised | (80) | 9.00 |
| Balance at March 31, 2002 | 4,161,165 | $10.09 |
| Options available for grant at March 31, 2002 | 2,363,755 | |

## (11) PROPERTY AND EQUIPMENT

Property and equipment at March 31, 2002 and 2001 consisted of:

| (In thousands) | 2002 | 2001 |
|---|---|---|
| Computer equipment and software | $ 319,893 | $ 310,147 |
| Buildings | 97,939 | 94,784 |
| Land | 44,911 | 44,721 |
| Office equipment, furniture and fixtures | 31,915 | 32,569 |
| Leasehold improvements | 15,463 | 13,483 |
| Warehouse equipment and other | 5,396 | 4,319 |
| | 515,517 | 500,023 |
| Less accumulated depreciation and amortization | (206,690) | (162,824) |
| | $ 308,827 | $ 337,199 |

Depreciation and amortization expenses associated with property and equipment amounted to $67,619,000, $50,345,000 and $34,736,000 for the fiscal years ended March 31, 2002, 2001 and 2000, respectively.

## (12) ACCRUED AND OTHER LIABILITIES

Accrued and other liabilities at March 31, 2002 and 2001 consisted of:

| (In thousands) | 2002 | 2001 |
|---|---|---|
| Accrued income taxes | $ 94,444 | $ 42,371 |
| Accrued compensation and benefits | 87,985 | 75,603 |
| Accrued expenses | 87,104 | 73,997 |
| Accrued royalties | 77,590 | 55,997 |
| Deferred revenue | 13,286 | 16,967 |
| Warranty reserve | 4,010 | 2,030 |
| | $ 364,419 | $ 266,965 |

## (13) BUSINESS COMBINATIONS

### (a) Pogo Corporation

On February 28, 2001, EA.com acquired Pogo Corporation (now referred to as "Pogo") for $43,333,000, including an initial investment of $42,000,000 and the redemption of Pogo preferred stock of $1,333,000. Pogo operates an ad-supported games service that reaches a broad consumer market. Pogo's internet-based family games focus on easy-to-play card, board and puzzle games.

The acquisition has been accounted for under the purchase method. The results of operations of Pogo and the estimated fair market values of the acquired assets and liabilities have been included in the consolidated financial statements from the date of acquisition. The adjusted allocation of the excess purchase price over the net tangible assets acquired was $40,516,000, of which, based on management's estimates prepared in conjunction with a third party valuation consultant, $2,719,000 was allocated to purchased in-process research and development and $37,797,000 was allocated to other intangible assets. Amounts allocated to other intangibles include goodwill of $16,927,000, existing technology of $12,505,000, and other intangibles of $8,365,000. The allocation of intangible assets is being amortized on a straight-line basis over lives ranging from three to seven years.

Purchased in-process research and development includes the value of products in the development stage that are not considered to have reached technological feasibility or to have alternative future use. Accordingly, this non-recurring item was expensed in the Consolidated Statement of Operations upon consummation of the acquisition. The non-recurring charge for in-process research and development increased diluted loss per share by approximately $0.01 and $0.07 in the fiscal year 2001 for Class A and Class B, respectively.

Pogo had various projects in progress at the time of the acquisition. As of the acquisition date, costs to complete Pogo projects acquired were expected to be approximately $1,200,000 in future periods. During fiscal 2002, all of these development projects were completed and launched on Pogo gamesites. In conjunction with the acquisition of Pogo, the Company accrued approximately $100,000 related to direct transaction costs and other related costs.

The purchase price for the Pogo transaction was allocated to assets acquired and liabilities assumed as set forth below (in thousands):

| | |
|---|---|
| Current assets | $ 3,048 |
| Fixed assets | 4,998 |
| Other long-term assets | 1,969 |
| In-process technology | 2,719 |
| Goodwill and other intangibles | 37,797 |
| Liabilities | (7,198) |
| Total cash paid | $ 43,333 |

The following table reflects unaudited pro forma combined results of operations of the Company and Pogo on the basis that the acquisition had taken place on April 1, 1999 (in thousands, except per share data):

| | AS REPORTED | PRO FORMA |
|---|---|---|
| **FISCAL YEAR ENDED MARCH 31, 2001** | | |
| Net revenues | $ 1,322,273 | $ 1,336,654 |
| Class A common stock: | | |
| Net income (loss): | | |
| Basic | $ 11,944 | $ 475 |
| Diluted | $ (11,082) | $ (26,292) |
| Net income (loss) per share: | | |
| Basic | $ 0.09 | $ 0.00 |
| Diluted | $ (0.08) | $ (0.20) |
| Number of shares used in computation: | | |
| Basic | 131,404 | 131,404 |
| Diluted | 132,056 | 132,056 |
| Class B common stock: | | |
| Net loss, net of retained interest in EA.com | $ (23,026) | $ (26,767) |
| Net loss per share: | | |
| Basic | $ (3.83) | $ (4.45) |
| Diluted | $ (3.83) | $ (4.45) |
| Number of shares used in computation: | | |
| Basic | 6,015 | 6,015 |
| Diluted | 6,015 | 6,015 |
| **FISCAL YEAR ENDED MARCH 31, 2000** | | |
| Net revenues | $ 1,420,011 | $ 1,422,340 |
| Net income | $ 116,751 | $ 107,285 |
| Net income per share: | | |
| Basic | $ 0.93 | $ 0.85 |
| Diluted | $ 0.88 | $ 0.81 |
| Number of shares used in computation: | | |
| Basic | 125,660 | 125,660 |
| Diluted | 132,742 | 132,742 |

In management's opinion, the unaudited pro forma combined results of operations are not indicative of the actual results that would have occurred had the acquisition been consummated at the beginning of fiscal 2000 or of future operations of the combined companies under the ownership and management of the Company.

