

Activision Blizzard, Inc.
Form 10-K
March 01, 2010

Table of Contents

UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549
FORM 10-K

(Mark one)

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

For the fiscal year ended December 31, 2009

OR

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

**For the transition period from to
Commission File Number 1-15839**

ACTIVISION BLIZZARD, INC.

(Exact name of registrant as specified in its charter)

Delaware

(State or other jurisdiction of incorporation or organization)

95-4803544

(I.R.S. Employer Identification No.)

3100 Ocean Park Blvd., Santa Monica, CA

(Address of principal executive offices)

90405

(Zip Code)

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

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

Title of each Class
Common Stock, par value \$.000001 per share

Name of Each Exchange on Which Registered
The NASDAQ Global Select Market

Edgar Filing: Activision Blizzard, Inc. - Form 10-K

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

None

Indicate by check mark if the registrant is a well-known seasoned issuer, as defined in Rule 405 of the Securities Act. Yes ☒ No ☐

Indicate by check mark if the registrant is not required to file reports pursuant to Section 13 or Section 15 (d) of the Act. Yes ☐ No ☒

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

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

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

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

Large Accelerated Filer ☒ Accelerated Filer ☐ Non-accelerated Filer ☐ Smaller Reporting Company ☐

(Do not check if a smaller
reporting company)

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

The aggregate market value of the registrant's Common Stock held by non-affiliates on June 30, 2009 as reported on the NASDAQ was \$7,039,447,050.

The number of shares of the registrant's Common Stock outstanding at February 22, 2010 was 1,249,909,250.

Documents Incorporated by Reference

Portions of the registrant's definitive Proxy Statement, to be filed with the Securities and Exchange Commission with respect to the 2010 Annual Meeting of Shareholders, are incorporated by reference into Part III of this Annual Report.

Table of Contents

ACTIVISION BLIZZARD, INC. AND SUBSIDIARIES
TABLE OF CONTENTS

	Page No.
<u>PART I.</u>	<u>3</u>
<u>Explanatory Note</u>	<u>3</u>
<u>Cautionary Statement</u>	<u>3</u>
<u>Item 1. Business</u>	<u>4</u>
<u>Item 1A. Risk Factors</u>	<u>13</u>
<u>Item 1B. Unresolved Staff Comments</u>	<u>30</u>
<u>Item 2. Properties</u>	<u>30</u>
<u>Item 3. Legal Proceedings</u>	<u>31</u>
<u>Item 4. Submission of Matters to a Vote of Security Holders</u>	<u>31</u>
<u>PART II.</u>	<u>32</u>
<u>Item 5. Market for Registrant's Common Equity, Related Stockholder Matters, and Issuer Purchases of Equity Securities</u>	<u>32</u>
<u>Item 6. Selected Financial Data</u>	<u>35</u>
<u>Item 7. Management's Discussion and Analysis of Financial Condition and Results of Operations</u>	<u>36</u>
<u>Item 7A. Quantitative and Qualitative Disclosures about Market Risk</u>	<u>66</u>
<u>Item 8. Financial Statements and Supplementary Data</u>	<u>67</u>
<u>Item 9. Changes in and Disagreements with Accountants on Accounting and Financial Disclosure</u>	<u>67</u>
<u>Item 9A. Controls and Procedures</u>	<u>67</u>
<u>Item 9B. Other Information</u>	<u>68</u>
<u>PART III.</u>	<u>69</u>
<u>Item 10. Directors, Executive Officers, and Corporate Governance</u>	<u>69</u>
<u>Item 11. Executive Compensation</u>	<u>69</u>
<u>Item 12. Security Ownership of Certain Beneficial Owners and Management and Related Stockholder Matters</u>	<u>69</u>
<u>Item 13. Certain Relationships and Related Transactions, and Director Independence</u>	<u>69</u>
<u>Item 14. Principal Accounting Fees and Services</u>	<u>69</u>
<u>PART IV.</u>	<u>70</u>
<u>Item 15. Exhibits and Financial Statement Schedule</u>	<u>70</u>
<u>SIGNATURES</u>	<u>71</u>
<u>Exhibit Index</u>	<u>E-1</u>

Table of Contents

PART I

EXPLANATORY NOTE

On July 9, 2008, a business combination (the "Business Combination") by and among Activision, Inc., Sego Merger Corporation, a wholly-owned subsidiary of Activision, Inc., Vivendi S.A. ("Vivendi"), VGAC LLC, a wholly-owned subsidiary of Vivendi, and Vivendi Games, Inc. ("Vivendi Games"), a wholly-owned subsidiary of VGAC LLC, was consummated. As a result of the consummation of the Business Combination, Activision, Inc. was renamed Activision Blizzard, Inc. ("Activision Blizzard"). For accounting purposes, the Business Combination is treated as a "reverse acquisition," with Vivendi Games deemed to be the acquirer. The historical financial statements of Activision Blizzard, Inc. prior to July 10, 2008 are those of Vivendi Games, Inc.

CAUTIONARY STATEMENT

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

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

Table of Contents

Item 1. BUSINESS

Overview

Activision Blizzard is a worldwide online, personal computer ("PC"), console, and handheld game publisher. Through Activision Publishing, Inc. ("Activision"), we are a leading international publisher of interactive software products and peripherals. Activision develops and publishes video games on various consoles, handheld platforms and the PC platform through internally developed franchises and license agreements. Activision currently offers games that operate on the Sony Computer Entertainment Inc. ("Sony") PlayStation 2 ("PS2"), Sony PlayStation 3 ("PS3"), Nintendo Co. Ltd. ("Nintendo") Wii ("Wii"), and Microsoft Corporation ("Microsoft") Xbox 360 ("Xbox 360") console systems; the Sony PlayStation Portable ("PSP") and Nintendo Dual Screen ("NDS") handheld devices; the PC; the Apple iPhone ("iPhone"); and the new handheld game system Nintendo DSi. Through Blizzard Entertainment, Inc. ("Blizzard"), we are the leader in terms of subscriber base and revenues generated in the subscription-based massively multiplayer online role-playing game ("MMORPG") category. Blizzard internally develops and publishes PC-based computer games and maintains its proprietary online-game related service, Battle.net.

Our Activision business involves the development, marketing, and sale of products directly, by license, and through our affiliate label program with certain third-party publishers. Activision's products cover diverse game categories including action/adventure, action sports, racing, role-playing, simulation, first-person action, music, and strategy. Activision's target customer base ranges from casual players to core gamers, and children to adults. During 2009, Activision released *Call of Duty: Modern Warfare 2*, *Guitar Hero V*, *DJ Hero*, *Band Hero*, *Tony Hawk: Ride*, and *PROTOTYPE* and continued to publish licensed products, with titles such as *Monsters vs. Aliens*, *Ice Age: Dawn of the Dinosaurs*, *Bakugan Battle Brawlers*, *Transformers: Revenge of the Fallen*, *X-Men Origins: Wolverine*, *Marvel Ultimate Alliance 2*, and several other titles. Activision is currently developing sequels to the Guitar Hero and Call of Duty franchises, *True Crime*, an action thriller through United Front Games, *Blur* through Bizarre Creations for the racing genre and *Singularity* a first person action game through Raven Software, among other titles.

Our Blizzard business involves the development, marketing, sales and support of role playing action and strategy games. Blizzard also develops, hosts, and supports its online subscription-based games in the MMORPG category. Blizzard is the development studio and publisher best known as the creator of *World of Warcraft* and the multiple award winning Diablo, StarCraft, and World of Warcraft franchises. Blizzard distributes its products and generates revenues worldwide through various means, including: subscriptions (which consist of fees from individuals playing *World of Warcraft*, including from sales of prepaid-cards and other value added services); retail sales of physical "boxed" products; electronic download sales of PC products; and licensing of software to third-party companies that distribute *World of Warcraft* in Russia, China and Taiwan. Blizzard has released two expansion packs to *World of Warcraft*; *World of Warcraft: The Burning Crusade* and *World of Warcraft: Wrath of the Lich King*. Blizzard is currently developing new games, including a new expansion pack to the World of Warcraft franchise, *Cataclysm*, *StarCraft II: Wings of Liberty*, which will be released with the new and improved Battle.net, and sequels to the Diablo franchise.

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

The Company

Activision, Inc. was originally incorporated in California in 1979 and was reincorporated in Delaware in December 1992. In June 2000, Activision, Inc. reorganized into a holding company organizational structure. As described in the explanatory note above, Activision, Inc. consummated a

Edgar Filing: Activision Blizzard, Inc. - Form 10-K

Table of Contents

business combination with Vivendi Games during the year ended December 31, 2008 and was renamed Activision Blizzard, Inc. Activision Blizzard is a public company traded on the NASDAQ under the ticker symbol "ATVI."

Our Strategy

Our objective is to continue to be a worldwide leader in the development, publishing, and distribution of quality interactive entertainment software, peripheral products, and online games that deliver a highly satisfying consumer entertainment experience. Through Blizzard, we plan to maintain and build upon our worldwide leadership position of online subscription-based games in the MMORPG category.

Continue to Improve Profitability. We continually strive to manage risk and increase our operating leverage and efficiency with the goal of increased profitability. We believe that the key factors affecting our future profitability will be the success rate of our core properties, proven franchises and genres, and our ability to leverage the continued growth of online and digital revenue opportunities.

Create Shareholder Value. We continue to focus and enhance shareholder return in growing operating margin, maintaining a strong balance sheet, and producing strong cash flow generation.

Grow Through Continued Strategic Acquisitions and Alliances. We intend to continue to evaluate the expansion of our resources and intellectual properties library through acquisitions, strategic relationships, and key license transactions. We will also continue to evaluate opportunities to increase our proven development expertise through the acquisition of, or investment in, selected experienced software development firms.

Competition

We compete for the leisure time and discretionary spending of consumers with other video game companies, as well as with other providers of different forms of entertainment, such as motion pictures, television, social networking, online casual entertainment and music.

The interactive entertainment industry is intensely competitive and new interactive entertainment software products and platforms are regularly introduced. Our competitors vary in size from small companies with limited resources to large corporations with greater financial, marketing, and product development resources than we have. Due to their different focuses and allocation of resources, certain of our competitors spend more money and time on developing and testing products, undertake more extensive marketing campaigns, adopt more aggressive pricing policies, pay higher fees to licensors for desirable motion picture, television, sports and character properties, and pay more to third-party software developers. In addition, competitors with large product lines and popular titles typically have greater leverage with retailers, distributors, and other customers who may be willing to promote titles with less consumer appeal in return for access to such competitor's most popular titles. We believe that the main competitive factors in the interactive entertainment industry include: product features and playability; brand name recognition; compatibility of products with popular platforms; access to distribution channels; quality of products; ease of use; price; marketing support; and quality of customer service.

We compete primarily with other publishers of personal computer and video game console interactive entertainment software. In addition to third-party software competitors, integrated video game console hardware and software companies such as Sony, Nintendo, and Microsoft compete directly with us in the development of software titles for their respective platforms. In addition, certain major media companies, such as Walt Disney Company and Time Warner, Inc., which have been investing in video game products, have increased competition within the industry. Further, a number of software publishers have developed and commercialized, or are currently developing, online games for

Table of Contents

use by consumers over the Internet, and we expect new competitors to continue to emerge in the MMORPG category.

Employees

We had approximately 7,000 total full-time and part-time employees at December 31, 2009. At December 31, 2009, 191 of our full-time employees were subject to term employment agreements with us. These agreements generally commit the employees to employment terms of between one and five years from the commencement of their respective agreements. Most of the employees subject to these agreements are executive officers or key members of the product development, sales, or marketing divisions. These individuals perform services for us as executives, directors, producers, associate producers, computer programmers, game designers, sales directors, or marketing product managers. In our experience, entering into employment agreements with these employees reduces our turnover during the development, production, and distribution phases of our entertainment software products and allows us to plan more effectively for future development and marketing activities.

A small number of our employees in France, Spain and Germany are subject to collective bargaining agreements. To date, we have not experienced any labor-related work stoppages.

Intellectual Property

Like other entertainment companies, our business is significantly based on the creation, acquisition, exploitation and protection of intellectual property. Some of this intellectual property is in the form of software code, patented technology, and other technology and trade secrets that we use to develop our games and to make them run properly. Other intellectual property is in the form of audio-visual elements that consumers can see, hear and interact with when they are playing our games.

We develop products from wholly-owned intellectual properties we create within our own studios. We also acquire the rights to include proprietary intellectual property in our products through acquisitions. In addition, we also obtain intellectual property through licenses and service agreements. These agreements typically limit our use of the licensed rights in products for specific time periods. In addition, our products that play on game consoles and handheld platforms include technology that is owned by the console, or wireless device manufacturer, and licensed non-exclusively to us for use. We also license technology from providers other than console manufacturers. While we may have renewal rights for some licenses, our business and the justification for the development of many of our products is dependent on our ability to continue to obtain the intellectual property rights from the owners of these rights on reasonable terms and at reasonable rates.

We actively engage in enforcement and other activities to protect our intellectual property. We typically own the copyright to the software code, as well as the brand or title name trademark under which our products are marketed. We register copyrights and trademarks in the United States and other countries as appropriate.

We often distribute our PC products using copy protection technology or other technological protection measures to prevent piracy and the use of unauthorized copies of our products. In addition, console manufacturers typically incorporate technological protections and other security measures in their consoles in an effort to prevent the use of unlicensed product. We are actively engaged in enforcement and other activities to protect against unauthorized copying and piracy, including monitoring online channels for distribution of pirated copies, and participating in various enforcement initiatives, education programs and legislative activity around the world.

Table of Contents

Operating Segments

We operate three operating segments: (i) Activision Publishing publishing interactive entertainment software and peripherals which includes Activision Publishing, Inc. and studios, assets, and titles previously included in Vivendi Games' Sierra Entertainment operating segment prior to the Business Combination ("Activision"), (ii) Blizzard Entertainment, Inc. and its subsidiaries publishing real-time strategy, role-playing PC games and online subscription-based games in the MMORPG category ("Blizzard"), and (iii) Activision Blizzard Distribution distribution of interactive entertainment software and hardware products ("Distribution"). These three operating segments form Activision Blizzard's core operations. Activision Blizzard's non-core exit operations ("Non-Core") represent legacy Vivendi Games' divisions or business units we have exited, divested or wound down as part of our restructuring and integration efforts as a result of the Business Combination, but that do not meet the criteria for separate reporting of discontinued operations. Prior to July 1, 2009, Non-Core activities were managed as a stand-alone operating segment; however, in light of the minimal activities and insignificance of Non-Core activities, as of that date we ceased their management as a separate operating segment and consequently we are no longer providing separate operating segment disclosure and have reclassified our prior periods' segment presentation so that it conforms to the current periods' presentation. In accordance with the provisions of the Financial Accounting Standards Board ("FASB") Accounting Standards Codification ("ASC") regarding disclosures about segments of an enterprise and related information, all prior period segment information has been restated to conform to this new segment presentation.

Activision Publishing Segment ("Activision") Business Overview

Strategy

Create, Acquire, and Maintain Strong Franchises. Activision focuses on development and publishing activities principally for products that are, or have the potential to become, franchises with sustainable mass consumer appeal and recognition. It is our experience that these products can then serve as the basis for sequels, prequels, and related new products that can be released over an extended period of time. We believe that the publishing and distribution of products based on proven franchises enhances predictability of revenues and the probability of high unit volume sales and operating profits. We own a number of successful intellectual properties such as the Call of Duty and Guitar Hero franchises. We intend to continue to develop owned franchises in the future. We have also entered into a series of strategic relationships with the owners of intellectual properties pursuant to which we have acquired the rights to publish products based on franchises such as DreamWorks' Animation LLC ("DreamWorks"), Harrah's Entertainment, Inc. ("Harrah"), Hasbro Properties Group ("Hasbro"), MGM Interactive and EON Productions Ltd. ("MGM & EON"), Mattel, Inc. ("Mattel"), Marvel Entertainment, Inc. ("Marvel"), and professional skateboarder Tony Hawk, to develop video games based on their intellectual property.

Execute Disciplined Product Selection and Development Processes. The success of our publishing business depends, in significant part, on our ability to develop high quality games that will generate high unit volume sales. Our publishing units have implemented a formal control process for the selection, development, production, and quality assurance of our products. We apply this process, which we refer to as the "Greenlight Process," to all of our products, whether externally or internally developed. The Greenlight Process includes in-depth reviews of each project at several important stages of development by a team that includes many of our highest-ranking operating managers and coordination between our sales and marketing personnel and development staff at each step in the process.

We develop our products using a combination of our internal development resources and external development resources acting under contract with us. We typically select our external developers based

Table of Contents

on their track records and expertise in producing products in the same category. One developer will often produce the same game for multiple platforms and will produce sequels to the original game. We believe that selecting and using development resources in this manner allows us to leverage the particular expertise of our internal and external development resources, which we believe enhances the quality of our products and timing of releases.

Create and Maintain Diversity in Product Mix, Platforms, and Markets. We believe that maintaining a diversified mix of products can reduce our operating risks and enhance profitability. Therefore, we develop and publish products spanning a wide range of genres, including action/adventure, action sports, racing, role-playing, simulation, first-person action, music-based gaming, and strategy. We also develop products designed for target audiences ranging from casual players to core gamers, children to adults, and mass-market consumers to "value" buyers who seek budget-priced software. Presently, the majority of products that we develop, publish, and distribute operate on the PS3, Xbox 360, and Wii console systems, the PSP, NDS and the iPhone, and the PC. We offer games with localized content in different geographies and both online and offline. We typically offer our products for use on multiple platforms to reduce the risks associated with any single platform, leverage our costs over a larger installed hardware base, and increase unit sales.

Products

Activision has been best known for our action/adventure, action sports, role-playing, simulation, first-person action, and music video game products. We have had long-term success in the first person action categories through the Call of Duty original intellectual property, including the latest release, *Call of Duty: Modern Warfare 2*, and we plan on continuing to develop this franchise. Call of Duty has achieved approximately \$3 billion life-to-date revenue. We are a leading company in the music-based gaming genre with the Guitar Hero franchise, which combines interactive software with hardware peripherals. We expanded the franchise with the additions of *DJ Hero* and *Band Hero* releases during 2009. *Band Hero* is accompanied by hardware peripherals consisting of a guitar, drum, and microphone, and *DJ Hero* is accompanied with a turntable peripheral. We have been successful in the superheroes category with our releases of titles based on the Spider-Man and X-Men properties, including the 2009 release of *Marvel Ultimate Alliance 2* and *X-Men Origins: Wolverine*. Our Tony Hawk franchise has been a leader in the action sports genre, and we have a recently released game, *Tony Hawk: Ride*, to continue the strength of this franchise with an innovative skateboard controller. We have continued our success with the DreamWorks animated movie titles, with the 2009 release of *Monsters vs. Aliens*. We have expanded our portfolio in the action/adventure genre with the launch of a new internally developed intellectual property, *PROTOTYPE*. Further, we released *Bakugan Battle Brawlers*, which is based on the top-rated television series and a best-selling toy.

In 2010, we plan to release a diversified lineup of games based on Activision's best-selling franchises including Call of Duty, Guitar Hero, and Tony Hawk, together with other well-known titles such as True Crime, Spider-Man, and Bakugan, and a select number of new intellectual property franchises such as *Blur* and *Singularity*.

Product Development and Support

Activision develops and produces titles using a model in which a core group of creative, production, and technical professionals, in coordination with our marketing and finance departments, have responsibility for the entire development and production process including the supervision and coordination of internal and external resources. This team assembles the necessary creative elements to complete a title using, where appropriate, outside programmers, artists, animators, scriptwriters, musicians and songwriters, sound effects and special effects experts, and sound and video studios. Activision believes that this model allows us to supplement internal expertise with top quality external resources on an as-needed basis.

Table of Contents

In addition, Activision often seeks out and engages independent third-party developers to create products on our behalf. We either own these products or have unlimited rights to commercially exploit these products. In other circumstances, a third-party developer may retain ownership of the intellectual property and/or technology included in the product and reserves certain exploitation rights. Activision typically selects these independent third-party developers based on their expertise in developing products in a specific category for specific platforms. Each of our third-party developers is under contract with us for specific or multiple titles. From time to time, Activision also acquires the license rights to publish and/or distribute software products that are or will be independently created by third-party developers. In such cases, the agreements with these developers provide us with exclusive publishing and/or distribution rights for a specific period of time, often for specified platforms and territories. In either case, Activision often has the ability to publish and/or distribute sequels, conversions, enhancements, and add-ons to the product initially being produced by the independent developer and Activision frequently has the right to engage the services of the original developer with regard to the further product development.

In consideration for the services that independent third-party developers provide, the developers receive a royalty, which is generally based on net sales of the developed products. Typically, developers also receive an advance, which Activision recoups from the royalties otherwise payable to the developers. The advance generally is paid in "milestone" stages. The payment at each stage is tied to the completion and delivery of a detailed performance milestone. Working with independent developers allows us to reduce our fixed development costs, share development risks with the third-party developers, take advantage of the third-party developers' expertise in connection with certain categories of products or certain platforms, and gain access to proprietary development technologies.

Activision provides various forms of product support to both our internally and externally developed titles. Activision quality assurance personnel are involved throughout the development and production of each title published. Activision subjects all such products to extensive testing before release to ensure compatibility with all appropriate hardware systems and configurations and to minimize the number of bugs and other defects found in the products. To support our products after release, Activision provides its customers online access on a 24-hour basis as well as live telephone operators who answer the help lines during regular business hours.

Marketing, Sales, and Distribution

Activision's marketing efforts include online activities (such as the creation of World Wide Web pages to promote specific titles and build user communities around our franchises), public relations, print and broadcast advertising, coordinated in-store and industry promotions (including merchandising and point of purchase displays), participation in cooperative advertising programs, direct response vehicles, and product sampling through demonstration software distributed through the Internet or on compact discs. From time to time, we also receive marketing support from hardware manufacturers and retailers in connection with their own promotional efforts. In addition, certain of our products contain software that enables customers to "electronically register" their purchases with us online.

We believe that our strong proven franchises and genres generate a loyal and devoted customer base that continues to purchase our sequels as a result of their dedication to the franchise and satisfaction from previous product purchases. We therefore market these sequels and expansion packs toward the established market as well as to broader audiences. In addition, for marketing titles based on licensed properties, we believe that we derive benefits from our continued marketing of these licensed properties as well as marketing and promotional activities of the property owners.

North America. Our products are available for sale or rental in thousands of retail outlets in North America. Our North American retail customers include, among others, Best Buy, GameStop, Target, Toys "R" Us, and Wal-Mart.

Edgar Filing: Activision Blizzard, Inc. - Form 10-K

Table of Contents

In the United States ("U.S.") and Canada, our products are sold primarily on a direct basis to mass-market retailers, consumer electronics stores, discount warehouses, and game specialty stores. We believe that a direct relationship with retail accounts results in more effective inventory management, merchandising, and communications than would be possible through indirect relationships. We have implemented electronic data interchange linkages with many of our retailers to facilitate the placing and shipping of orders. We also sell our products to a limited number of distributors.

International. Our products are sold internationally on a direct-to-retail basis, through third-party distribution and licensing arrangements, and through our wholly-owned European distribution subsidiaries. We conduct our international publishing activities through offices in the United Kingdom ("U.K."), Germany, France, Italy, Spain, Norway, the Netherlands, Sweden, Australia, China, Ireland, and Singapore. We seek to maximize our worldwide revenues and profits by releasing high quality foreign language releases concurrently with English language releases and by continuing to expand the number of direct selling relationships we maintain with key retailers in major territories.

On a worldwide basis, our largest customers, GameStop and Wal-Mart, each accounted for approximately 10% and 11% of consolidated revenues for the years ended December 31, 2009 and 2008, respectively.

Digital Distribution. Some of our products are sold in, or only in, a digital format, which allows consumers to purchase and download the game at their convenience. We partner with digital distributors to leverage this growing method of distribution. We also make available to our consumer value added downloadable contents to enhance their gaming experience through Microsoft, Sony and Nintendo's digital online services.

Affiliate Labels. In addition to our own products, we distribute a select number of interactive entertainment products that are developed and marketed by other third-party publishers through our "affiliate label" programs in North America, Europe, and the Asia Pacific region. The distribution of other publishers' products allows us to increase the efficiencies of our sales force and provides us with the ability to better ensure adequate shelf presence at retail stores for all of the products that we distribute. Revenues that we receive from distributing other publishers' titles mitigate the risk that a particular title or titles published by us fails to meet expectations. Services we provide under our affiliate label programs include order solicitation, in-store marketing, logistics and order fulfillment, and sales channel management, as well as other accounting and general administrative functions. Our current affiliate label partners include LucasArts, as well as several affiliate label partners in our "value" business, which offers budget-priced software to the public. Each affiliate label relationship is unique and may pertain only to distribution in certain geographic territories and may be further limited only to specific titles or titles for specific platforms.

Manufacturing

Activision prepares a set of master program copies, documentation, and packaging materials for our products for each hardware platform on which the product will be released. We also manufacture separate hardware peripherals, such as the guitar, drum and microphone for *Guitar Hero World Tour* and *Band Hero*, the new turntable for *DJ Hero*, and the new skateboard controller for *Tony Hawk: Ride*. With respect to products for use on the Sony, Nintendo, and Microsoft systems, our disk and hardware peripheral duplication, packaging, printing, manufacturing, warehousing, assembly, and shipping are performed by third-party subcontractors and Company-owned distribution facilities.

To maintain protection over their hardware technologies, Sony, Nintendo, and Microsoft generally specify or control the manufacturing and assembly of finished products. We deliver the master materials to the licensor or its approved replicator, which then manufactures finished goods and delivers them to us for distribution under our label. We use manufacturers authorized by Sony, Nintendo, or Microsoft

Table of Contents

to make the hardware peripherals for *Guitar Hero* titles, *Band Hero*, *DJ Hero*, and *Tony Hawk: Ride*. At the time our product unit orders are filled by the manufacturer, we become responsible for the costs of manufacturing and the applicable per unit royalty on such units, even if the units do not ultimately sell.

Blizzard Entertainment Segment ("Blizzard") Business Overview

Strategy

Maintain and Build upon Our Leadership Position in the MMORPG Category and PC Online Categories. Blizzard plans to maintain and build upon our leadership position in the MMORPG genre by regularly providing new content and game features to further solidify the loyalty of our subscriber base, as well as to expand the global game footprint to new markets.

We believe that the PC online market will remain a growing category throughout the world. The large and growing PC installed base in all regions and the continuing development of broadband connectivity facilitates online games and community experiences while creating access to new potential customers. Given the success of *World of Warcraft* and *StarCraft* in Asia, we expect to continue to be well positioned to capture the growing consumer demand in this region. Blizzard is among the few companies with video game franchises created and developed in the U.S. that have gained and retained success in Asia. *World of Warcraft* and *StarCraft* are strong brands in Asia. Titles in those series have been among the most played games in the region for many years and support a thriving professional gaming industry, particularly in South Korea. During 2009, Blizzard entered into licensing arrangements for *World of Warcraft*, *StarCraft II*, Battle.net and *Warcraft III* with an affiliated company of NetEase.com, Inc. in China. Further, as *World of Warcraft* is a server-based game, only playable online, Blizzard is one of the few companies that can target markets that have been dominated by piracy and monetize former illegitimate players as well as expand in markets that have not been penetrated by consoles, but offer a large PC installed base.

Products

Blizzard is a leading company in the subscription-based MMORPG category. *World of Warcraft* was initially launched in November 2004 in North America, Australia, and New Zealand; and was subsequently launched in South Korea, Europe, China, Singapore, Taiwan, Hong Kong, and Macau in 2005; Malaysia in 2006; and Thailand in 2007. As of December 31, 2009, *World of Warcraft* had approximately 11.5 million active subscribers. *World of Warcraft* is available in various languages based on the regions in which it is played and has earned awards and praise from publications around the world. Blizzard launched an expansion pack to *World of Warcraft*, *World of Warcraft: The Burning Crusade*, in January 2007 in North America, Europe, Australia, New Zealand, Singapore, Malaysia, and Thailand; in South Korea in February 2007; Taiwan, Hong Kong, and Macau in April 2007; and China in September 2007. Blizzard launched the second *World of Warcraft* expansion pack, *World of Warcraft: Wrath of the Lich King*, in November 2008 in all territories except China, where we intend to launch in 2010. Blizzard plans to launch the third installment of the *World of Warcraft* expansion pack, *World of Warcraft: Cataclysm* in 2010. Revenues associated with the *World of Warcraft* franchises accounted for 98%, 97%, and 97% of Blizzard's consolidated net revenues for the years ended December 31, 2009, 2008, and 2007, respectively.

Additionally, in the PC online category, in 2010, Blizzard plans to release *StarCraft II: Wings of Liberty* together with the new and improved Battle.net, which will provide integration of gameplay and community, customer services, and digital distribution of content in 2010. Blizzard has also announced the development of a sequel for *Diablo*, an action role-playing game.

Edgar Filing: Activision Blizzard, Inc. - Form 10-K

Table of Contents

Product Development and Support

As a development studio, creator and publisher of the World of Warcraft, Diablo, and StarCraft franchises, Blizzard focuses on creating well-designed, high quality games. Product development is handled internally by a strong core group of talented designers, producers, programmers, artists, and sound engineers. To maintain its current subscribers and attract new subscribers, Blizzard continues to develop new patches to upgrade *World of Warcraft*. In addition to its headquarters in Irvine, California, Blizzard maintains offices in or around Austin, Texas; Paris, France; Cork, Ireland; Seoul, South Korea; Shanghai, China; and Taipei, Taiwan, to provide 24/7 game support to *World of Warcraft* players in their native language, enhance online community management, and tailor marketing initiatives to specific regions.

Marketing, Sales, and Distribution

Blizzard distributes its product and generates revenues worldwide through various means: subscriptions (which consist of fees from individuals playing *World of Warcraft*, prepaid cards, and other value added services such as the ability to change "factions", the ability to transfer "realms" and the ability to purchase a virtual pet), retail sales of physical "boxed" product, electronic download sales of PC products, and licensing of software to third-party companies that distribute *World of Warcraft* in Russia, China and Taiwan. In addition, Blizzard operates a free online game service, Battle.net, which attracts millions of active players, making it one of the largest online-game related services in the world. Battle.net is a service that allows players to connect and play Blizzard games and strengthens brand loyalty among current Blizzard gamers.

Activision Blizzard Distribution Segment ("Distribution") Business Overview

We distribute interactive entertainment hardware and software products in Europe through our European distribution subsidiaries: Centresoft in the U.K.; and NBG in Germany. These subsidiaries act as wholesalers in the distribution of products and also provide packaging, logistical and sales services. They provide services to our publishing operations and to various third-party publishers, including Sony, Nintendo, and Microsoft. Centresoft is Sony's exclusive distributor of PlayStation products to the independent market sector of the U.K.

We entered into the distribution business to obtain distribution capacity in Europe for our own products, while supporting the distribution infrastructure with third-party sales, and to diversify our operations in the European market. Centresoft and our other distribution subsidiaries operate in accordance with strict confidentiality procedures to provide independent services to various third-party publishers.

Additional Financial Information

See Item 7 "Management's Discussion and Analysis of Financial Condition and Results of Operations" and Note 14 of the Notes to Consolidated Financial Statements included in Item 8 of this Annual Report on Form 10-K for certain additional information regarding operating segments and geographic areas. See the Critical Accounting Policies section under Item 7 "Management's Discussion and Analysis of Financial Condition and Results of Operations" for a discussion of our practices with regard to several working capital items, such as rights of returns, and inventory practices. See the Management's Overview of Business Trends under Item 7 "Management's Discussion and Analysis of Financial Condition and Results of Operations" for a discussion of the impact of seasonality on our business.

Table of Contents

Available Information

Our website is located at <http://www.activisionblizzard.com>. Our Annual Report on Form 10-K, quarterly reports on Form 10-Q, current reports on Form 8-K, and amendments to those reports filed or furnished pursuant to Section 13(a) or 15(d) of the Securities Exchange Act of 1934, as amended (the "Exchange Act"), are available free of charge through our website. The information found on our website is not a part of, and is not incorporated by reference into, this or any other report that we file with or furnish to the Securities and Exchange Commission ("SEC").