### (b) Kesmai

On February 7, 2000, the Company acquired Kesmai Corporation (now referred to as "Kesmai") from News America Corporation ("News Corp") in exchange for $22,500,000 in cash and approximately 206,000 shares of its existing common stock valued at $8,650,000. The Company granted 5 percent of the initial equity attributable to EA.com to News Corp, adjusting the total common stock consideration relating to the acquisition by $703,000 to $9,353,000. The Company has contributed Kesmai to EA.com.

The Company also agreed to spend $12,500,000 through the period ended June 1, 2002 in advertising with News Corp or any of its affiliates. In addition, if certain conditions are met, including that a qualified public offering of Class B common stock does not occur within twenty-four months of News Corp's purchase of such shares and all of the Class B outstanding shares have been converted to Class A common stock, then (1) News Corp has the right to (i) exchange Class B common stock for approximately 206,000 shares of Class A common stock, and (ii) receive cash from Electronic Arts in the amount of $9,650,000, and (2) the Company will agree to spend an additional $11,675,000 in advertising with News Corp and its affiliates.

The acquisition has been accounted for under the purchase method. The results of operations of Kesmai and the estimated fair market values of the acquired assets and liabilities have been included in the consolidated financial statements from the date of acquisition. The adjusted allocation of the excess purchase price over the net tangible liabilities assumed was $32,815,000, of which, based on management's estimates prepared in conjunction with a third party valuation consultant, $3,869,000 was allocated to purchased in-process research and development and $28,946,000 was allocated to other intangible assets. Amounts allocated to other intangibles include goodwill of $18,932,000, existing technology of $3,992,000, amounts attributed to a prior AOL agreement of $3,131,000 and other intangibles of $2,891,000. The allocation of intangible assets is being amortized over lives ranging from two to seven years.

As part of the restructuring plan announced in fiscal 2002 for EA.com, the Company evaluated its intangibles for impairment in accordance with Statement of Financial Accounting Standards No. 121 ("SFAS 121"), "*Accounting for the Impairment of Long-Lived Assets and for Long-Lived Assets to Be Disposed Of*". The Company assessed the recoverability of its intangibles by determining whether the carrying amount of the assets was recoverable through estimated future undiscounted net cash flows. The Company calculated the impairment loss as the amount that the carrying value of the asset exceeded the discounted future cash flows. The Company recorded in restructuring and asset impairment charges a write-off of $1,014,000 related to certain other intangibles associated with Kesmai. These intangibles had remaining lives ranging from 15 to 39 months.

Purchased in-process research and development includes the value of products in the development stage that are not considered to have reached technological feasibility or to have alternative future use. Accordingly, this non-recurring item was expensed in the Consolidated Statement of Operations upon consummation of the acquisition. The non-recurring charge for in-process research and development reduced diluted earnings per share by $0.02 in the fiscal year 2000.

Kesmai had various projects in progress at the time of the acquisition. As of the acquisition date, costs to complete Kesmai projects acquired were approximately $10,550,000 in future periods. During fiscal 2002 and fiscal 2001, all of these development projects were completed and launched on the EA.com gamesites. The resources were redirected to ongoing live game operations or to building the EA.com publishing platform. As a result, the Company does not anticipate incurring significant future development costs in relation to these projects after fiscal 2002. In conjunction with the acquisition of Kesmai, the Company accrued approximately $200,000 related to direct transaction costs and other related costs.

The purchase price for the Kesmai transaction was allocated to assets acquired and liabilities assumed as set forth below (in thousands):

| | |
|---|---|
| Current assets | $ 605 |
| Fixed assets (net of depreciation) | 759 |
| In-process technology | 3,869 |
| Goodwill and other intangibles | 28,946 |
| Liabilities | (2,326) |
| Total cash and stock paid | $ 31,853 |

The following table reflects unaudited pro forma combined results of operations of the Company and Kesmai on the basis that the acquisition had taken place on April 1, 1999 (in thousands, except per share data):

| YEAR ENDED MARCH 31, 2000 | |
|---|---|
| Net revenues | $ 1,421,313 |
| Net income | $ 113,996 |
| Net income per share – basic | $ 0.91 |
| Net income per share – diluted | $ 0.86 |
| Number of shares used in computation – basic | 125,660 |
| Number of shares used in computation – diluted | 132,742 |

In management's opinion, the unaudited pro forma combined results of operations are not indicative of the actual results that would have occurred had the acquisition been consummated at the beginning of fiscal 2000 or of future operations of the combined companies under the ownership and management of the Company.

### (c) Square Co., Ltd.

In May 1998, the Company and Square Co., Ltd. ("Square"), a leading developer and publisher of entertainment software in Japan, completed the formation of two new joint ventures in North America and Japan. In North America, the companies formed Square Electronic Arts, LLC ("Square EA"), which has exclusive publishing rights in North America for future interactive entertainment titles created by Square. Additionally, the Company has the exclusive right to distribute in North America products published by this joint venture. Either party may terminate the existence of Square EA and the distribution agreement effective March 31, 2003. The Company contributed $3,000,000 and owns a 30% minority interest in this joint venture while Square owns 70%. This joint venture is accounted for under the equity method.

In Japan, the companies established Electronic Arts Square KK ("EA Square KK"), which will localize and publish in Japan the Company's properties originally created in North America and Europe, as well as develop and publish original video games in Japan. The Company contributed cash and has a 70% majority ownership interest, while Square contributed cash and owns 30%. Accordingly, the assets, liabilities and results of operations for EA Square KK are included in the Company's Consolidated Balance Sheets and Results of Operations since June 1, 1998, the date of formation. Square's 30% interest in EA Square KK has been reflected as "Minority interest in consolidated joint venture" on the Company's consolidated financial statements.