The public may also read and copy any materials we file with the SEC at the SEC's Public Reference Room at Station Place, 100 F Street, N.E., Washington, D.C. 20549 (information on the operation of the Public Reference Room is available by calling the SEC at 1-800-SEC-0330). The SEC also maintains a web site that contains reports, proxy and information statements, and other information regarding issuers that file electronically with the SEC at <http://www.sec.gov>.

Item 1A. RISK FACTORS

A continuing deterioration of general economic conditions could result in a reduction in discretionary spending by consumers that could reduce demand for our products.

Most of our products involve discretionary spending on the part of consumers. Consumers are generally more willing to make discretionary purchases, including purchases of products like ours, during periods in which favorable economic conditions prevail. As a result, our products may be sensitive to general economic conditions and economic cycles. A continuation or worsening of current, adverse worldwide economic conditions, including declining consumer confidence, inflation, recession, rising unemployment and volatile gasoline prices, may lead consumers to delay or reduce purchases of our products. Reduced consumer spending may also require us to incur increased selling and promotional expenses. A reduction or shift in domestic or international consumer spending could negatively impact our business, results of operations and financial condition.

Our business may be harmed if our distributors, retailers or other parties with which we do business cannot honor their existing credit arrangements, default on their obligations to us, or seek protection under the bankruptcy laws.

We rely on various business partners for several important aspects of our business, including distribution of our products, product development, and intellectual property licensing. Some of these business partners are highly-leveraged or small businesses that may be particularly vulnerable to difficult economic conditions. As a result of the current economic downturn, we are subject to increased counterparty risks, including the risks that our business partners may default on their obligations to us or seek protection under the bankruptcy laws.

For example, retailers and distributors in the interactive entertainment industry have from time to time experienced significant fluctuations in their businesses and a number of them have failed. We typically make sales to most retailers and some distributors on unsecured credit, with terms that vary depending upon the customer's credit history, solvency, credit limits, and sales history, as well as whether the customer can obtain sufficient credit insurance. Challenging economic conditions may impair the ability of our customers to pay for products they have purchased, and as a result, our reserves for doubtful accounts and write-off of accounts receivable could increase and, even if increased, may turn out to be insufficient. Moreover, even in cases where we have insolvency risk insurance to protect against a customer's bankruptcy, insolvency, or liquidation, this insurance typically contains a significant deductible and co-payment obligation, and does not cover all instances of non-payment. As a result, a payment default by or the insolvency or business failure of a significant customer could significantly harm our business and financial results.

Table of Contents

The insolvency or business failure of other types of business partners could result in disruptions to the manufacturing or distribution of our products or the cancellation of contractual arrangements that we consider to be favorable.

Current general economic conditions may adversely affect other aspects of our business.

We are unable to predict the likely duration and severity of the current adverse economic conditions in the U.S. and other countries, and all of the effects the current macroeconomic conditions may have on our business. Among other things, because we generally maintain large cash reserves, we are subject to the risk that inflation may cause the real value of our cash and cash equivalents to decline. Furthermore, uncertainties concerning the likely length and severity of the economic downturn cause our forecasts to be subject to even greater risks and uncertainties.

Fluctuations in currency exchange rates may have a negative impact on our results of operations.

We transact business in various currencies other than the U.S. dollar and have significant international sales and expenses denominated in currencies other than the U.S. dollar, subjecting us to currency exchange rate risks. A substantial portion of our international sales and expenses are denominated in local currencies, including certain major currencies, such as the euro and U.K. pound, and emerging market currencies, such as the Korean won and Chinese renminbi, which could fluctuate against the U.S. dollar. We have, in the past, utilized currency derivative contracts to hedge certain foreign exchange exposures, with hedge tenors of generally less than 12 months, as well as managing these exposures with natural offsets. We may also, from time to time, hedge non-U.S. dollar earnings. Our principal counterparty in respect of currency derivative contracts is Vivendi, though we periodically evaluate and may use similar arrangements with other counterparties. There can be no assurance that we will continue these programs, or that we will be successful in managing exposure to currency exchange rate risks.

Vivendi owns a majority of our outstanding shares of common stock and the interests of Vivendi and its subsidiaries may conflict with the interests of our other shareholders.

Vivendi and its subsidiaries currently own approximately 57% of our issued and outstanding shares of common stock.

As a result of the Business Combination, Vivendi has the ability to nominate a majority of our board of directors and determine the outcome of certain matters submitted to our stockholders, such as the approval of significant transactions and the declaration of dividends on our common stock. As a result, actions that may be supported by a majority of stockholders other than Vivendi may be blocked by Vivendi. In addition, Vivendi's ownership may affect the liquidity in the market for our common stock.

Furthermore, the ownership position and governance rights of Vivendi may discourage a third party from proposing a change of control or other strategic transaction concerning Activision Blizzard. As a result, our common stock may trade at prices that do not reflect a "control premium" to the same extent as do the stocks of similarly situated companies that do not have a stockholder with an ownership interest as large as Vivendi's ownership interest.

We are a "controlled company" within the meaning of NASDAQ rules and, as a result, are exempt from certain corporate governance requirements.

For so long as Vivendi or any other entity or group owns more than 50% of the total voting power of our common shares, we will be a "controlled company" within the meaning of NASDAQ rules and,

Table of Contents

as a result, qualify for exemptions from certain corporate governance requirements. As a controlled company, we are exempt from several NASDAQ standards, including the requirements:

that a majority of our Board consists of independent directors;

that our prospective directors be nominated solely by independent directors; and

that the compensation of our executive officers be determined solely by independent directors.

We currently rely on these exemptions and as a result, a majority of our Board is not independent (as defined by the NASDAQ rules). In addition, while we have a nominating and corporate governance committee and a compensation committee, these committees do not consist entirely of independent directors. Accordingly, our stockholders do not have the same protections afforded to stockholders of companies that are subject to all of the NASDAQ corporate governance requirements.

We depend on a relatively small number of franchises for a significant portion of our revenues and profits.

A significant portion of our revenues has historically been derived from products based on a relatively small number of popular franchises and these products are responsible for a disproportionately high percentage of our profits. For example, our top three franchises, Call of Duty, Guitar Hero, and World of Warcraft, accounted for approximately 68% of our net revenues for the year ended December 31, 2009. We expect that a limited number of popular franchises will increasingly produce a disproportionately high percentage of our revenues and profits. Due to this dependence on a limited number of franchises, the failure to achieve anticipated results by one or more products based on these franchises may significantly harm our business and financial results.

Sales of certain titles are affected by hardware peripheral availability, which increases our exposure to imbalances between projected and actual demand.

Some of our titles involve one or more separate hardware peripherals, such as the guitar which accompanies *Guitar Hero* titles, the guitar, drum and microphone which accompany *Band Hero*, the turntable which accompanies *DJ Hero* and the skateboard controller which accompanies *Tony Hawk: Ride*. Typically, we sell such software both in bundles with the hardware peripherals and on a stand-alone basis. Consumers may not want to buy such game software if they cannot also buy the hardware peripherals. If we underestimate demand or otherwise are unable to produce sufficient quantities of the hardware peripherals of an acceptable quality or allocate too few peripherals to geographic markets and hardware platforms where demand exceeds supply, we will forego revenue. This may also create greater opportunities for competitors to develop or gain share with competitive product offerings.

In addition, if we overestimate demand and make too many peripherals, or allocate too many peripherals to geographic markets and hardware platforms where there is insufficient demand, we will incur unrecoverable manufacturing costs for unsold units as well as for unsold game software. In either case, hardware peripheral manufacturing and allocation decisions may negatively affect our financial performance.

The increasing importance and complexity of hardware peripherals in our business increases our exposure to hardware manufacturing and shipping risks, including availability of sufficient third-party manufacturing capacity, and increases in manufacturing and shipping costs.

A limited number of manufacturers are authorized by Sony, Nintendo or Microsoft to make the hardware peripherals for Guitar Hero, and the majority of those manufacturers are located in China. Anything that impacts the ability of those manufacturers to produce or otherwise supply the hardware peripherals for us or increases their costs of production, including the revocation of the first party license to produce the hardware, the utilization of such manufacturer's capacity by one of our competitors, changes in safety, environmental or other regulations applicable to the peripherals and the

Table of Contents

manufacturing thereof, natural or manmade disasters that disrupt manufacturing, transportation or communications, labor shortages, civil unrest or issues generally negatively impacting international companies operating in China, increases in the price of petroleum or other raw materials, increases in fuel prices and other shipping costs, and increases in local labor costs in China, may adversely impact our ability to supply those peripherals to the market and the prices we must pay for those peripherals, and therefore our financial performance. Additionally, the increasing complexity and expense of these hardware peripherals increases the risk of production delays or product defects.

Our sales may decline substantially without warning and in a brief period of time because a substantial portion of our sales are made to a relatively small number of key customers and because we do not have long-term contracts for the sale of our products.

In the U.S. and Canada, Activision has primarily sold its products on a direct basis to mass-market retailers, consumer electronics stores, discount warehouses, and game specialty stores. Activision products are sold internationally on a direct-to-retail basis, through third-party distribution and licensing arrangements and through our wholly-owned European distribution subsidiaries. Activision's sales are made primarily on a purchase order basis without long-term agreements or other forms of commitments. We had two customers, Wal-Mart and GameStop, which each accounted for approximately 10% of our consolidated revenues for the year ended December 31, 2009 and accounted for approximately 18% and 10% of our consolidated gross receivables at December 31, 2009, respectively. The loss of, or significant reduction in sales to, any of Activision's principal retail customers or distributors could significantly harm our business and financial results. The concentration of sales in a small number of large customers also could make us more vulnerable to collection risk if one or more of these large customers becomes unable to pay for our products or seeks protection under the bankruptcy laws. In addition, having such a large portion of our total net revenue concentrated in a few customers reduces our negotiating leverage with these customers.

We may not be able to maintain our distribution relationships with key vendors and customers.

Our NBG and Centresoft subsidiaries distribute interactive entertainment software and hardware products and provide related services in Germany, and the U.K., respectively, and via export in other European countries for a variety of entertainment software publishers, many of which are our competitors, and hardware manufacturers. From time to time, they also maintain exclusive relationships to serve certain retail customers. These services are generally performed subject to limited-term arrangements. Although we expect to use reasonable efforts to retain these vendors and retail customer relationships, we may not be successful in this regard. The cancellation or non-renewal of one or more of these arrangements could adversely affect our business and financial results.

Indications of some regulatory uncertainty exist regarding our licensee's ongoing ability to operate World of Warcraft in China on a paying basis without interruption.

In April 2009, Blizzard agreed to license World of Warcraft to an affiliated company of NetEase.com, Inc. ("NetEase") in China for a term of three years. World of Warcraft was unavailable to players in China from June 7, 2009 (local), the date on which our prior license arrangements expired, until July 30, 2009 (local), when NetEase began making the game available to our previous players in China in a test format without charge. Subsequently, NetEase advised us that it received the necessary regulatory approval, and accordingly, relaunched the game to subscribers in China. Having World of Warcraft unavailable for play or available only on an unpaid basis would result in lost revenues and income, and having it unavailable for a prolonged period could have a negative effect on our reputation and subscriber base in China.

Table of Contents

As online functionality has become an increasingly important feature of our software products, we may need to defer the recognition of an increasing amount of revenue, which may adversely affect the net revenue, net income and earnings per share that we will report under U.S. GAAP.

As online functionality has become a more important component of gameplay, an increasing number of our online-enabled games contain a more-than-inconsequential separate service deliverable in addition to the product, and our performance obligations for these games extend beyond the sale of the games. Vendor-specific objective evidence of fair value does not exist for the online services, as we do not plan to separately charge for this component of online-enabled games. As a result, we recognize revenues from the sale of certain online-enabled games for certain platforms ratably over an estimated service period. In addition, we defer the costs of sales of those titles. If we are required to recognize a greater portion of the revenue of a sale after shipment, or if we are required to recognize revenue over a longer service period, there may be an adverse effect on our reported net revenue, net income and earnings per share under accounting principles generally accepted in the United States of America ("U.S. GAAP").

A substantial portion of our revenue and profitability will depend on the subscription-based massively multiplayer online role-playing game category. If we do not maintain our leadership position in this category, our financial results could suffer.

Activision Blizzard is the leading global developer, publisher and distributor in terms of subscriber base and revenues in the subscription-based MMORPG category, due to the popularity of Blizzard's *World of Warcraft* and related expansion packs. Subscription revenues from this game comprise a significant portion of our consolidated revenues. To remain the leader in the MMORPG category, it is important that we continue to refresh *World of Warcraft* or develop new MMORPG products that are favorably received by both our existing customer base and new customers. A number of software publishers have developed and commercialized or are currently developing online games for use by consumers over the Internet which pose a threat to the popularity of *World of Warcraft*, and we expect new competitors to continue to emerge in the MMORPG category. If consumer demand for *World of Warcraft* games declines and we have not introduced new MMORPG or other products that replace *World of Warcraft's* potentially decreasing revenue, or added other sources of revenue, our financial condition could suffer. Additionally, if new technologies are developed that replace MMORPG games, consumer preferences trend away from MMORPG games or new business models emerge that offer online subscriptions for free or at a substantial discount to current MMORPG subscription fees, our revenue and profitability may decline.

The development of MMORPG products requires substantial up-front expenditures. We may not be able to recover development costs for our future MMORPG products.

Consumer preferences for games are usually cyclical and difficult to predict, and even the most successful titles remain popular for only limited periods of time, unless refreshed with new content. In order to remain competitive in the MMORPG market, we must continuously develop new products and enhancements to existing products. Because of the significant complexity of MMORPG games, these products require a longer development time and are more expensive to create than traditional console game products. In addition, the long lead time involved in developing a MMORPG product and the significant allocation of financial resources that each product requires means it is critical that we accurately predict consumer demand for new MMORPG products. If future MMORPG products do not achieve expected market acceptance or generate sufficient sales and subscription revenues upon introduction, we may not be able to recover the development and marketing costs associated with new products, and our financial results could suffer.

Table of Contents

Our results of operation may suffer if consumer preferences shift away from the genres from which we currently derive the majority of our revenue.

A significant portion of our revenue is derived from products in the music-based gaming, first-person action and MMORPG genres. Consumer preferences for games are difficult to predict, and if interest in those genres declines, even if our share of those genres is stable or expands, we will not be able to sustain the same level of sales of our products in those genres, and our financial results could suffer. For example, we recorded a non-cash impairment charge on finite-lived intangible assets for 2009 as a result of the weaker environment for casual and music games and our net revenues were lower in 2009 as compared to 2008 in part due to this environment.

A substantial portion of Activision Blizzard's revenues is derived from subscriptions paid by World of Warcraft subscribers. If these customers cancel their subscriptions, our results of operations may suffer.

A substantial portion of our revenues is generated by subscription fees paid by consumers who play *World of Warcraft*. Typically, *World of Warcraft* subscribers purchase one to three month memberships that are cancelable, without penalty, at the end of the membership period. If *World of Warcraft* subscribers become dissatisfied, they may choose not to renew their memberships in order to engage in other forms of entertainment (including competing MMORPG offerings) and we may not be able to replace lost subscribers. Additionally, if general economic conditions deteriorate further, consumers may decrease their discretionary spending on entertainment items such as MMORPG games and users may choose not to renew their *World of Warcraft* subscriptions. A decrease in the overall subscription base of *World of Warcraft* could substantially harm our operating results.

We depend on servers to operate our MMORPG business and other games of ours that have online features. If we were to lose server capacity, for any reason, our business could suffer.

Our business relies on the continuous operation of our data servers. Any broad based catastrophic server malfunction, a significant intrusion by hackers that circumvents our security measures, or a failure of our disaster recovery service would likely interrupt the operation of our MMORPG game, *World of Warcraft*, and other games of ours with online features and could result in the loss of sales for such games (including subscription-based sales for *World of Warcraft*). An extended interruption of service could harm our reputation and operating results.