### (d) Other Business Combinations

Additionally, during the fiscal year ended March 31, 2000, the Company acquired two software development companies. In connection with these acquisitions, the Company incurred a charge of $2,670,000 for acquired in-process technology. The charge was made after the Company concluded that the in-process technology had not reached technological feasibility and had no alternative future use after taking into consideration the potential for usage of the software in different products and resale of the software.

## (14) INCOME TAXES

The Company's pretax income (loss) from operations for the fiscal years ended March 31, 2002, 2001 and 2000 consisted of the following components:

| (In thousands) | 2002 | 2001 | 2000 |
|---|---|---|---|
| Domestic | $ 17,020 | $ (27,166) | $ 104,096 |
| Foreign | 131,267 | 13,736 | 65,718 |
| Total pretax income (loss) | $ 148,287 | $ (13,430) | $ 169,814 |

Income tax expense (benefit) for the fiscal years ended March 31, 2002, 2001 and 2000 consisted of:

| (In thousands) | CURRENT | DEFERRED | TOTAL |
|---|---|---|---|
| 2002: | | | |
| Federal | $ 60,728 | $ (44,277) | $ 16,451 |
| State | 1,048 | (672) | 376 |
| Foreign | 4,306 | 2,295 | 6,601 |
| Charge in lieu of taxes from employee stock plans for Class A | 22,541 | — | 22,541 |
| | $ 88,623 | $ (42,654) | $ 45,969 |
| 2001: | | | |
| Federal | $ (4,233) | $ (19,975) | $ (24,208) |
| State | 582 | (13,809) | (13,227) |
| Foreign | 6,981 | 541 | 7,522 |
| Charge in lieu of taxes from employee stock plans for Class A | 25,750 | — | 25,750 |
| | $ 29,080 | $ (33,243) | $ (4,163) |
| 2000: | | | |
| Federal | $ 2,766 | $ 3,231 | $ 5,997 |
| State | 299 | 859 | 1,158 |
| Foreign | 15,573 | (2,649) | 12,924 |
| Charge in lieu of taxes from employee stock plans | 32,563 | — | 32,563 |
| | $ 51,201 | $ 1,441 | $ 52,642 |

The components of the net deferred tax assets as of March 31, 2002 and 2001 consist of:

| (In thousands) | 2002 | 2001 |
|---|---|---|
| Deferred tax assets: | | |
| Accruals, reserves and other expenses | $ 53,891 | $ 76,603 |
| Net operating loss carryforwards | 50,174 | 6,662 |
| Tax credits | 46,118 | 27,066 |
| Total | 150,183 | 110,331 |
| Deferred tax liabilities: | | |
| Undistributed earnings of DISC | (913) | (1,189) |
| Prepaid royalty expenses | (11,342) | (44,678) |
| Fixed assets | (35,266) | (4,456) |
| Total | (47,521) | (50,323) |
| Net deferred tax asset | $ 102,662 | $ 60,008 |

At March 31, 2002, deferred tax assets of $38,597,000 and $64,065,000 were included in other current assets and other assets, respectively.

At March 31, 2002, the Company had Federal net operating loss carryforwards of approximately $127,000,000 for income tax reporting purposes, which expire in 2021 and 2022. The Company also had state net operating loss carryforwards of approximately $177,000,000 for income tax reporting purposes, which expire beginning in 2006.

The Company also has research and experimental tax credits aggregating approximately $25,000,000 and $10,000,000 for federal and California purposes, respectively. The federal credit carryforwards expire from 2006 to 2022. The California credits carry over indefinitely until utilized. The Company also has foreign tax credit carryforwards of approximately $10,500,000, which expire from 2003 to 2007.

The differences between the statutory income tax rate and the Company's effective tax rate, expressed as a percentage of income (loss) before provision for (benefit from) income taxes, for the years ended March 31, 2002, 2001 and 2000 were as follows:

| | 2002 | 2001 | 2000 |
|---|---|---|---|
| Statutory Federal tax rate | 35.0% | (35.0%) | 35.0% |
| State taxes, net of Federal benefit | 1.5% | (10.0%) | 1.5% |
| Differences between statutory rate and foreign effective tax rate | (3.0%) | 20.2% | (2.8%) |
| Research and development credits | (3.4%) | (4.7%) | (1.7%) |
| Other | 0.9% | (1.5%) | (1.0%) |
| | 31.0% | (31.0%) | 31.0% |

The Company provides for U.S. taxes on an insignificant portion of the undistributed earnings of its foreign subsidiaries and does not provide taxes on the remainder. The Company has not provided for Federal income tax on approximately $259,000,000 of undistributed earnings of its foreign subsidiaries, since the Company intends to reinvest this amount in foreign subsidiary operations indefinitely.

At March 31, 2002, the Company believes it is more likely than not that the results of future operations will generate sufficient taxable income to realize the net deferred tax assets.

The Company's U.S. income tax returns for the years 1992 through 1995 have been examined by the Internal Revenue Service (IRS). In 1998, the Company received a notice of deficiencies from the IRS. These deficiencies relate primarily to operations in Puerto Rico, which the Company is contesting in Tax Court. The Company substantially prevailed with respect to the principal issues at the Tax Court level. The time for the IRS to appeal has not yet expired. The Company believes that additional liabilities, if any, that arise from the outcome of this examination will not be material to the Company's consolidated financial statements.