We must project our future server needs and make advance purchases of servers to accommodate expected business demands. If we underestimate the amount of server capacity our business requires or if our business were to grow more quickly than expected, our customers may experience service problems, such as slow or interrupted gaming access. Insufficient server capacity may result in our experiencing decreased sales, a loss of our customer base, and adverse consequences to our reputation. Conversely, if we overestimate the amount of server capacity required by our business, we may incur additional operating costs that would adversely affect our operating margins.

We may not accurately predict the amount of Internet bandwidth necessary to sustain our online gaming businesses.

Our online gaming businesses are dependent on the availability of sufficient Internet bandwidth. An increase in the price of bandwidth could have an adverse effect on operating margins since we may not be able to increase our prices or subscriber levels to compensate for such costs. Because of the importance of our MMORPG business to our revenues and results of operations, our ability to access adequate bandwidth to support our business is critical. To secure bandwidth access, we have entered into arrangements with several bandwidth providers and entered into long-term contracts with some of them to secure future bandwidth capacity. If the price of bandwidth were to decrease, our contractual commitments to pay higher prices could affect our ability to compete with other video game producers.

Table of Contents

Conversely, because we purchase additional bandwidth based on anticipated growth, our bandwidth capacity is sometimes larger than necessary to sustain our existing needs. If our projected online business growth is delayed or does not occur, we will incur larger bandwidth expenses than necessary. If we underestimate the amount of bandwidth that our online business requires, and our purchased bandwidth capacity is insufficient to meet demand, our business and reputation may suffer.

Our results of operations or reputation may be harmed as a result of offensive consumer posted content.

We are subject to risks associated with the collaborative online features in our games, such as *World of Warcraft's* online chat feature, which allows consumers to post narrative comment, in real time, that is visible to other players. Despite our efforts to restrict inappropriate consumer content, from time to time objectionable and offensive consumer content may be posted to a *World of Warcraft* gaming site or the sites of other games or game services, such as Battle.net, with online chat features or game forums which allow consumers to post comments. We may be subject to lawsuits, governmental regulation or restrictions, and consumer backlash (including decreased sales and harmed reputation), as a result of consumers posting offensive content, any of which could harm our operating results.

A substantial portion of World of Warcraft's subscribers pays their subscription fees using credit cards. Credit card fraud could have a negative impact on our business and operating results.

A substantial portion of the subscription revenue generated by *World of Warcraft* is paid by subscribers using credit cards. At times, there may be attempts to use fraudulently obtained credit card numbers to pay for *World of Warcraft* upgrades or subscriptions. Additionally, the credit card numbers of *World of Warcraft's* subscribers are maintained in a proprietary database that may be compromised internally or externally by fraudulent maneuvers. As fraudulent schemes become more sophisticated, it may become more difficult and more costly for us to detect credit card fraud and protect subscriber information. An increase in credit card fraud could have an adverse effect on our business and operating results.

The future success of our business depends on our ability to release popular products in a timely manner.

The life of any one console or hand-held game product is relatively short and generally involves a relatively high level of sales during the first few months after introduction followed by a rapid decline in sales. Because revenues associated with an initial product launch generally constitute a high percentage of the total revenues associated with the life of a product, delays in product releases or disruptions following the commercial release of one or more new products could have an adverse effect on our operating results and cause our operating results to be materially different from expectations. It is therefore important for us to be able to continue to develop many high quality new products that are popularly received and to release those products in a timely manner. If we are unable to continue to do so, our business and financial results may be negatively affected.

Our business is "hit" driven. If we do not deliver "hit" titles, or if consumers prefer competing products, our sales could suffer.

While many new products are regularly introduced, only a relatively small number of high-quality "hit" titles account for a significant portion of net revenue. Competitors may develop titles that imitate or compete with our "hit" titles, and take sales away from them or reduce our ability to command premium prices for those titles. "Hit" products published by our competitors may take a larger share of consumer spending than anticipated, which could cause our product sales to fall below expectations. If our competitors develop more successful products or offer competitive products at lower prices, or if we do not continue to develop consistently high-quality and well received products, our revenues, margins, and profitability could decline. In addition, our own "hit" products could compete with our other titles, reducing sales for those other titles.

Table of Contents

If we are unable to successfully develop or market owned intellectual property, we may publish fewer "hit" titles and our revenues may decline.

Some of our products are based on intellectual property that we have developed internally or acquired from third parties. If this new intellectual property does not gain market acceptance, whether because we are unable to successfully create consumer appeal and brand recognition or otherwise, our revenues, margins, and profitability could decline.

If we are unable to maintain or acquire licenses to intellectual property, we may publish fewer "hit" titles and revenues may decline.

Some of our products are based on intellectual property and other character or story rights licensed from third parties. These license and distribution agreements are limited in scope and time, and we may not be able to renew key licenses when they expire or to include new products in existing licenses. Our loss of a significant number of intellectual property licenses or relationships with licensors, or inability to obtain additional licenses of significant commercial value could have an adverse effect on our ability to develop new products and therefore on our business and financial results. Additionally, the failure of intellectual property we license to be popularly received could impact the market acceptance of those products in which the intellectual property is included. Such lack of market acceptance could result in the write-off of the unrecovered portion of acquired intellectual property assets, which could harm our business and financial results. Furthermore, the competition for these licenses and distribution agreements is often intense. Competition for these licenses may also increase the advances, guarantees, and royalties that must be paid to the licensor.

Competition within and to the interactive entertainment industry is intense, and competitors may succeed in reducing our sales.

We compete with other publishers of PC and video game console interactive entertainment software and peripherals. Those competitors vary in size from small companies with limited resources to very large corporations with significantly greater financial, marketing, and product development resources than we have. For example, integrated video game console hardware and software companies such as Sony, Nintendo, and Microsoft compete directly with us in the development of software titles for their respective platforms. Further, certain major media companies, such as the Walt Disney Company and Time Warner, Inc., which have been investing in video game products, have increased competition within the industry. Our competitors may spend more money and time on developing and testing products, undertake more extensive marketing campaigns, adopt more aggressive pricing policies, pay higher fees to licensors for desirable motion picture, television, sports, music and character properties, pay more to third-party software developers, or otherwise develop more commercially successful products for the PC or video game platforms than we do. In addition, competitors with large product lines and popular titles typically have greater leverage with retailers, distributors, and other customers who may be willing to promote titles with less consumer appeal in return for access to those competitors' most popular titles.

We also compete with other forms of interactive entertainment, such as casual games like iPhone applications and other mobile phone games, and games developed for use by consumers on social networking sites. Future increased consumer acceptance and increases in the availability such games or other online games, or technological advances in online game software or the Internet, could result in a decline in platform-based software and negatively impact sales of our console and hand-held products. Newer technological advances in online game software may also render products such as *World of Warcraft* obsolete. Additionally, direct sales of software over the Internet by competitors could adversely affect our distribution business.

Table of Contents

We also compete with other forms of entertainment and leisure activities. For example, the overall growth in the use of the Internet and online services such as social networking sites by consumers may pose a competitive threat if customers and potential customers spend less of their available time using interactive entertainment software and more using the Internet, including those online services.

Increased sales of used video game products could lower our sales.

Certain of our larger customers sell used video games, which are generally priced lower than new video games and do not result in any revenue to the publisher of the games, and the market for these games has been growing. If our customers continue to increase their sales of used video games, it could negatively affect our sales of new video games and have an adverse impact on our operating results.

Our business is subject to the risks and uncertainties of international trade.

We conduct business throughout the world, and we derive a substantial amount of revenue from international trade, particularly from Europe, Australia, and Asia. We expect that international revenues will continue to account for a significant portion of total revenues in the future and, moreover, believe that Asia will be a significant source of growth for us.

As such, we are subject to risks inherent in foreign trade, including increased tariffs and duties, fluctuations in currency exchange rates, shipping delays, increases in transportation costs, increases in local labor costs in overseas locations where our hardware peripherals are manufactured, international political, regulatory and economic developments and differing local business practices, all of which may impact operating margins or make it more difficult, if not impossible, for us to conduct business in foreign markets.

For example, a deterioration in relations between either us or the U.S. and any country in which we have significant operations or sales, or the implementation of government regulations in such a country, including China in particular, could result in the adoption or expansion of trade restrictions that harm our business and operating results. For instance, to operate in China, *World of Warcraft* must have regulatory approval. Such regulatory approval will also be required to sell the *World of Warcraft: Wrath of the Lich King* expansion pack in China. A decision by the Chinese government to revoke its approval for *World of Warcraft* or to decline to approve the *World of Warcraft: Wrath of the Lich King* expansion pack or other future products would adversely impact our operating results. Additionally, in the past, legislation has been implemented in China that has required modifications to the *World of Warcraft* software. The future implementation of similar laws may require engineering modifications to our products that are not cost-effective, if even feasible at all, or could degrade the customer experience to the point where customers cease to purchase such products.

Further, if government regulations or restrictions prevent us from repatriating internationally derived revenue into the U.S., or a country's tax structure makes repatriation prohibitively expensive, we may not transfer such revenue into the U.S., which could affect our ability to reinvest or utilize such amounts in our business.

In addition, cultural differences may affect consumer preferences and limit the popularity of titles that are "hits" in the U.S. If we do not correctly assess consumer preferences in the countries in our market, our sales and revenue may be lower than expected.

We rely on independent third parties to develop some of our software products.

We rely on independent third-party software developers to develop some of our software products. Because we depend on these developers, we are subject to the following risks:

continuing strong demand for developers' resources, combined with the recognition they receive in connection with their work, may cause developers who worked for us in the past either to

Edgar Filing: Activision Blizzard, Inc. - Form 10-K

Table of Contents

work for a competitor in the future or to renegotiate agreements with us on terms less favorable for us;

limited financial resources and business expertise and inability to retain skilled personnel may force developers out of business prior to completing products or require us to fund additional costs; and

a competitor may acquire the businesses of key developers or sign them to exclusive development arrangements. In either case, we would not be able to continue to engage such developers' services for our products, except for those developers that are contractually obligated to complete development for us.

Increased competition for skilled third-party software developers also has compelled us to agree to make significant advance payments on royalties to game developers. If the products subject to these arrangements do not generate sufficient revenues to recover these royalty advances, we would have to write-off unrecovered portions of these payments, which could harm our business and financial results. Typically, we pay developers a royalty based on a percentage of net revenues from product sales, less agreed upon deductions, but from time to time, we have agreed to pay developers fixed per unit product royalties after royalty advances are fully recouped. To the extent that sales prices of products on which we have agreed to pay a fixed per unit royalty are marked down, our profitability could be adversely affected.

Our platform licensors set the royalty rates and other fees that must be paid to publish games for their platforms, and therefore have significant influence on our costs.

We pay a licensing fee to the hardware manufacturer for each copy of a product manufactured for that manufacturer's game platform. In order to publish products for new hardware platforms, we must take a license from the platform licensor which gives the platform licensor the opportunity to set the fee structure that we must pay in order to publish games for that platform. Similarly, the platform licensors have retained the flexibility to change their fee structures for online gameplay and features for their consoles and the manufacturing of products. The control that platform licensors have over the fee structures for their platforms and online access makes it difficult for us to predict our costs and profitability in the medium to long term. It is also possible that platform licensors will not renew our existing licenses. Any increase in fee structures or nonrenewal of licenses could have a significant negative impact on our business models and profitability, particularly for Activision, as the publishing of products for console systems is the largest portion of Activision's business.

Our business is highly dependent on the success, timely release and availability of new video game platforms and on the continued availability of existing video game platforms, as well as our ability to develop commercially successful products for these platforms.

We derive a substantial portion of our revenue from the sale of products for play on video game platforms manufactured by third parties, such as Sony's PlayStation 3 and PlayStation Portable, Microsoft's Xbox 360 and Nintendo's Wii and NDS. For example, sales of products for consoles accounted for 51% of our consolidated net revenue in 2009. The success of our business is driven in large part by the availability of an adequate supply of these video game platforms, our ability to accurately predict which platforms will be successful in the marketplace, and our ability to develop commercially successful products for these platforms. We must make product development decisions and commit significant resources well in advance of the anticipated introduction of a new platform. A new platform for which we are developing products may be delayed, may not succeed or may have a shorter life cycle than anticipated. Alternatively, a platform for which we have not devoted significant resources could be more successful than initially anticipated, causing us to miss a meaningful revenue opportunity. Additionally, if the platforms for which we are developing products are not released when

Table of Contents

anticipated, are not available in adequate quantities to meet consumer demand, or do not attain wide market acceptance, our revenues may suffer, we may be unable to fully recover our investment in developing those products, and our financial performance may be harmed.

Transitions in console platforms could adversely affect the market for interactive entertainment software.

In 2005, Microsoft released the Xbox 360 and, in 2006, Sony and Nintendo introduced the PlayStation 3 and Wii, respectively. When new console platforms are announced or introduced into the market, consumers typically reduce their purchases of game console entertainment software products for current console platforms in anticipation of new platforms becoming available. During these periods, sales of game console entertainment software products we publish may slow or even decline until new platforms are introduced and achieve wide consumer acceptance. This decline may not be offset by increased sales of products for the new console platforms. As console hardware moves through its life cycle, hardware manufacturers typically enact price reductions and decreasing prices may put downward pressure on software prices. During platform transitions, we may simultaneously incur costs both in continuing to develop and market new titles for prior-generation video game platforms, which may not sell at premium prices, and also in developing products for current-generation platforms, which will not generate immediate or near-term revenue. As a result, our operating results during platform transitions may be more volatile and more difficult to predict than during other times, and such volatility may cause greater fluctuations in our stock price.

We must make significant expenditures to develop products for new platforms which may not be successful.

We must make substantial product development and other investments in a particular platform well in advance of introduction of the platform and may be required to realign our product portfolio and development efforts in response to market changes. Furthermore, development costs for new console platforms are greater than such costs for current console platforms. If increased costs are not offset by higher revenues and other cost efficiencies, operating results will suffer and our financial position will be harmed. If the platforms for which we develop new software products or modify existing products do not attain significant market penetration, we may not be able to recover our development costs, which could be significant, and our business and financial results could be significantly harmed.

If we are unable to sustain launch pricing on current-generation titles, our operating results will suffer.

We expect to be able to price current-generation titles for the Microsoft Xbox 360, Sony's PlayStation 3 and the Nintendo Wii at a premium launch level, but if we are unable to sustain launch pricing on these current-generation titles, whether because retailers elect to price these products at a lower price or otherwise, we may experience a negative effect on our margins and operating results.

Platform licensors are our chief competitors and frequently control the manufacturing of and have broad approval rights over our console and hand-held video game products.

Generally, when we develop interactive entertainment software products for hardware platforms offered by Sony, Nintendo, or Microsoft, the products are manufactured exclusively by that hardware manufacturer or their approved replicator.

The agreements with these manufacturers include certain provisions, such as approval rights over all software products and related hardware peripherals and promotional materials and the ability to change the fee they charge for the manufacturing of products, which allow them substantial influence over the cost and the release schedule of such interactive entertainment software products. In addition, because each of the manufacturers is also a publisher of games for its own hardware platforms and manufactures products for all of its other licensees, a manufacturer may give priority to its own

Table of Contents

products or those of our competitors in the event of insufficient manufacturing capacity. Accordingly, Sony, Nintendo, or Microsoft could cause unanticipated delays in the release of our products as well as increases to projected development, manufacturing, marketing, or distribution costs, which could harm our business and financial results.

In addition, platform licensors control our ability to provide online game capabilities for console platform products and in large part establish the financial terms on which these services are offered to consumers. Currently, Microsoft provides online capabilities for the Xbox 360, Sony provides online capabilities for PlayStation 3 products, and Nintendo provides online capabilities for the Wii. In each case, compatibility code and/or the consent of the licensor are required for us to include online capabilities in its console products. As these capabilities become more significant, the failure or refusal of licensors to approve our products may harm our business and financial results.

Our market is subject to rapid technological change, and if we do not adapt to, and appropriately allocate our new resources among, emerging technologies, our revenues would be negatively affected.