## (15) INTEREST AND OTHER INCOME, NET

Interest and other income, net for the years ended March 31, 2002, 2001 and 2000 consisted of:

| (In thousands) | 2002 | 2001 | 2000 |
|---|---|---|---|
| Interest income | $ 16,691 | $ 17,903 | $ 13,744 |
| Gain (loss) on disposition of assets, net | (131) | (1,778) | 8,339 |
| Foreign currency losses | (412) | (888) | (1,781) |
| Foreign currency cost of hedging | (3,032) | — | — |
| Equity in net gain of affiliates | 2,999 | 820 | 1,138 |
| Other income (expense), net | (3,267) | 829 | (5,412) |
| | $ 12,848 | $ 16,886 | $ 16,028 |

## (16) COMPREHENSIVE INCOME

Statement of Financial Accounting Standards No. 130 ("SFAS 130") requires classification of other comprehensive income in a financial statement and display of other comprehensive income separately from retained earnings and additional paid-in capital. Other comprehensive income includes primarily foreign currency translation adjustments and unrealized gains (losses) on investments.

The change in the components of comprehensive income, net of tax, is summarized as follows (in thousands):

| | FOREIGN CURRENCY TRANSLATION ADJUSTMENTS | UNREALIZED GAINS (LOSSES) ON INVESTMENTS | ACCUMULATED OTHER COMPREHENSIVE LOSS |
|---|---|---|---|
| Balance at March 31, 1999 | $ (5,841) | $ 3,274 | $ (2,567) |
| Other comprehensive loss | (339) | (3,455) | (3,794) |
| Balance at March 31, 2000 | (6,180) | (181) | (6,361) |
| Other comprehensive income (loss) | (9,439) | 3,097 | (6,342) |
| Balance at March 31, 2001 | (15,619) | 2,916 | (12,703) |
| Other comprehensive income (loss) | 1,453 | (3,474) | (2,021) |
| Balance at March 31, 2002 | $(14,166) | $ (558) | $ (14,724) |

Change in unrealized gains (losses) on investments, net are shown net of taxes of $(1,561,000), $1,391,000 and $(1,553,000) in fiscal 2002, 2001 and 2000, respectively.

The currency translation adjustments are not adjusted for income taxes as they relate to indefinite investments in non-U.S. subsidiaries.

## (17) DISCLOSURES ABOUT FAIR VALUE OF FINANCIAL INSTRUMENTS

The following methods and assumptions were used to estimate the fair value of each class of financial instruments for which it is practicable to estimate that value:

***Cash, cash equivalents, short-term investments, receivables, accounts payable and accrued liabilities*** – the carrying amount approximates fair value because of the short maturity of these instruments.

***Long-term investments, investments classified as held-to-maturity and marketable securities*** – fair value is based on quoted market prices.

## (18) SEGMENT INFORMATION

Statement of Financial Accounting Standards No. 131 ("SFAS 131"), "*Disclosures About Segments of an Enterprise and Related Information*", establishes standards for the reporting by public business enterprises of information about product lines, geographic areas and major customers. The method for determining what information to report is based on the way that management organizes the operating segments within the Company for making operational decisions and assessments of financial performance.

The Company's chief operating decision maker is considered to be the Company's Chief Executive Officer ("CEO"). The CEO reviews financial information presented on a consolidated basis accompanied by disaggregated information about revenues by geographic region and by product lines for purposes of making operating decisions and assessing financial performance.

The Company operates in two principal business segments globally:

- EA Core business segment: creation, marketing and distribution of entertainment software.
- EA.com business segment: creation, marketing and distribution of entertainment software which can be played or sold online, ongoing management of subscriptions of online games and website advertising.

Please see the discussion regarding segment reporting in the MD&A.

Information about Electronic Arts business segments is presented below for the fiscal years ended March 31, 2002, 2001 and 2000 (in thousands):

| YEAR ENDED MARCH 31, 2002 | EA CORE (EXCLUDING EA.COM) | EA.COM | ADJUSTMENTS AND ELIMINATIONS | ELECTRONIC ARTS |
|---|---|---|---|---|
| Net revenues from unaffiliated customers | $ 1,647,502 | $ 77,173 | $ — | $ 1,724,675 |
| Group sales | 4,016 | — | (4,016)[a] | — |
| Total net revenues | 1,651,518 | 77,173 | (4,016) | 1,724,675 |
| Cost of goods sold from unaffiliated customers | 794,738 | 12,873 | — | 807,611 |
| Group cost of goods sold | — | 4,016 | (4,016)[a] | — |
| Total cost of goods sold | 794,738 | 16,889 | (4,016) | 807,611 |
| Gross profit | 856,780 | 60,284 | — | 917,064 |
| Operating expenses: | | | | |
| Marketing and sales | 202,749 | 20,496 | 17,864[c] | 241,109 |
| General and administrative | 96,919 | 10,140 | — | 107,059 |
| Research and development | 257,762 | 59,892 | 70,082[b] | 387,736 |
| Network development and support | — | 59,483 | (59,483)[b] | — |
| Customer relationship management | — | 10,599 | (10,599)[b] | — |
| Carriage fee | — | 17,864 | (17,864)[c] | — |
| Amortization of intangibles | 12,888 | 12,530 | — | 25,418 |
| Restructuring and asset impairment charges | — | 20,303 | — | 20,303 |
| Total operating expenses | 570,318 | 211,307 | — | 781,625 |
| Operating income (loss) | 286,462 | (151,023) | — | 135,439 |
| Interest and other income (expense), net | 13,472 | (624) | — | 12,848 |
| Income (loss) before provision for income taxes and minority interest | 299,934 | (151,647) | — | 148,287 |
| Provision for income taxes | 45,969 | — | — | 45,969 |
| Income (loss) before minority interest | 253,965 | (151,647) | — | 102,318 |
| Minority interest in consolidated joint venture | (809) | — | — | (809) |
| Net income (loss) before retained interest in EA.com | $ 253,156 | $ (151,647) | $ — | $ 101,509 |
| Interest income | $ 16,641 | $ 50 | $ — | $ 16,691 |
| Depreciation and amortization | 51,673 | 59,228 | — | 110,901 |
| Identifiable assets | 1,529,422 | 169,952 | — | 1,699,374 |
| Capital expenditures | 38,406 | 13,112 | — | 51,518 |