Technology changes rapidly in the interactive entertainment industry. We must continually anticipate and adapt our products to emerging technologies. When we choose to incorporate a new technology into a product or to develop a product for a new platform, operating system or media format, we often are required to make a substantial investment one to two years prior to the introduction of the product. If we invest in the development of video games incorporating a new technology or for a new platform that does not achieve significant commercial success, our revenues from those products likely will be lower than we anticipated and may not cover our development costs. If, on the other hand, we elect not to pursue the development of products incorporating a new technology or for new platforms that achieve significant commercial success, our revenues would also be adversely affected, and it may take significant time and resources to shift product development resources to that technology or platform. Any such failure to adapt to, and appropriately allocate resources among, emerging technologies would harm our competitive position, reduce our share and significantly increase the time we take to bring popular products to market.

We may face difficulty obtaining access to retail shelf space necessary to market and sell our products effectively.

Retailers typically have a limited amount of shelf space and promotional resources, and there is intense competition among consumer interactive entertainment software products for high quality retail shelf space and promotional support from retailers. To the extent that the number of products and platforms increases, competition for shelf space may intensify and may require us to increase our marketing expenditures. Retailers with limited shelf space typically devote the most and highest quality shelf space to those products expected to be best sellers. We cannot be certain that our new products will consistently achieve such "best seller" status. Due to increased competition for limited shelf space, retailers and distributors are in an increasingly better position to negotiate favorable terms of sale, including price discounts, price protection, marketing and display fees, and product return policies. Our products constitute a relatively small percentage of most retailers' sales volume. We cannot be certain that retailers will continue to purchase our products or to provide those products with adequate levels of shelf space and promotional support on acceptable terms. A prolonged failure in this regard may significantly harm our business and financial results.

Our products may be subject to legal claims.

In prior years, at least two lawsuits have been filed against numerous video game companies, including against Activision, by the families of victims who were shot and killed by teenage gunmen in attacks perpetrated at schools. These lawsuits alleged that the video game companies manufactured and/or supplied these teenagers with violent video games, teaching them how to use a gun and causing

Table of Contents

them to act out in a violent manner. These lawsuits have been dismissed. Similar additional lawsuits may be filed in the future. Although our general liability insurance carrier has agreed to defend lawsuits of this nature with respect to the prior lawsuits, it is uncertain whether insurance carriers would do so in the future, or if such insurance carriers would cover all or any amounts for which we might be liable if such future lawsuits are not decided in our favor. If such future lawsuits are filed and ultimately decided against us and the relevant insurance carrier does not cover the amounts for which we may be liable, it could have an adverse effect on our business and financial results. Payment of significant claims by insurance carriers may make insurance coverage materially more expensive or unavailable in the future, thereby exposing us to additional risk.

If our products contain defects, our business could be harmed significantly.

Software products and hardware peripherals as complex as the ones published and distributed by us may contain undetected errors and defects. This risk is often higher when such products or peripherals are first introduced or when new versions are released. Failure to avoid, or to timely detect and correct, such errors or defects could result in loss of, or delay in, market acceptance, and could significantly harm our business, financial results, and reputation.

We may permit our customers to return products and to receive pricing concessions which could reduce net revenues and results of operations.

We are exposed to the risk of product returns and price protection with respect to our distributors and retailers. Return policies allow distributors and retailers to return defective, shelf-worn, and damaged products in accordance with terms granted. Price protection, when granted and applicable, allows customers a credit against amounts owed with respect to merchandise unsold by them. We may permit product returns from, or grant price protection to, our customers under certain conditions. These conditions include compliance with applicable payment terms, delivery of weekly inventory and sell-through reports, and consistent participation in the launches of premium title releases. We may also consider other factors, including the facilitation of slow-moving inventory and other market factors. When we offer price protection, it is offered with respect to a particular product to all of our retail customers (although only customers who meet the conditions detailed above are entitled to such price protection). Activision also offers a 90-day limited warranty to its end users that Activision products will be free from manufacturing defects. Although we maintain a reserve for returns and price protection, and although we may place limits on product returns and price protection, we could be forced to accept substantial product returns and provide substantial price protection to maintain our relationships with retailers and our access to distribution channels. Product returns and price protection that exceed our reserves could significantly harm our business and financial results.

Our business is subject to risks generally associated with the entertainment industry, any of which could significantly harm our operating results.

Our business is subject to risks that are generally associated with the entertainment industry, including the popularity, price and timing of the release of our games and the platforms on which they are played, economic conditions that adversely affect discretionary consumer spending, changes in consumer demographics, the availability and popularity of other forms of entertainment, and critical reviews and public tastes and preferences, which may change rapidly and cannot necessarily be predicted. Many of these risks are beyond our control. These risks could negatively impact our business and financial results.

We are exposed to seasonality in the sale of our products.

The interactive entertainment industry is highly seasonal, with the highest levels of consumer demand occurring during the year-end holiday buying season. As a result, net revenues, gross profits,

Table of Contents

and operating income have historically been highest during the second half of the year. Receivables and credit risk are likewise higher during the second half of the year as customers stock up on our products for the holiday season. Further, delays in development, licensor approvals, or manufacturing can also affect the timing of the release of products, causing us to miss key selling periods such as the year-end holiday buying season.

We may not be able to adequately adjust our cost structures in a timely fashion in response to a sudden decrease in demand.

A significant portion of our selling and general and administrative expense is comprised of personnel and facilities. In the event of a significant decline in revenues, we may not be able to exit facilities, reduce personnel, or make other changes to our cost structures without disruption to operations or without significant termination and exit costs. Management may not be able to implement such actions in a timely manner, if at all, to offset an immediate shortfall in revenues and profit.

If we do not continue to attract and retain key personnel, we will be unable to effectively conduct our business.

Our success depends to a significant extent on our ability to identify, hire, and retain skilled personnel, particularly personnel with the specialized skills needed to create the high-quality "hit" titles upon which our business is substantially dependent. The software industry is characterized by a high level of employee mobility and aggressive recruiting among competitors for personnel with technical, marketing, sales, product development, and management skills. We may have difficulties in attracting and retaining skilled personnel or may incur significant costs in order to do so. If we are unable to attract additional qualified employees or retain the services of key personnel, our business and financial results could be negatively impacted.

Our products are subject to the threat of piracy and unauthorized copying, and inadequate intellectual property laws and other protections could prevent us from enforcing or defending our proprietary technologies. We may also face legal risks arising out of user-generated content.

We regard our software as proprietary and rely on a variety of methods, including a combination of copyright, patent, trademark and trade secret laws and employee and third-party nondisclosure agreements, to protect our proprietary rights. We own or license various copyrights, patents, and trademarks. We are aware that some unauthorized copying occurs, and if a significantly greater amount of unauthorized copying of our software products were to occur, it could cause harm to our business and financial results.

Policing unauthorized use of our products is difficult, and software piracy is a persistent problem for us, especially in certain countries. Further, the laws of some countries where our products are or may be distributed either do not protect their products and intellectual property rights to the same extent as the laws of the U.S., or are poorly enforced. Legal protection of our rights may be ineffective in such countries. In addition, though we take steps to make the unauthorized copying and distribution of our products more difficult and to otherwise enforce and police our rights, as do the manufacturers of consoles on which some of those games (and a majority of those games published by Activision) are played, our efforts and the efforts of the console manufacturers may not be successful in controlling the piracy of our products in all instances. Organized pirate operations have been expanding globally. In addition, the proliferation of technology designed to circumvent the protection measures used in our products, the availability of broadband access to the Internet, the ability to download pirated copies of games from various Internet sites and peer-to-peer networks, and the widespread proliferation of Internet cafes using pirated copies of our products all have contributed to an expansion in piracy. This could have a negative effect on our growth and profitability in the future.

Table of Contents

Moreover, as we leverage our software products using technologies such as the Internet and online services, and as user-generated content increases, our ability to protect our intellectual property rights and to avoid infringing intellectual property rights of others may diminish. We cannot be certain that existing intellectual property laws will provide adequate protection for our products in connection with these emerging technologies.

Data breaches involving the source code for our products or customer or employee data stored by us could adversely affect our reputation and revenues.

We store the source code and game assets for our interactive entertainment software products as created. In addition, we store confidential information with respect to our customers and employees. A breach of the systems on which such source code and assets, account information (including personally identifiable information) and other sensitive data is stored could lead to piracy of our software or fraudulent activity resulting in claims and lawsuits against us in connection with data security breaches. A data intrusion into a server for a game with online features, such as *World of Warcraft*, could also disrupt the operation of such game. If we are subject to data security breaches, we may have a loss in sales or be forced to pay damages or other amounts, which could adversely affect profitability. In addition, any damage to our reputation resulting from a data breach could have an adverse impact on our revenues and future growth prospects, or increased costs arising from the implementation of additional security measures.

We may be subject to intellectual property claims.

As the number of interactive entertainment software products increases and the features and content of these products continue to overlap, software developers increasingly may become subject to infringement claims. Many of our products are highly realistic and feature materials that are based on real world examples, which may be the subject of intellectual property infringement claims of others. In addition, our products often utilize complex, cutting edge technology that may become subject to emerging intellectual property rights of others. Although we take steps to avoid knowingly violating the intellectual property rights of others, it is possible that third parties still may claim infringement. From time to time, we receive communications from third parties regarding such claims. Existing or future infringement claims against us, whether valid or not, may be time consuming, distracting to management and expensive to defend.

Intellectual property litigation or claims could force us to do one or more of the following:

cease selling, incorporating, supporting or using products or services that incorporate the challenged intellectual property;

obtain a license from the holder of the infringed intellectual property, which if available at all, may not be available on commercially favorable terms; or

redesign the affected interactive entertainment software products or hardware peripherals, which could result in additional costs, delay introduction and possibly reduce commercial appeal of the affected products.

Any of these actions may harm our business and financial results.

Our products are subject to ratings by the Entertainment Software Rating Board and similar agencies. Our failure to obtain our target ratings for our products could negatively impact our sales.

The Entertainment Software Rating Board (the "ESRB") is a self-regulatory body in the U.S. that provides consumers of interactive entertainment software with ratings information, including information relating to violence, nudity, or sexual content contained in software titles. Certain countries other than the U.S. have also established similar rating systems as prerequisites for product sales in

Table of Contents

those countries. In some countries, a company may be required to modify its products to comply with the requirements of the rating systems, which could delay or disrupt the release of any given product, or may prevent its sale altogether in certain territories. The relevant ESRB ratings include "Everyone" (age 6 and older), "Everyone 10+" (age 10 and older), "Teen" (age 13 and over), or "Mature" (age 17 and over). Certain of our titles have received a "Mature" rating. None of our titles has received the "Adults Only" rating (18 and over). If we are unable to obtain the ratings we have targeted for our products as a result of changes in the ESRB's ratings standards or for other reasons, including the adoption of legislation in this area, our business and prospects could be negatively affected.

Our business, products, and distribution are subject to increasing regulation of content in key territories. If we do not successfully respond to these regulations, our business may suffer.

Legislation is continually being introduced that may affect both the content and the distribution of our products. Those laws and regulations vary by territory. For example, privacy laws in the U.S and Europe impose various restrictions on the collection, storage and use of personal information.

In addition, many foreign countries, such as China and Germany, have laws that permit governmental entities to censor the content and/or advertising of interactive entertainment software or prohibit certain types of content. In the U.S, numerous laws have been introduced at one time or another at the federal and state level which attempt to restrict the content of games or the distribution of such products (although, to date, most courts that have ruled on such legislation have ruled in a manner favorable to the interactive entertainment industry).

The adoption and enforcement of such legislation in the U.S. and other countries in which we do business may harm the sales of our products, as products we are able to offer to our customers and the size of the potential market for our products may be limited. We may also be required to modify certain products or alter our marketing strategies to comply with new and possibly inconsistent regulations, which could be costly or delay the release of our products.

If one or more of our titles were found to contain objectionable undisclosed content, our business could suffer.

Throughout the history of the interactive entertainment industry, many video games have been designed to include certain hidden content and gameplay features that are accessible through the use of in-game cheat codes or other technological means that are intended to enhance the gameplay experience. However, in some cases, objectionable undisclosed content or features have been found in our and other publishers' interactive entertainment software products. In a few cases, the ESRB has reacted to discoveries of undisclosed content and features in other publisher's products by changing the rating that was originally assigned to the product, requiring the publisher to change the game and/or game packaging and/or fining the publisher. Retailers have on occasion reacted to the discovery of such undisclosed content by removing these games from their shelves, refusing to sell them, and demanding that their publishers accept them as product returns. Likewise, some interactive entertainment software consumers have reacted to the revelation of undisclosed content by refusing to purchase such games, demanding refunds for games they have already purchased, refraining from buying other games published by the company whose game contained the objectionable material, and, on at least one occasion, filing a lawsuit against the publisher of the product containing such content.

We have implemented preventive measures designed to reduce the possibility of objectionable undisclosed content from appearing in the video games we publish. Nonetheless, these preventive measures are subject to human error, circumvention, overriding, and reasonable resource constraints. If a video game we publish is found to contain undisclosed content, we could be subject to any of these consequences and our reputation could be harmed, which could have a negative impact on our operating results and financial condition, and our business and financial performance could be significantly harmed.

Table of Contents

We engage in acquisitions, and may encounter difficulties in integrating these businesses and, therefore, may not realize the anticipated benefits of the acquisitions.

As part of our business strategy we, from time to time, acquire complementary companies or businesses, enter into strategic alliances and joint ventures and make investments to further our business. In the past several years, we have made various acquisitions and entered into joint venture arrangements intended to complement or expand our business, and may continue to do so in the future. The success of these transactions will depend on our ability to integrate assets and personnel acquired in these transactions and to cooperate with our strategic partners. We may encounter difficulties in integrating acquisitions with our operations, and in managing strategic investments. Furthermore, we may not realize the degree, or timing, of benefits we anticipate when we first enter into a transaction. Any of the foregoing could adversely affect our business and results of operations.

Our involvement in joint ventures decreases our ability to manage risk.

We conduct some of our operations through joint ventures in which we share control with our joint venture partners. Although we enter into joint venture arrangements in order to share risks with our joint venture partners, these arrangements may also decrease our ability to manage risk. As with any joint venture arrangement, differences in views among the joint venture participants may result in delayed decisions or in failures to agree on major issues. There is the risk that our joint venture partners may at any time have economic, business or legal interests or goals that are inconsistent with ours. There is also risk that our joint venture partners may be unable to meet their economic or other obligations and we may be required to fulfill those obligations alone. Failure by us, or an entity in which we have a joint venture interest, to adequately manage the risks associated with any joint ventures could have an adverse effect on the financial condition or results of operations of our joint ventures and, in turn, our business and operations.

We anticipate entering into additional joint ventures with other entities. We cannot assure that we will undertake such joint ventures or, if undertaken, that such joint ventures will be successful or produce the anticipated benefits.

Historically, our stock price has been highly volatile.

The trading price of our common stock has been and could continue to be subject to wide fluctuations in response to many factors, including for example, but without limitation:

quarter to quarter variations in results of operations;

the announcement of new products;

the announcement of lower prices on competing products;

product development or release schedule;

general conditions in the computer, software, entertainment, media or electronics industries, and in the economy;

timing of the introduction of new platforms and delays in the actual release of new platforms;

hardware manufacturers' announcements of price changes for hardware platforms;

consumer acceptance of hardware platforms;

consumer spending trends;

the outcome of lawsuits or regulatory investigations in which we may become involved;

changes in earnings estimates or buy/sell recommendations by analysts;

Table of Contents

sales or acquisitions of common stock by our directors or executive management, or by Vivendi and its affiliates; and

investor perceptions and expectations regarding our products, plans and strategic position, and those of our competitors and customers.

In addition, the public stock markets have been experiencing extreme price and trading volume volatility. This volatility has significantly affected the market prices of securities of many technology companies for reasons often unrelated to the operating performance of the specific companies. These broad market fluctuations may adversely affect the market price of our common stock.

Subject to certain limitations, Vivendi may sell common stock at any time, which could cause our stock price to decrease.

Vivendi may sell the shares of our stock that it owns, including pursuant to a registered underwritten public offering under the Securities Act of 1933, as amended (the "Securities Act"), or in accordance with Rule 144 under the Securities Act. We have entered into an investor agreement with Vivendi, which includes registration rights and which gives Vivendi the right to require us to register all or a portion of its shares at any time, subject to certain limitations. The sale of a substantial number of shares of common stock by Vivendi within a short period of time could cause our stock price to decrease, and make it more difficult for us to raise funds through future offerings of common stock.