| YEAR ENDED MARCH 31, 2001 | EA CORE (EXCLUDING EA.COM) | EA.COM | ADJUSTMENTS AND ELIMINATIONS | ELECTRONIC ARTS |
|---|---|---|---|---|
| Net revenues from | | | | |
| unaffiliated customers | $ 1,280,172 | $ 42,101 | $ — | $1,322,273 |
| Group sales | 2,658 | — | (2,658)[a] | — |
| Total net revenues | 1,282,830 | 42,101 | (2,658) | 1,322,273 |
| Cost of goods sold from | | | | |
| unaffiliated customers | 640,239 | 12,003 | — | 652,242 |
| Group cost of goods sold | — | 2,658 | (2,658)[a] | — |
| Total cost of goods sold | 640,239 | 14,661 | (2,658) | 652,242 |
| Gross profit | 642,591 | 27,440 | — | 670,031 |
| Operating expenses: | | | | |
| Marketing and sales | 163,928 | 12,475 | 8,933[c] | 185,336 |
| General and administrative | 93,885 | 10,156 | — | 104,041 |
| Research and development | 248,534 | 77,243 | 63,151[b] | 388,928 |
| Network development and support | — | 51,794 | (51,794)[b] | — |
| Customer relationship management | — | 11,357 | (11,357)[b] | — |
| Carriage fee | — | 8,933 | (8,933)[c] | — |
| Amortization of intangibles | 12,829 | 6,494 | — | 19,323 |
| Charge for acquired | | | | |
| in-process technology | — | 2,719 | — | 2,719 |
| Total operating expenses | 519,176 | 181,171 | — | 700,347 |
| Operating income (loss) | 123,415 | (153,731) | — | (30,316) |
| Interest and other income, net | 16,659 | 227 | — | 16,886 |
| Income (loss) before benefit | | | | |
| from income taxes and | | | | |
| minority interest | 140,074 | (153,504) | — | (13,430) |
| Benefit from income taxes | (4,163) | — | — | (4,163) |
| Income (loss) before minority interest | 144,237 | (153,504) | — | (9,267) |
| Minority interest in | | | | |
| consolidated joint venture | (1,815) | — | — | (1,815) |
| Net income (loss) before retained | | | | |
| interest in EA.com | $ 142,422 | $ (153,504) | $ — | $ (11,082) |
| Interest income | $ 17,809 | $ 94 | $ — | $ 17,903 |
| Depreciation and amortization | 45,382 | 33,219 | — | 78,601 |
| Identifiable assets | 1,167,846 | 211,072 | — | 1,378,918 |
| Capital expenditures | 51,460 | 68,887 | — | 120,347 |

| YEAR ENDED MARCH 31, 2000 | EA CORE (EXCLUDING EA.COM) | EA.COM | ADJUSTMENTS AND ELIMINATIONS | ELECTRONIC ARTS |
|---|---|---|---|---|
| Net revenues from unaffiliated customers | $ 1,399,093 | $ 20,918 | $ — | $ 1,420,011 |
| Group sales | 2,014 | — | (2,014)[a] | — |
| Total net revenues | 1,401,107 | 20,918 | (2,014) | 1,420,011 |
| Cost of goods sold from unaffiliated customers | 700,024 | 4,678 | — | 704,702 |
| Group cost of goods sold | — | 2,014 | (2,014)[a] | — |
| Total cost of goods sold | 700,024 | 6,692 | (2,014) | 704,702 |
| Gross profit | 701,083 | 14,226 | — | 715,309 |
| Operating expenses: | | | | |
| Marketing and sales | 185,714 | 2,897 | — | 188,611 |
| General and administrative | 87,513 | 4,905 | — | 92,418 |
| Research and development | 205,933 | 34,716 | 21,317[b] | 261,966 |
| Network development and support | — | 17,993 | (17,993)[b] | — |
| Customer relationship management | — | 3,324 | (3,324)[b] | — |
| Amortization of intangibles | 10,866 | 1,123 | — | 11,989 |
| Charge for acquired in-process technology | 2,670 | 3,869 | — | 6,539 |
| Total operating expenses | 492,696 | 68,827 | — | 561,523 |
| Operating income (loss) | 208,387 | (54,601) | — | 153,786 |
| Interest and other income, net | 16,017 | 11 | — | 16,028 |
| Income (loss) before provision for income taxes and minority interest | 224,404 | (54,590) | — | 169,814 |
| Provision for income taxes | 52,642 | — | — | 52,642 |
| Income (loss) before minority interest | 171,762 | (54,590) | — | 117,172 |
| Minority interest in consolidated joint venture | (421) | — | — | (421) |
| Net income (loss) | $ 171,341 | $ (54,590) | $ — | $ 116,751 |
| Interest income | $ 13,733 | $ 11 | $ — | $ 13,744 |
| Depreciation and amortization | 39,818 | 6,907 | — | 46,725 |
| Identifiable assets | 1,085,411 | 106,901 | — | 1,192,312 |
| Capital expenditures | 97,279 | 37,605 | — | 134,884 |

(a) Represents elimination of intercompany sales of Electronic Arts packaged goods products to EA.com; and represents elimination of royalties paid to Electronic Arts by EA.com for intellectual property rights.
(b) Represents reclassification of Network Development and Support and Customer Relationship Management to Research and Development.
(c) Represents reclassification of amortization of the Carriage Fee to Marketing and Sales.