Changes in tax rates or exposure to additional tax liabilities could adversely affect our operating results and financial condition.

We are subject to income taxes in the U.S. and in various other jurisdictions. Significant judgment is required in determining our worldwide provision for income taxes and, in the ordinary course of business, there are many transactions and calculations where the ultimate tax determination is uncertain. We are required to estimate future taxes. Although we currently believe our tax estimates are reasonable, the estimate process is inherently uncertain, and such estimates are not binding on tax authorities. The effective tax rate could be adversely affected by changes in the business, including the mix of earnings in countries with differing statutory tax rates, changes in tax elections, and changes in applicable tax laws, as well as other factors. Further, tax determinations are regularly subject to audit by tax authorities and developments in those audits could adversely affect our income tax provision. Should the ultimate tax liability exceed estimates, our income tax provision and net income could be adversely affected.

We are also required to pay taxes other than income taxes, such as payroll, sales, use, value-added, net worth, property, and goods and services taxes, in both the U.S. and various other jurisdictions. Tax authorities regularly examine these non-income taxes. There can be no assurance that the outcomes from these examinations, changes in the business or changes in applicable tax rules will not have an adverse effect on our operating results and financial condition.

Item 1B. UNRESOLVED STAFF COMMENTS

None.

Item 2. PROPERTIES

Our principal corporate and administrative offices are located at 3100 Ocean Park Boulevard, Santa Monica, California 90405 under a lease set to expire in December 2010. Other significant leased facilities include: our Blizzard offices located in Irvine, California 92612 and our North America Distribution warehouse located in Fresno, California 93725, for which the leases are set to expire in October 2013 and February 2011, respectively.

Edgar Filing: Activision Blizzard, Inc. - Form 10-K

Table of Contents

The following is a summary of the principal leased offices we maintained as of December 31, 2009:

Purpose	North America	Europe	Asia	Total
	Square footage of leased properties			
Corporate Offices	140,151	3,961		144,112
Activision Product Development & Publishing Facilities (Activision Segment)	1,331,366	146,704	21,474	1,499,544
Blizzard Product Development & Publishing Facilities (Blizzard Segment)	325,600	86,000	29,450	441,050
Distribution Facilities (Distribution Segment)		458,100		458,100
Sales offices	14,847			14,847
Total	1,811,964	694,765	50,924	2,557,653

In total, we lease approximately 50 facilities in 13 countries, including the United States, Canada, the U.K., Germany, France, Italy, Spain, Australia, Sweden, China, the Netherlands and Ireland. We anticipate no difficulty in extending the leases of our facilities or obtaining comparable facilities in suitable locations, as needed, and we consider our facilities to be adequate for our current needs.

Item 3. LEGAL PROCEEDINGS

The discussion in Note 18 to the Consolidated Financial Statements regarding legal proceedings is incorporated herein by reference. Additionally, with regard to the internal human resource inquiry and related matters described in Note 18 to the Consolidated Financial Statements, please refer to the Risk Factors set forth on pp. 15 and 26.

Item 4. SUBMISSION OF MATTERS TO A VOTE OF SECURITY HOLDERS [RESERVED]

Table of Contents**PART II****Item 5. MARKET FOR REGISTRANT'S COMMON EQUITY, RELATED STOCKHOLDER MATTERS, AND ISSUER PURCHASES OF EQUITY SECURITIES**

Our common stock is quoted on the NASDAQ National Market under the symbol "ATVI."

The following table sets forth, for the periods indicated, the high and low reported sale prices for our common stock. At February 22, 2010, there were 1,853 holders of record of our common stock. For periods prior to July 9, 2008, the reported prices are for shares of Activision, Inc. before completion of the Business Combination. In addition, in July 2008, the Board of Directors approved a two-for-one split of our outstanding common stock and the prices set forth below have been restated as if the split had occurred as of the earliest period presented.

	High	Low
<i>2008</i>		
First Quarter ended March 31, 2008	\$ 14.88	\$ 12.56
Second Quarter ended June 30, 2008	18.65	13.46
Third Quarter ended September 30, 2008	19.28	14.04
Fourth Quarter ended December 31, 2008	15.39	8.28
<i>2009</i>		
First Quarter ended March 31, 2009	\$ 10.99	\$ 8.14
Second Quarter ended June 30, 2009	13.14	9.85
Third Quarter ended September 30, 2009	13.00	10.79
Fourth Quarter ended December 31, 2009	12.96	10.25

Edgar Filing: Activision Blizzard, Inc. - Form 10-K

Table of Contents

Stock Performance Graph

This performance graph shall not be deemed "filed" for purposes of Section 18 of the Exchange Act or otherwise subject to the liabilities under that Section, and shall not be deemed to be incorporated by reference into any filing of Activision Blizzard Inc. under the Exchange Act or the Securities Act of 1933, as amended.

The graph below matches the cumulative 69-month total return of holders of Activision, Inc.'s common stock with the cumulative total returns of the NASDAQ Composite index and the RDG Technology Composite index. The graph assumes that the value of the investment in our common stock and in each of the indexes (including reinvestment of dividends) was \$100 on March 31, 2004 and tracks it through December 31, 2009.

For periods prior to July 9, 2008, the share price information for Activision Blizzard is for Activision, Inc. before completion of the Business Combination. In connection with the Business Combination, Activision, Inc. changed its fiscal year end from March 31 to December 31.

COMPARISON OF 6 YEAR CUMULATIVE TOTAL RETURN*

Among Activision Blizzard, Inc., The NASDAQ Composite Index
And The RDG Technology Composite Index

*
100 invested on 3/31/04 in stock or index, including reinvestment of dividends.
Fiscal year ending December 31.

	3/04	3/05	3/06	3/07	3/08	12/08	12/09
Activision Blizzard, Inc.	100.00	124.74	154.97	212.84	306.90	194.18	249.70
NASDAQ Composite	100.00	102.04	118.97	126.37	116.84	80.73	116.61
RDG Technology Composite	100.00	96.69	114.09	118.05	113.80	76.05	122.68

The stock price performance included in this graph is not necessarily indicative of future stock price performance.

Table of Contents

Cash Dividends

On February 10, 2010 Activision Blizzard's Board of Directors declared a cash dividend of \$0.15 per common share payable on April 2, 2010 to shareholders of record at the close of business on February 22, 2010. Although we expect dividends to be an annual occurrence, future dividends will depend upon our earnings, financial condition, cash requirements, future prospects, and other factors deemed relevant by our Board of Directors. We did not pay cash dividends in 2008 or 2009.

Upon completion of the Business Combination on July 9, 2008, Vivendi Games returned \$79 million of capital to Vivendi and distributed its excess cash on-hand, as defined in the Business Combination Agreement, of \$79 million to Vivendi.

Return of capital to Vivendi related to settlement of pre-Business Combination taxes

Prior to the Business Combination, Vivendi Games' income taxes are presented in the financial statements as if Vivendi Games were a stand-alone taxpayer even though Vivendi Games' operating results are included in the consolidated federal, certain foreign, and state and local income tax returns of Vivendi or Vivendi's subsidiaries. Based on the subsequent filing of these tax returns by Vivendi or Vivendi's subsidiaries, we determined that the amount paid by Vivendi Games was greater than the actual amount due (and settled) based upon filing of these returns. This difference between the amount paid and the actual amount due (and settled) represents a return of capital to Vivendi, which was required in accordance with the terms of the Business Combination agreement immediately prior to the close of the Business Combination.

Stock Splits

In July 2008, the Board of Directors approved a two-for-one split of our outstanding common stock effected in the form of a stock dividend ("the split"). The split was paid September 5, 2008 to shareholders of record as of August 25, 2008. The par value of our common stock was maintained at the pre-split amount of \$.000001 per share. The Consolidated Financial Statements and Notes thereto, including all share and per share data, have been restated as if the split had occurred as of the earliest period presented.

Edgar Filing: Activision Blizzard, Inc. - Form 10-K

Table of Contents

Issuer Repurchase of Equity Securities (amounts in millions, except number of shares and per share data)

The following table provides the number of shares repurchased and average price paid per share during each quarter for the year ended December 31, 2009, and the approximate dollar value of shares that may yet be purchased under our \$1.25 billion stock repurchase program as of December 31, 2009.

Period	Total number of shares repurchased(1)	Average price paid per share	Total number of shares purchased as part of publicly announced plans or programs	Approximate dollar value of shares that may yet be purchased under the plan (in millions)
January 1, 2009 - March 31, 2009	31,877,760	\$ 9.82	31,877,760	\$ 561
April 1, 2009 - June 30, 2009	19,371,247	11.85	19,371,247	332
July 1, 2009 - September 30, 2009	24,585,978	11.85	24,585,978	290
October 1, 2009 - October 31, 2009				
November 1, 2009 - November 30, 2009	4,400,900	11.43	4,400,900	240
December 1, 2009 - December 31, 2009	20,483,348	10.98	20,483,348	15
Total	100,719,233	\$ 11.01	100,719,233	

(1)

All purchases were made pursuant to a stock repurchase program, announced on November 5, 2008, authorized by our Board of Directors pursuant to which we were originally authorized to repurchase up to \$1 billion of our common stock. On July 31, 2009, our Board of Directors authorized an increase of \$250 million to the stock repurchase program bringing the total authorization to \$1.25 billion.

In addition to the repurchases in the above table, we had agreed to repurchase approximately 1.3 million shares of our common stock at an average price per share of \$11.32 for a value of \$15 million that had not yet settled at December 31, 2009. This completed the \$1.25 billion stock repurchase program.

On February 10, 2010, we announced that our Board of Directors authorized a new stock repurchase program under which we may repurchase up to \$1 billion of our common stock on terms and conditions to be determined by the Company until the earlier of December 31, 2010 or a determination by the Board of Directors to discontinue the repurchase program.

Item 6. SELECTED FINANCIAL DATA

On July 9, 2008, a business combination (the "Business Combination") by and among Activision, Inc., Sego Merger Corporation, a wholly-owned subsidiary of Activision, Inc., Vivendi S.A. ("Vivendi"), VGAC LLC, a wholly-owned subsidiary of Vivendi, and Vivendi Games, Inc. ("Vivendi Games"), a wholly-owned subsidiary of VGAC LLC, was consummated. As a result of the consummation of the Business Combination, Activision, Inc. was renamed Activision Blizzard, Inc. For accounting purposes, the Business Combination is treated as a "reverse acquisition," with Vivendi Games deemed to be the acquirer. The historical financial statements of Activision Blizzard, Inc. prior to July 9, 2008 are those of Vivendi Games, Inc. (see Note 1 of the Notes to Consolidated Financial Statements included in Item 8 of this Annual Report on Form 10-K). Therefore, 2009 and 2008 financial data is not comparable with prior periods.

Edgar Filing: Activision Blizzard, Inc. - Form 10-K

Table of Contents

The following table summarizes certain selected consolidated financial data, which should be read in conjunction with our Consolidated Financial Statements and Notes thereto and with Management's Discussion and Analysis of Financial Condition and Results of Operations included elsewhere in this Form 10-K. The selected consolidated financial data presented below at and for each of the years in the five-year period ended December 31, 2009 is derived from our Consolidated Financial Statements. All amounts set forth in the following tables are in millions, except per share data.

	For the years ended December 31,				
	2009	2008	2007	2006	2005
Statement of Operations Data:					
Net revenues	\$ 4,279	\$ 3,026	\$ 1,349	\$ 1,018	\$ 780
Net income (loss)	113	(107)	227	139	45
Net income (loss) per share(1)	0.09	(0.11)	0.38	0.24	0.08

	At December 31,				
	2009	2008	2007	2006	2005
Balance Sheet Data:					
Total assets	\$ 13,742	\$ 14,465	\$ 879	\$ 758	\$ 539

(1)

Stock Split In July 2008, the Board of Directors approved a two-for-one split of our outstanding shares of common stock effected in the form of a stock dividend ("the split"). The split was paid September 5, 2008 to shareholders of record at August 25, 2008.

Cash Dividends

On February 10, 2010 Activision Blizzard's Board of Directors declared a cash dividend of \$0.15 per common share payable on April 2, 2010 to shareholders of record at the close of business on February 22, 2010. Although we expect dividends to be an annual occurrence, future dividends will depend upon our earnings, financial condition, cash requirements, future prospects, and other factors deemed relevant by our Board of Directors. We did not pay cash dividends in 2009, 2008, 2007, 2006 or 2005.

Item 7. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

Business Overview

Activision Blizzard, Inc. is a worldwide online, personal computer ("PC"), console, and handheld game publisher. The terms "Activision Blizzard," the "Company," "we," "us," and "our" are used to refer collectively to Activision Blizzard, Inc. and its subsidiaries. Based upon our current organizational structure, we operate three operating segments as follows:

Activision Publishing, Inc.

Activision Publishing, Inc. ("Activision") is a leading international publisher of interactive software products and peripherals. Activision develops and publishes video games on various consoles, handheld platforms and the PC platform through internally developed franchises and license agreements. Activision currently offers games that operate on the Sony Computer Entertainment Inc. ("Sony") PlayStation 2 ("PS2"), Sony PlayStation 3 ("PS3"), Nintendo Co. Ltd. ("Nintendo") Wii ("Wii"), and Microsoft Corporation ("Microsoft") Xbox 360 ("Xbox 360") console systems; the Sony PlayStation Portable ("PSP") and Nintendo Dual Screen ("NDS") handheld devices; the PC; the iPhone; and the new handheld game system Nintendo DSi. Our Activision business involves the development, marketing, and sale of products directly, by license, and through our affiliate label program with certain

Table of Contents

third-party publishers. Activision's products cover diverse game genres including action/adventure, action sports, racing, role-playing, simulation, first-person action, music, and strategy. Activision's target customer base ranges from casual players to core gamers, and children to adults.

Blizzard Entertainment, Inc.

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

Activision Blizzard Distribution

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

Business Combination

On July 9, 2008, a business combination (the "Business Combination") by and among Activision, Inc., Sego Merger Corporation, a wholly-owned subsidiary of Activision, Inc., Vivendi S.A. ("Vivendi"), VGAC LLC, a wholly-owned subsidiary of Vivendi, and Vivendi Games, Inc. ("Vivendi Games"), a wholly-owned subsidiary of VGAC LLC, was consummated. As a result of the consummation of the Business Combination, Activision, Inc. was renamed Activision Blizzard, Inc. For accounting purposes, the Business Combination is treated as a "reverse acquisition," with Vivendi Games deemed to be the acquirer. The historical financial statements of Activision Blizzard, Inc. prior to July 10, 2008 are those of Vivendi Games.

Activision Blizzard's Non-Core Exit Operations

Activision Blizzard's non-core exit operations ("Other" or "Non-Core") represent legacy Vivendi Games' divisions or business units that we have exited, divested, or wound down as part of our restructuring and integration efforts as a result of the Business Combination, but that do not meet the criteria for separate reporting of discontinued operations. Prior to July 1, 2009, Non-Core activities were managed as a stand-alone operating segment; however, in light of the minimal activities and insignificance of Non-Core activities, as of that date we ceased their management as a separate operating segment and consequently we are no longer providing separate operating segment disclosure and have reclassified our prior periods' segment presentation so that it conforms to the current periods' presentation.

Table of Contents

Key Market Conditions and Business Results

Market conditions were challenging in 2009 with total retail software sales in the U.S. and Europe down 10% from the prior year, according to The NPD Group, Charttrack, and Gfk. With the weakened economy, retailers focused on reducing inventories. The market weakness was most notable in the casual game and music genres, as compared to core gamer performing titles, with casual consumers scaling back their purchases, including making fewer purchases of higher-priced point peripheral-based games in the music genre.

For 2009, Activision Blizzard's consolidated net revenues were \$4,279 million, and consolidated net income was \$113 million, which included a \$409 million charge from the impairment of finite-lived intangible assets reflecting the impact of the weaker market for the casual and music genres. The Company generated \$1,183 million in net cash from operating activities.

Notwithstanding, this challenging macroeconomic environment, Activision Blizzard grew its share by 1.8 points over the previous year across all platforms to 16% in the combined U.S. and European market, according to The NPD Group, Charttrack, and Gfk.

Following the year end, the Company announced a new stock repurchase program under which the Company can repurchase up to \$1 billion of the Company's common stock. The Board of Directors also declared a cash dividend of \$0.15 per common share payable on April 2, 2010 to shareholders of record at the close of business on February 22, 2010.

Additional Business Highlights

According to The NPD Group with respect to the U.S. market, Charttrack and Gfk, for the European market, during the year ended December 31, 2009:

Call of Duty: Modern Warfare 2 was the #1 best selling console title in the U.S. and Europe;

DJ Hero was the highest grossing new intellectual property launched in 2009 in the U.S. and Europe;

Call of Duty and Guitar Hero were two of the top-five best selling franchises across all platforms in the U.S. and Europe;

We are the #1 U.S. publisher overall for the PS3 and Xbox 360, and the #1 third-party publisher for the Wii; and

Call of Duty: Modern Warfare 2 and *World of Warcraft: Wrath of the Lich King* were two of the top five-best selling PC titles in dollars in the U.S. and Europe.

To date, *Call of Duty: Modern Warfare 2* has sold more than \$1 billion in retail sales worldwide, according to The NPD Group, Charttrack, and Gfk. Further, at December 31, 2009, there were approximately 11.5 million gamers worldwide subscribed to play *World of Warcraft*.

Table of Contents

Product Releases

Games released during the year ended December 31, 2009 included:

<i>Monsters vs. Aliens;</i>	<i>Guitar Hero 5;</i>
<i>Guitar Hero: Metallica;</i>	<i>Marvel Ultimate Alliance 2;</i>
<i>X-Men Origins: Wolverine;</i>	<i>Bakugan Battle Brawlers;</i>
<i>Guitar Hero: Modern Hits;</i>	<i>DJ Hero;</i>
<i>PROTOTYPE;</i>	<i>Band Hero;</i>
<i>Guitar Hero: Smash Hits;</i>	<i>Call of Duty: Modern Warfare 2;</i>
<i>Transformers: Revenge of the Fallen;</i>	<i>Tony Hawk: Ride;</i>
<i>Ice Age: Dawn of the Dinosaurs;</i>	<i>Guitar Hero: Van Halen;</i> and
<i>Wolfenstein;</i>	Three map packs for <i>Call of Duty: World at War.</i>

In 2010, we expect to continue to build on our success by releasing key franchise games including Blizzard's *StarCraft II: Wings of Liberty* and the World of Warcraft expansion pack, *Cataclysm*, as well as a diversified lineup of games based on Activision's best-selling franchises including Call of Duty, Guitar Hero, and Tony Hawk, together with other well-known titles such as True Crime, Spider-Man, and Bakugan, and a select number of new intellectual property franchises such as *Blur* and *Singularity*.

International Operations

International sales are a fundamental part of our business. Net revenues from international sales accounted for approximately 48%, 50%, and 53% of our total consolidated net revenues for the years ended December 31, 2009, 2008 and 2007, respectively. We maintain significant operations in the United States, Canada, the United Kingdom, Germany, France, Italy, Spain, Australia, Sweden, South Korea, Norway, Denmark, China, and the Netherlands. We believe that it is important to develop content locally that is specifically directed toward local cultures and customs to succeed internationally. Our international business is subject to risks typical of an international business, including, but not limited to, foreign currency exchange rate volatility. Accordingly, our future results could be materially and adversely affected by changes in foreign currency exchange rates.

Management's Overview of Business Trends

Online Content and Digital Downloads

We provide a variety of electronically delivered products. Many of our video games that are available through retailers as physical "boxed" products such as DVDs are also available by direct digital download through the Internet (from websites that we own and others owned by third parties to which we license our products). We also offer downloadable content and add-ons to our products (e.g., map packs and additional songs). Electronically delivered content is generally offered to consumers for a one-time fee. We continue to focus on and grow our digital download and online revenues and we believe that this will become an increasingly important part of our business over time.

Current Generation of Game Consoles

The current generation of game consoles began with Microsoft's launch of the Xbox 360 in 2005, and continued in 2006 when Sony and Nintendo launched their next-generation systems, the PS3 and the Wii, respectively. We have seen a significant decline in PS2 revenues during 2009 as compared to 2008, suggesting that this prior generation platform may soon be completely replaced by the current generation of consoles. Overall console sales remained strong in 2009, with an installed base of hardware in the U.S. and Europe of 218 million units as of December 31, 2009, representing an increase of 37% in units year over year. We will continue to monitor game console sales to manage our product delivery on each platform in a manner we believe to be most effective.

Table of Contents

Concentration of Top Titles

A significant portion of our revenues has historically been derived from video games based on a few popular franchises and these video games are responsible for a disproportionately high percentage of our profits. We expect that a limited number of popular franchises will continue to produce a disproportionately high percentage of our revenues and profits. For example, our top three franchises, Call of Duty, Guitar Hero, and World of Warcraft, accounted for approximately 68% of our net revenues for the year ended December 31, 2009. This is similar to the overall trend in the video game industry. For example, the top 10 titles accounted for 37% of the sales in the U.S. video game industry in the three months ended December 31, 2009, according to The NPD Group. In 2010, we expect to release key franchise games including Blizzard's *StarCraft II: Wings of Liberty* and the World of Warcraft expansion pack, *Cataclysm*, as well as a diversified lineup of games based on Activision Publishing's best-selling franchises including Call of Duty, Guitar Hero, and Tony Hawk, together with other well-known titles such as True Crime, Spider-Man, and Bakugan. Also in 2010, we expect to continue to explore new intellectual properties to broaden our franchise portfolio by releasing a select number of new intellectual properties, such as *Blur* and *Singularity*.

Seasonality

The interactive entertainment industry is highly seasonal. We have historically experienced our highest sales volume in the year-end holiday buying season, which occurs in the fourth quarter and lowest sales volume in the second quarter of our calendar year. We defer the recognition of a significant amount of net revenue related to our software titles containing online functionality that constitutes a more-than-inconsequential separate service deliverable over an extended period of time (i.e., typically six months to less than a year). As a result, the quarter in which we generate the highest sales volume may be different than the quarter in which we recognize the highest amount of net revenue. Our results can also vary based on a number of factors, including title release dates, consumer demand for our products, and shipment schedules.

Consolidated Statements of Operations Data

Note The historical financial statements prior to July 10, 2008 are those of Vivendi Games only. The financial information of the businesses operated by Activision, Inc. prior to the Business Combination is included from the date of the Business Combination (i.e. from July 10, 2008 onwards), but not for prior periods.

Edgar Filing: Activision Blizzard, Inc. - Form 10-K

Table of Contents

The following table sets forth certain consolidated statements of operations data for the periods indicated in dollars and as a percentage of total net revenues (amounts in millions):

	For the years ended December 31,					
	2009		2008		2007	
Net revenues:						
Product sales	\$ 3,080	72%	\$ 1,872	62%	\$ 457	34%
Subscription, licensing, and other revenues	1,199	28	1,154	38	892	66
Total net revenues	4,279	100	3,026	100	1,349	100
Costs and expenses:						
Cost of sales product costs	1,432	33	1,160	38	171	13
Cost of sales software royalties and amortization	348	8	267	9	52	4
Cost of sales intellectual property licenses	315	7	219	7	9	1
Cost of sales massively multi-player online role-playing game ("MMORPG")	212	5	193	7	204	15
Product development	627	15	592	20	397	29
Sales and marketing	544	13	464	15	172	13
General and administrative	395	9	271	9	166	12
Impairment of intangible assets	409	10				
Restructuring	23	1	93	3	(1)	
Total costs and expenses	4,305	101	3,259	108	1,170	87
Operating income (loss)	(26)	(1)	(233)	(8)	179	13
Investment and other income (loss), net	18	1	46	2	(4)	
Income (loss) before income tax benefit	(8)		(187)	(6)	175	13
Income tax benefit	(121)	(3)	(80)	(2)	(52)	(4)
Net income (loss)	\$ 113	3%	\$ (107)	(4)%	\$ 227	17%

Operating Segment Results

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

The CODM reviews segment performance exclusive of the impact of the change in deferred net revenues and related cost of sales with respect to certain of the Company's online-enabled games, stock-based compensation expense, restructuring expense, amortization of intangible assets and purchase price accounting related adjustments, impairment of intangible assets, integration and transaction costs, and other*. Information on the operating segments and reconciliations of total net revenues and total segment income (loss) from operations to consolidated net revenues and operating

Edgar Filing: Activision Blizzard, Inc. - Form 10-K

Table of Contents

income (loss) for the years ended December 31, 2009, 2008, and 2007 are presented below (amounts in millions):

	For the years ended December 31,			Increase/ (decrease)	Increase/ (decrease)
	2009	2008	2007	2009 v 2008	2008 v 2007
Segment net revenues:					
Activision	\$ 3,156	\$ 2,152	\$ 272	\$ 1,004	\$ 1,880
Blizzard	1,196	1,343	1,107	(147)	236
Distribution	423	227		196	227
Operating segment net revenue total	4,775	3,722	1,379	1,053	2,343
Reconciliation to consolidated net revenues:					
Net effect from deferred net revenues	(497)	(713)	(40)	216	(673)
Other*	1	17	10	(16)	7
Consolidated net revenues	\$ 4,279	\$ 3,026	\$ 1,349	\$ 1,253	\$ 1,677
Segment income (loss) from operations:					
Activision	\$ 663	\$ 307	\$ (13)	\$ 356	\$ 320
Blizzard	555	704	568	(149)	136
Distribution	16	22		(6)	22
Operating segment income from operations total	1,234	1,033	555	201	478
Reconciliation to consolidated operating income (loss):					
Net effect from deferral of net revenues and related cost of sales	(383)	(496)	(38)	113	(458)
Stock-based compensation expense	(154)	(90)	(137)	(64)	47
Restructuring	(23)	(93)	1	70	(94)
Amortization of intangible assets and purchase price accounting related adjustments	(259)	(292)	(4)	33	(288)
Impairment of intangible assets	(409)			(409)	
Integration and transaction costs	(24)	(29)		5	(29)
Other*	(8)	(266)	(198)	258	(68)
Total consolidated operating income (loss)	\$ (26)	\$ (233)	\$ 179	\$ 207	\$ (412)

(*)

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

Note The historical financial statements prior to July 10, 2008 are those of Vivendi Games only. The financial information of the businesses operated by Activision, Inc. prior to the Business Combination is included from the date of the Business Combination (i.e. from July 10, 2008 onwards), but not for prior periods. We provide a discussion and analysis of the operating segments for the years ended December 31, 2009, 2008, and 2007 in the Supplemental Pro Forma Information section below as the pro forma basis provides greater comparability for the Activision and Distribution segments as

Table of Contents

the Supplemental Pro Forma Information reflects pre-Business Combination businesses previously operated by Activision, Inc. The Blizzard segment is not affected by any of the pro forma adjustments.

For better understanding of the differences in presentation between our segment results and the consolidated results, the following explains the nature of each reconciling item.

Net Effect from Deferral of Net Revenues and Related Cost of Sales

We have determined that some of our games' online functionality represents an essential component of gameplay and as a result a more-than-inconsequential separate deliverable. As such, we are required to recognize the revenues of these game titles over the estimated service periods. The product life may range from a minimum of five months to a maximum of less than a year. The related cost of sales are deferred and recognized to match revenues. In the table above, we present the amount of net revenues and related cost of sales separately for each period as a result of the accounting treatment.

Stock-Based Compensation Expense

We expense our stock-based awards using the grant date fair value over the vesting periods of the stock awards. In the case of liability awards, the liability is subject to mark to market based on the current stock price. Included within stock-based compensation are the net effects of capitalization, deferral, and amortization. The stock-based compensation expenses for each period are presented above.

Restructuring

We have implemented an organizational restructuring plan as a result of the Business Combination. The restructuring activities include severance costs, facility exit costs and balance sheet write downs and exit costs from the cancellation of projects. We do not expect any material costs relating to this item going forward as we have completed our restructuring activities.

Amortization of Intangible Assets and Purchase Price Accounting Related Adjustments

All of our intangible assets are the result of the Business Combination and other acquisitions. We amortize the intangible assets over their estimated useful lives based on the pattern of their economic benefits consumption. The amount presented in the table represents the effect of the amortization of intangible assets as well as other purchase price accounting adjustments, where applicable, in our consolidated statements of operations.

Impairment of Intangible Assets

As a result of the accounting impairment test, we recorded a non-cash impairment charge on finite-lived intangible assets of \$409 million, or \$0.19 loss per share, for the year ended December 31, 2009 reflecting a weaker environment for the casual game and music genres.

Integration and Transaction Costs

These costs were incurred to effect the Business Combination and included activities such as merging systems and streamlining the business processes of the combined company of Activision Blizzard. We do not expect any further costs relating to this item going forward as we have completed our integration and transaction activities.

Edgar Filing: Activision Blizzard, Inc. - Form 10-K

Table of Contents

Segment Net Revenues

Activision

For the year ended December 31, 2009, net revenues from the Activision segment increased as compared to 2008 primarily due to the following:

As a result of the consummation of the Business Combination, net revenues of \$685 million from the Activision businesses operated by Activision, Inc. for the six months ended June 30, 2009 were included in 2009, but not in 2008;

Strong performance from new intellectual property launches of *DJ Hero* and *PROTOTYPE* in 2009; and

Exceptional performance from *Call of Duty: Modern Warfare 2*.

These were partially offset by stronger performance of the Guitar Hero franchise in 2008 versus 2009.

For the year ended December 31, 2008, net revenues from the Activision segment increased as compared to 2007 primarily due to the consummation of the Business Combination, which resulted in revenues from Activision, Inc. of approximately \$1,988 million being included from the date of the Business Combination, but not in 2007.

Blizzard

Blizzard's net revenues decreased for the year ended December 31, 2009 as compared to 2008 primarily due to no new releases in 2009 and an interruption of licensing royalties for *World of Warcraft* in China from June 2009 to September 2009 as a result of a license transfer. This compared to 2008 with the successful November 2008 release of the second expansion pack of *World of Warcraft: Wrath of the Lich King*. This decrease was partially offset by an increase in other value added service revenues.

Blizzard's net revenues increased for the year ended December 31, 2008 as compared to 2007 primarily due to the release of the second expansion pack of *World of Warcraft: Wrath of the Lich King* in November 2008 and an increase in the number of *World of Warcraft* subscribers.

Distribution

The increase in Distribution net revenues for the year ended December 31, 2009 as compared to 2008 was primarily due to the consummation of Business Combination in which net revenues of \$148 million from the Distribution businesses operated by Activision, Inc. for the six months ended June 30, 2009 were included in the year ended December 31, 2009, but not in 2008.

The increase in Distribution net revenues for the year ended December 31, 2008 as compared to 2007 is due to the consummation of the Business Combination, which resulted in revenues from Activision, Inc. of \$227 million relating to Distribution segment being included from the date of the Business Combination but not in 2007.

Segment Income (Loss) from Operations Highlights

Activision

For the year ended December 31, 2009, operating income from the Activision segment increased as compared to 2008 primarily due to the following:

The increase in net revenues from Activision as noted above; and

Table of Contents

Lower operating expenses stemming from continuing effective cost containment strategies.

For the year ended December 31, 2008, operating income from the Activision segment increased as compared to 2007 primarily due to the consummation of the Business Combination, which resulted in operating income from Activision, Inc. of approximately \$371 million being included from the date of the Business Combination, but not in 2007.

Blizzard

For the year ended December 31, 2009, operating income from the Blizzard segment decreased as compared to 2008 primarily as a result of the following:

The decrease in net revenues noted above; and

Incremental investments made by Blizzard for customer service and for product development for the sequel to StarCraft, the next World of Warcraft expansion pack, and for enhancing Battle.net.

For the year ended December 31, 2008, operating income from the Blizzard segment increased as compared to 2007 mainly as a result of the successful release of the second expansion pack of *World of Warcraft: Wrath of the Lich King* in November 2008.