Information about Electronic Arts' operations in the North America and foreign areas for the fiscal years ended March 31, 2002, 2001 and 2000 is presented below:

| (In thousands) | NORTH AMERICA | EUROPE | ASIA PACIFIC (EXCLUDING JAPAN) | JAPAN | ELIMINATIONS | TOTAL |
|---|---|---|---|---|---|---|
| **Fiscal 2002** | | | | | | |
| Net revenues from unaffiliated customers | $ 1,093,244 | $ 519,458 | $ 53,376 | $ 58,597 | $ — | $ 1,724,675 |
| Intercompany revenues | 2,411 | 37,533 | 8,755 | 55 | (48,754) | — |
| Total net revenues | 1,095,655 | 556,991 | 62,131 | 58,652 | (48,754) | 1,724,675 |
| Operating income | 8,328 | 121,058 | 2,277 | 3,401 | 375 | 135,439 |
| Interest income | 14,440 | 2,010 | 241 | — | — | 16,691 |
| Depreciation and amortization | 95,395 | 13,768 | 1,091 | 647 | — | 110,901 |
| Capital expenditures | 39,259 | 10,350 | 1,038 | 871 | — | 51,518 |
| Identifiable assets | 1,325,939 | 333,825 | 21,435 | 18,175 | — | 1,699,374 |
| Long-lived assets | 348,120 | 158,500 | 4,469 | 4,428 | — | 515,517 |
| **Fiscal 2001** | | | | | | |
| Net revenues from unaffiliated customers | $ 831,924 | $ 386,728 | $ 51,039 | $ 52,582 | $ — | $ 1,322,273 |
| Intercompany revenues | 11,915 | 30,996 | 13,040 | 3,802 | (59,753) | — |
| Total net revenues | 843,839 | 417,724 | 64,079 | 56,384 | (59,753) | 1,322,273 |
| Operating income (loss) | (31,996) | (8,914) | 2,962 | 7,437 | 195 | (30,316) |
| Interest income | 14,230 | 3,271 | 402 | — | — | 17,903 |
| Depreciation and amortization | 71,501 | 6,510 | 275 | 315 | — | 78,601 |
| Capital expenditures | 103,048 | 15,535 | 1,104 | 660 | — | 120,347 |
| Identifiable assets | 1,034,625 | 300,196 | 20,364 | 23,733 | — | 1,378,918 |
| Long-lived assets | 334,398 | 154,832 | 3,807 | 3,806 | — | 496,843 |
| **Fiscal 2000** | | | | | | |
| Net revenues from unaffiliated customers | $ 846,637 | $ 486,816 | $ 53,187 | $ 33,371 | $ — | $ 1,420,011 |
| Intercompany revenues | 28,701 | 30,440 | 9,059 | — | (68,200) | — |
| Total net revenues | 875,338 | 517,256 | 62,246 | 33,371 | (68,200) | 1,420,011 |
| Operating income | 101,919 | 50,828 | 1,498 | 1,921 | (2,380) | 153,786 |
| Interest income | 11,775 | 1,755 | 214 | — | — | 13,744 |
| Depreciation and amortization | 35,114 | 9,968 | 473 | 1,170 | — | 46,725 |
| Capital expenditures | 78,298 | 54,379 | 1,447 | 760 | — | 134,884 |
| Identifiable assets | 734,626 | 418,034 | 18,019 | 21,633 | — | 1,192,312 |
| Long-lived assets | 244,845 | 154,475 | 3,306 | 3,975 | — | 406,601 |

Electronic Arts had sales to one customer which represented 14% of total net revenues in fiscal 2002 and 12% of total net revenues in fiscal 2001 and 2000.

Information about Electronic Arts' net revenues by product line for the fiscal years ended March 31, 2002, 2001 and 2000 is presented below (in thousands):

| | 2002 | 2001 | 2000 |
|---|---|---|---|
| PlayStation 2 | $ 482,882 | $ 258,988 | $ — |
| PC | 456,292 | 405,256 | 395,522 |
| Affiliated label | 269,010 | 222,278 | 275,333 |
| PlayStation | 189,535 | 309,988 | 586,821 |
| Xbox | 78,363 | — | — |
| Nintendo GameCube | 51,740 | — | — |
| Game Boy Advance | 43,653 | — | — |
| Game Boy Color | 38,026 | — | — |
| Advertising | 38,024 | 6,175 | — |
| Online Subscriptions | 30,940 | 28,878 | 16,771 |
| License, OEM and Other | 24,762 | 20,468 | 22,894 |
| N64 | 18,152 | 67,044 | 120,415 |
| Online Packaged Goods | 3,296 | 3,198 | 2,255 |
| | $ 1,724,675 | $ 1,322,273 | $ 1,420,011 |

## (19) RESTRUCTURING AND ASSET IMPAIRMENT CHARGES

In October 2001, the Company announced a restructuring plan for EA.com. The restructuring initiatives involved strategic decisions to discontinue certain product offerings and focus only on key online priorities that align with its fiscal 2003 operational objectives. The workforce reduction resulted in the termination of approximately 270 positions.

During fiscal 2002, the Company recorded restructuring charges of $20,303,000, consisting of $4,173,000 for workforce reductions, $3,312,000 for consolidation of facilities and other administrative charges, and $12,818,000 for the write-off of non-current assets and facilities. The estimated costs for workforce reduction included severance charges for terminated employees and costs for certain outplacement service contracts. The consolidation of facilities resulted in the closure of EA.com's San Diego studio and consolidation of its San Francisco and Virginia facilities. The estimated costs for consolidation of facilities included contractual rental commitments under real estate leases for unutilized office space offset by estimated future sub-lease income, costs to close or consolidate facilities, and costs to write off a portion of the assets from these facilities.

The Company recorded restructuring charges for EA.com in accordance with Emerging Issues Task Force No. 94-03, *"Liability Recognition for Certain Employee Termination Benefits and Other Costs to Exit an Activity (Including Certain Costs Incurred in a Restructuring)"*, Emerging Issues Task Force No. 95-03, *"Recognition of Liabilities in Connection with a Purchase Business Combination"*, and Staff Accounting Bulletin No. 100, *"Restructuring and Impairment Charges"*. Adjustments to the restructuring reserves will be made in future periods, if necessary, based upon current events and circumstances.

As part of the restructuring efforts, the Company assessed the remaining useful lives of goodwill, purchased intangible assets and other long-lived assets and tested the recoverability of its long-lived assets in accordance with SFAS 121. Management evaluated the impact of consolidating or abandoning certain EA.com technologies and processes and reviewed the effect of changes to EA.com's subscription product offerings in relation to EA.com's asset base. Based on computations of estimated future net cash flows attributable to these assets and product offerings, it was determined that there was a need to reduce the value of certain assets on our balance sheet to reflect their estimated fair value. Impairment charges on long-lived assets amounted to $12,818,000 and included $11,177,000 relating to consolidated or abandoned technologies for the EA.com infrastructure and $1,641,000 of goodwill and intangibles impairment charges relating to the EA.com's San Diego and Kesmai studios. There are no assurances that the impairment factors evaluated by management will not change in subsequent periods and accordingly, this could result in additional impairment charges in future periods.

The pre-tax restructuring charge of $20,303,000 consisted of $6,836,000 in cash outlays and $13,467,000 in non-cash charges related to the write-offs of non-current assets and facilities. As of March 31, 2002, an aggregate of $4,016,000 in cash had been paid out under the restructuring plan. Of the remaining cash outlay of $2,820,000, $1,590,000 is expected to occur in fiscal 2003 while the remaining $1,230,000 will occur in fiscal years 2004 and beyond.

The following table summarizes the activity in the accrued restructuring account in fiscal 2002 (in thousands):

| | WORKFORCE | FACILITIES | NON-CURRENT ASSETS | TOTAL |
|---|---|---|---|---|
| Charged to operations in fiscal 2002 | $ 4,173 | $ 3,312 | $ 12,818 | $ 20,303 |
| Charges utilized in cash in fiscal 2002 | (3,499) | (517) | — | (4,016) |
| Charges utilized in non-cash in fiscal 2002 | — | (581) | (12,818) | (13,399) |
| Accrual balance as of March 31, 2002 | $ 674 | $ 2,214 | $ — | $ 2,888 |

The restructuring accrual is included in accrued expenses in Note 12 of the Notes to Consolidated Financial Statements.

# QUARTERLY FINANCIAL AND MARKET INFORMATION (UNAUDITED)

| (In thousands, except per share data) | QUARTER ENDED JUNE 30 | SEPT. 30 | DEC. 31 | MARCH 31 | YEAR ENDED |
|---|---|---|---|---|---|
| **Fiscal 2002** | | | | | |
| CONSOLIDATED | | | | | |
| Net revenues | $ 181,950 | $ 240,156 | $ 832,878 | $ 469,691 | $ 1,724,675 |
| Operating income (loss) | (68,378) | (52,057) | 188,501 | 67,373 | 135,439 |
| Net income (loss) | (45,254)[a] | (32,824)[a] | 132,292[b] | 47,295[c] | 101,509 |
| CLASS A STOCKHOLDERS | | | | | |
| Net income (loss) per share - basic | $ (0.29) | $ (0.20) | $ 1.01 | $ 0.38 | $ 0.91 |
| Net income (loss) per share - diluted | $ (0.33) | $ (0.24) | $ 0.92 | $ 0.33 | $ 0.71 |
| Common stock price per share | | | | | |
| High | $ 63.04 | $ 60.60 | $ 66.01 | $ 62.95 | $ 66.01 |
| Low | $ 48.31 | $ 44.50 | $ 42.40 | $ 51.16 | $ 42.40 |
| CLASS B STOCKHOLDERS | | | | | |
| Net loss per share – basic | $ (0.98) | $ (0.93) | $ (1.11) | $ (0.76) | $ (3.77) |
| Net loss per share – diluted | $ (0.98) | $ (0.93) | $ (1.11) | $ (0.76) | $ (3.77) |
| Common stock price per share | | | | | |
| High | N/A | N/A | N/A | N/A | N/A |
| Low | N/A | N/A | N/A | N/A | N/A |
| **Fiscal 2001** | | | | | |
| CONSOLIDATED | | | | | |
| Net revenues | $ 154,799 | $ 219,900 | $ 640,319 | $ 307,255 | $ 1,322,273 |
| Operating income (loss) | (64,377) | (60,154) | 125,368 | (31,153) | (30,316) |
| Net income (loss) | (42,271)[d] | (38,909)[e] | 87,978[d] | (17,880)[f] | (11,082) |
| CLASS A STOCKHOLDERS | | | | | |
| Net income (loss) per share – basic | $ (0.30) | $ (0.27) | $ 0.72 | $ (0.07) | $ 0.09 |
| Net income (loss) per share – diluted | $ (0.33) | $ (0.30) | $ 0.63 | $ (0.13) | $ (0.08) |
| Common stock price per share | | | | | |
| High | $ 39.06 | $ 54.47 | $ 55.38 | $ 56.13 | $ 56.13 |
| Low | $ 26.59 | $ 37.06 | $ 35.19 | $ 29.84 | $ 26.59 |
| CLASS B STOCKHOLDERS | | | | | |
| Net loss per share – basic | $ (0.61) | $ (0.67) | $ (1.24) | $ (1.31) | $ (3.83) |
| Net loss per share – diluted | $ (0.61) | $ (0.67) | $ (1.24) | $ (1.31) | $ (3.83) |
| Common stock price per share | | | | | |
| High | N/A | N/A | N/A | N/A | N/A |
| Low | N/A | N/A | N/A | N/A | N/A |
| **Fiscal 2000** | | | | | |
| Net revenues | $ 186,120 | $ 338,887 | $ 600,691 | $ 294,313 | $ 1,420,011 |
| Operating income (loss) | (849) | 23,697 | 129,536 | 1,402 | 153,786 |
| Net income | 2,326[g] | 18,132[g] | 92,861[g] | 3,432[h] | 116,751 |
| Net income per share – basic | $ 0.02 | $ 0.15 | $ 0.73 | $ 0.03 | $ 0.93 |
| Net income per share – diluted | $ 0.02 | $ 0.14 | $ 0.69 | $ 0.03 | $ 0.88 |
| Common stock price per share | | | | | |
| High | $ 27.41 | $ 38.10 | $ 60.47 | $ 51.10 | $ 60.47 |
| Low | $ 22.82 | $ 26.44 | $ 33.22 | $ 34.50 | $ 22.82 |

(a) Net loss includes goodwill amortization of $4.5 million, net of taxes.
(b) Net income includes restructuring and asset impairment charges of $9.7 million, net of taxes, as well as goodwill amortization of $4.3 million, net of taxes.
(c) Net income includes restructuring and asset impairment charges of $4.3 million, net of taxes, as well as goodwill amortization of $4.2 million, net of taxes.
(d) Net income (loss) includes goodwill amortization of $3.2 million, net of taxes.
(e) Net loss includes goodwill amortization of $3.3 million, net of taxes.
(f) Net loss includes one-time acquisition related charges of $1.9 million, net of taxes, incurred in connection with the acquisition of Pogo as well as goodwill amortization of $3.6 million, net of taxes.
(g) Net income includes goodwill amortization of $1.8 million, net of taxes.
(h) Net income includes one-time acquisition related charges of $4.5 million, net of taxes, incurred in connection with the acquisition of Kesmai and other business combinations made during the quarter as well as goodwill amortization of $2.9 million, net of taxes.

The Company's common stock is traded in the over-the-counter market under the Nasdaq Stock Market symbol ERTS. The closing prices for the common stock in the table above represent the high and low closing prices as reported on the Nasdaq National Market.

# CORPORATE INFORMATION

## Corporate Officers

### BOARD OF DIRECTORS

M. RICHARD ASHER
Consultant, Former President
Polygram Records, Inc.

WILLIAM J. BYRON
Former Owner and President
CMA Sales

DANIEL H. CASE III
Chairman
J.P. Morgan Securities Inc.

LEONARD S. COLEMAN
Chairman of ARENACO
Senior Advisor
Major League Baseball

GARY M. KUSIN
President & Chief
Executive Officer
Kinko's, Inc.

TIMOTHY MOTT
Chairman & CEO
All Bases Covered

LAWRENCE F. PROBST III
Chairman and Chief
Executive Officer
Electronic Arts

LINDA J. SRERE
Marketing &
Advertising Consultant
Former President, Young
& Rubican Advertising

### CORPORATE OFFICERS

LAWRENCE F. PROBST III
Chairman and Chief
Executive Officer

DON A. MATTRICK
President
Worldwide Studios

JOHN S. RICCITIELLO
President and Chief
Operating Officer

WILLIAM B. GORDON
Executive Vice President
Chief Creative Officer

E. STANTON MCKEE, JR.
Executive Vice President and
Chief Financial and
Administrative Officer

NANCY L. SMITH
Executive Vice President
and General Manager
North American Publishing

DAVID L. CARBONE
Senior Vice President
Finance

DAVID GARDNER
Senior Vice President
European Publishing

RUTH A. KENNEDY
Senior Vice President,
General Counsel and
Secretary

V. PAUL LEE
Senior Vice President and
Chief Operating Officer
Worldwide Studios

J. RUSSELL RUEFF, JR.
Senior Vice President
Human Resources

## Corporate Offices

### CORPORATE HEADQUARTERS

209 Redwood Shores Parkway
Redwood City, CA 94065
(650) 628-1500

### NORTH AMERICA

Rogers, Arkansas
Burnaby, British Columbia
Costa Mesa, California
Irvine, California
Los Angeles, California
San Francisco, California
Walnut Creek, California
Maitland, Florida
Chicago, Illinois
Louisville, Kentucky
Hunt Valley, Maryland
Plymouth, Minnesota
Las Vegas, Nevada
New York, New York
Etobicoke, Ontario
Santa Isabel, Puerto Rico
Austin, Texas
Dallas, Texas
Charlottesville, Virginia
Bellevue, Washington

### INTERNATIONAL

Adelaide, Australia
The Gold Coast, Australia
Melbourne, Australia
Perth, Australia
Sydney, Australia
Neudorf, Austria
Bridgetown, Barbados
Sao Paulo, Brazil
Beijing, China
Hong Kong, China
Virum, Denmark
Chertsey, England
Turku, Finland
Lyon, France
Aachen, Germany
Milano, Italy
Tokyo, Japan
Rotterdam, The Netherlands
Auckland, New Zealand
Oslo, Norway
Lisbon, Portugal
Singapore
Johannesburg, South Africa
Seoul, South Korea
Barcelona, Spain
Madrid, Spain
Upplands Vasby, Sweden
Sennwald, Switzerland
Taipei, Taiwan
Bangkok, Thailand

### AUDITORS

KPMG LLP
Mountain View, California

### TRANSFER AGENT

Wells Fargo
Shareowner Services
South St. Paul, Minnesota

### FORM 10-K

A copy of the Company's Annual Report on Form 10-k, as filed with the Securities and Exchange Commission, will be furnished upon written request to:

Investor Relations Department
Electronic Arts Inc.
209 Redwood Shores Parkway
Redwood City, CA 94065

### ANNUAL MEETING

The Annual Meeting of stockholders will be held on August 1, 2002 at 3:00 P.M. at the Company's headquarters:

Electronic Arts Inc.
209 Redwood Shores Parkway
Redwood City, CA 94065