Supplemental Pro Forma Operating Segment Results

The consummation of the Business Combination has resulted in the businesses operated by Activision, Inc. prior to the Business Combination being included from the date of the Business Combination (i.e. from July 9, 2008 onwards), but not for prior periods. Therefore, for comparability purposes, we combined Activision, Inc.'s financial information with Activision Blizzard's reported financial information in the following table to create pro forma Activision Blizzard financial information for the years ended December 31, 2008 and 2007. This pro forma information is for informational purposes only and does not reflect any operating efficiencies or inefficiencies which may have resulted from the Business Combination and therefore is not necessarily indicative of results that would have been achieved had the business been combined during the years presented. We have included a reconciliation between the reported consolidated and segment financial information to the

Edgar Filing: Activision Blizzard, Inc. - Form 10-K

Table of Contents

pro forma consolidated and segment financial information. See Note 14 of the Notes to Consolidated Financial Statements for further details of our segment presentation.

	For the years ended December 31,						
	2009	2008	2007	Increase/ (decrease) 2009 v 2008	Increase/ (decrease) 2008 v 2007	% change 2009 v 2008	% change 2008 v 2007
Pro forma segment net revenues:							
Activision	\$ 3,156	\$ 3,279	\$ 2,472	\$ (123)	\$ 807	(4)%	33%
Blizzard	1,196	1,343	1,107	(147)	236	(11)	21
Distribution	423	410	408	13	2	3	
Pro forma operating segment net revenue total	4,775	5,032	3,987	(257)	1,045	(5)	26
Reconciliation to pro forma consolidated net revenues:							
Net effect from deferral of net revenues	(497)	(713)	(40)	216	(673)	30	NM
Other*	1	17	10	(16)	7	(94)	70
Pro forma consolidated net revenues	\$ 4,279	\$ 4,336	\$ 3,957	\$ (57)	\$ 379	(1)%	10%
Pro forma segment income (loss) from operations:							
Activision	\$ 663	\$ 469	\$ 411	\$ 194	\$ 58	41%	14%
Blizzard	555	704	568	(149)	136	(21)	24
Distribution	16	27	15	(11)	12	(41)	80
Pro forma operating segment income from operations total	1,234	1,200	994	34	206	3	21
Reconciliation to pro forma consolidated operating income (loss):							
Net effect from deferral of net revenues and related cost of sales	(383)	(496)	(38)	113	(458)	23	NM
Stock-based compensation expense	(154)	(181)	(225)	27	44	15	20
Restructuring	(23)	(93)	1	70	(94)	75	NM
Amortization of intangible assets and purchase price accounting related adjustments	(259)	(376)	(380)	117	4	31	1
Impairment of intangible assets	(409)			(409)			
Integration and transaction costs	(24)	(42)	4	18	(46)	43	NM
Other*	(8)	(266)	(198)	258	(68)	97	(34)
Total pro forma consolidated operating income (loss)	\$ (26)	\$ (254)	\$ 158	\$ 228	\$ (412)	90%	(261)%

(*)

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

Edgar Filing: Activision Blizzard, Inc. - Form 10-K

Table of Contents

reclassified our prior periods' segment presentation so that it conforms to the current period's presentation.

On a pro forma operating segment basis, our operating margin for the years ended December 31, 2009, 2008 and 2007 was 26%, 24% and 25%, respectively. Highlights and analysis of our individual segment net revenues and income from operations are as follows:

Pro forma Activision Segment Net Revenues

Activision's net revenues decreased for the year ended December 31, 2009 as compared to 2008 primarily due to:

The prolonged weakness in the economy adversely impacting the casual game and music genres and the stronger performance of the Guitar Hero franchise in 2008 as compared to 2009; and

The decline in sales of PS2 platform titles due to the aging lifecycle of the PS2 platform as consumers transition to current generation platforms.

Partially offsetting this decrease was an increase in net revenues from the exceptional performance of *Call of Duty: Modern Warfare 2* in November 2009 and growth in online digital revenues from downloadable content.

Activision's net revenues increased for the year ended December 31, 2008 as compared to 2007 primarily as a result of:

Stronger performance of games related to the Guitar Hero franchise;

Higher price points for the Guitar Hero franchise's hardware bundles, which consisted of drums, guitars and/or microphones, as compared to our software-only products; and

Growth in the Nintendo Wii platform installed base positively impacting Wii software titles.

Pro Forma Activision Segment Income from Operations

Activision's operating income increased for the year ended December 31, 2009 as compared to 2008 primarily due to:

Exceptional performance of *Call of Duty: Modern Warfare 2*, which was released in November 2009;

Strong performance from new intellectual property launches of *DJ Hero* and *PROTOTYPE* in 2009;

Growth in the higher margin online digital revenues; and

Lower operating expenses stemming from continuing effective cost containment strategies.

These factors were partially offset by the decrease in net revenues described above.

The increase in Activision segment operating income for the year ended December 31, 2008 as compared to 2007 was mainly attributable to:

The increase in net revenues discussed above;

Partially offset by:

The higher cost of sales related to the manufacturing and distribution cost of the Guitar Hero hardware bundle; and

The unfavorable impact of changes in foreign exchange rates, as the U.S. dollar strengthened primarily in relation to the British pound, euro and Australian dollar.

Edgar Filing: Activision Blizzard, Inc. - Form 10-K

Table of Contents

Schedules of Reconciliation of Reported Consolidated and Segment Financial Information to Pro Forma Consolidated and Segment Financial Information for the Years Ended December 31, 2008 and 2007

For the year ended December 31, 2008, the pro forma consolidated financial information below is comprised of Activision, Inc.'s financial information for the period January 1, 2008 to July 9, 2008 together with Activision Blizzard's reported financial information for the year ended December 31, 2008. Activision, Inc.'s financial information for the three months ended March 31, 2008 and June 30, 2008 are extracted from the quarterly information which has not been audited. Activision, Inc.'s financial information from July 1, 2008 to July 9, 2008 has not been audited. In conjunction with the Business Combination, senior management changed the manner in which they assess the operating performance of, and allocate resources to, our operating segments during the year ended December 31, 2008.

	For the year ended December 31, 2008			
	Reported	Activision, Inc.	Pro forma adjustments(i)	Pro forma Activision Blizzard
Consolidated net revenues	\$ 3,026	\$ 1,310	\$	\$ 4,336
Reconciliation to segment net revenues:				
Net effect from deferral of net revenues	713			713
Other(ii)	(17)			(17)
Total segment net revenues	\$ 3,722	\$ 1,310	\$	\$ 5,032
Segment net revenues				
Activision	\$ 2,152	\$ 1,127	\$	\$ 3,279
Blizzard	1,343			1,343
Distribution	227	183		410
Total segment net revenues	\$ 3,722	\$ 1,310	\$	\$ 5,032
Consolidated operating income (loss)	\$ (233)	\$ 85	\$ (106)	\$ (254)
Reconciliation to segment operating income (loss):				
Net effect from deferral of net revenues and related cost of sales	496			496
Stock-based compensation expense	90	32	59	181
Restructuring	93			93
Amortization of intangible assets and purchase price accounting related adjustments	292		84	376
Integration and transaction costs	29	50	(37)	42
Other(ii)	266			266
Total segment operating income (loss) from operations	\$ 1,033	\$ 167	\$	\$ 1,200
Segment income from operations				
Activision	\$ 307	\$ 162	\$	\$ 469
Blizzard	704			704
Distribution	22	5		27
Total segment income from operations	\$ 1,033	\$ 167	\$	\$ 1,200
Consolidated net income (loss)	\$ (107)	\$ 60	\$ (64)	\$ (111)

Edgar Filing: Activision Blizzard, Inc. - Form 10-K

Table of Contents

For the year ended December 31, 2007, the pro forma Activision Blizzard financial information is comprised of Activision, Inc.'s financial information for each quarter of calendar year 2007 together with Activision Blizzard's reported financial information for the year ended December 31, 2007. We extracted the financial information of each quarter of calendar year 2007 from Activision, Inc.'s quarterly information which has not been audited.

	For the year ended December 31, 2007			
	Reported	Activision, Inc.	Pro forma adjustments(i)	Pro forma Activision Blizzard
Consolidated net revenues	\$ 1,349	\$ 2,608	\$	\$ 3,957
Reconciliation to segment net revenues:				
Net effect from deferral of net revenues	40			40
Other(ii)	(10)			(10)
Total segment net revenues	\$ 1,379	\$ 2,608	\$	\$ 3,987
Segment net revenues				
Activision	\$ 272	\$ 2,200	\$	\$ 2,472
Blizzard	1,107			1,107
Distribution		408		408
Total segment net revenues	\$ 1,379	\$ 2,608	\$	\$ 3,987
Consolidated operating income (loss)	\$ 179	\$ 396	\$ (417)	\$ 158
Reconciliation to segment operating income (loss):				
Net effect from deferral of net revenues and related cost of sales	38			38
Stock-based compensation expense	137	43	45	225
Restructuring	(1)			(1)
Amortization of intangible assets and purchase price accounting related adjustments	4		376	380
Integration and transaction costs			(4)	(4)
Other(ii)	198			198
Total segment income from operations	\$ 555	\$ 439	\$	\$ 994
Segment income (loss) from operations				
Activision	\$ (13)	\$ 424	\$	\$ 411
Blizzard	568			568
Distribution		15		15
Total segment income from operations	\$ 555	\$ 439	\$	\$ 994
Consolidated net income	\$ 227	\$ 286	\$ (253)	\$ 260

(i)

The pro forma adjustments include the increased amortization expense resulting from the application of the purchase method of accounting (\$84 million and \$376 million for the years ended December 31, 2008 and 2007, respectively), elimination of Activision, Inc.'s historical transaction costs (\$37 million and \$4 million for the years ended December 31, 2008 and 2007, respectively), and an increase in stock-based compensation expense associated with the increase in the fair value of Activision, Inc.'s unvested stock awards at the closing date of the Business Combination (\$59 million and \$45 million for the years ended December 31, 2008 and 2007,

Edgar Filing: Activision Blizzard, Inc. - Form 10-K

Table of Contents

respectively). Pro forma adjustments are shown net of tax using an assumed combined federal and state statutory tax rate of 39.4%.

(ii)

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

Results of Operations Years Ended December 31, 2009, 2008, and 2007

Net Revenues by Geographic Area

The following table details our consolidated net revenues by geographic area for the years ended December 31, 2009, 2008, and 2007 (amounts in millions):

	For the years ended December 31,			Increase/ (decrease)	Increase/ (decrease)
	2009	2008	2007	2009 v 2008	2008 v 2007
Geographic area net revenues:					
North America	\$ 2,217	\$ 1,494	\$ 620	\$ 723	\$ 874
Europe	1,798	1,288	555	510	733
Asia Pacific	263	227	164	36	63
Total geographic area net revenues	4,278	3,009	1,339	1,269	1,670
Other	1	17	10	(16)	7
Consolidated net revenues	\$ 4,279	\$ 3,026	\$ 1,349	\$ 1,253	\$ 1,677

Consolidated net revenues increased in all regions for the year ended December 31, 2009 as compared to 2008 primarily due to the post-Business Combination net revenues consisting of \$690 million in North America, \$507 million in Europe and \$54 million in Asia Pacific from the businesses previously operated by Activision, Inc. for the six month period ended June 30, 2009 that were included in 2009 but not in 2008. The increase in North America, which was further driven by the strong performance of the Call of Duty franchise, in particular the 2009 release of *Call of Duty: Modern Warfare 2*. The increase was partially offset by the impact of the weaker casual games and music genre in 2009.

Geographically, consolidated net revenues increased in all regions for the year ended December 31, 2008 as compared to 2007 as a result of the following:

The consummation of the Business Combination, which resulted in consolidated net revenues from Activision, Inc. of approximately \$1,648 million, of which \$227 million relates to our Distribution segment, being included from the date of the Business Combination, but not in 2007;

Activision had two of the top-five best-selling franchises across all platforms Guitar Hero and Call of Duty in North America and Europe for the quarter ending December 31, 2008 according to The NPD Group, Gfk, and Charttrack;

Activision's successful releases in 2008, including *Call of Duty: World at War*, *Guitar Hero World Tour*, *Guitar Hero: Aerosmith*, and *Guitar Hero: On Tour*;

Edgar Filing: Activision Blizzard, Inc. - Form 10-K

Table of Contents

Back catalog sales of *Guitar Hero III: Legends of Rock*, and *Call of Duty: Modern Warfare*;

The release of the second expansion pack of *World of Warcraft: Wrath of the Lich King* in November 2008;

Activision's release of an affiliated LucasArts' title, *Star Wars: The Force Unleashed* in Europe and Asia Pacific; and

An increase in the number of *World of Warcraft* subscribers.

Foreign Exchange Impact

We estimate that changes in foreign exchange rates had a negative impact of approximately \$71 million and \$112 million on Activision Blizzard's net revenues for the years ended December 31, 2009 and 2008, respectively, as compared to 2008 and 2007, respectively, as the U.S. dollar strengthened primarily in relation to the British pound, euro, Australian dollar, Korean won, and Swedish krona.

Net Revenues by Platform

The following table details our net revenues by platform and as a percentage of total consolidated net revenues for the years ended December 31, 2009, 2008, and 2007 (amounts in millions):

	Year ended December 31, 2009	% of total consolidated net revs.	Year ended December 31, 2008	% of total consolidated net revs.	Year ended December 31, 2007	% of total consolidated net revs.	Increase/ (decrease) 2009 v 2008	Increase/ (decrease) 2008 v 2007
Platform net revenues:								
MMORPG	\$ 1,248	29%	\$ 1,152	38%	\$ 1,024	76%	\$ 96	\$ 128
PC	164	4	99	3	94	7	65	5
Console:								
Sony PlayStation 3	584	14	241	8	22	2	343	219
Sony PlayStation 2	174	4	284	9	71	5	(110)	213
Microsoft Xbox 360	857	19	362	12	38	3	495	324
Nintendo Wii	584	14	407	14	25	2	177	382
Total console	2,199	51	1,294	43	156	12	905	1,138
Handheld	244	6	237	8	65	4	7	172
Total platform net revenues:	3,855	90	2,782	92	1,339	99	1,073	1,443
Distribution	423	10	227	7			196	227
Other	1		17	1	10	1	(16)	7
Total consolidated net revenues	\$ 4,279	100%	\$ 3,026	100%	\$ 1,349	100%	\$ 1,253	\$ 1,677

MMORPG net revenues increased for the years ended December 31, 2009 and 2008 as compared to 2008 and 2007 as a result of the continued growth of the *World of Warcraft* franchise and online value added services.

Net revenues from various consoles and hand-held platforms increased, except for PS2, for the year ended December 31, 2009 as compared to 2008 primarily as a result of the consummation of the Business Combination. The increases in net revenues by platform for the year ended December 31, 2009 was also driven by the success of our Call of Duty franchise, in particular, *Call of Duty: Modern Warfare 2*, in the Xbox360

and PS3 platforms. Partially offsetting the increase was the weaker sales of games in the casual games and music genre such as titles from our Guitar Hero franchise and our "value" Wii titles as compared to the core gamer genre, which includes titles from the Call of Duty

Edgar Filing: Activision Blizzard, Inc. - Form 10-K

Table of Contents

franchise. This was due to extended economic weakness and competition from emerging platforms, such as the iPhone and other community internet applications that accommodate game play. PS2 platform revenues declined due to the aging lifecycle of the PS2 platform as consumers transition to the current generation platforms.

Net revenues across all platforms increased for the year ended December 31, 2008, as compared to 2007 due to the following:

The consummation of the Business Combination resulted in consolidated net revenues from Activision, Inc. of approximately \$1,648 million, of which \$227 million relates to Distribution segment, being included from the date of the Business Combination, but not for prior periods; and

A growing installed base for the current generation hardware platforms (in particular, the Wii, PS3, and Xbox 360) and increased number of titles and skus available from Activision as compared to the titles and skus released by Vivendi Games.

Costs and Expenses

Cost of Sales

The following table details the components of cost of sales in dollars and as a percentage of total consolidated net revenues for the years ended December 31, 2009, 2008, and 2007 (amounts in millions):

	Year ended December 31, 2009	% of total consolidated net revs.	Year ended December 31, 2008	% of total consolidated net revs.	Year ended December 31, 2007	% of total consolidated net revs.	Increase/ (decrease) 2009 v 2008	Increase/ (decrease) 2008 v 2007
Product costs	\$ 1,432	33%	\$ 1,160	38%	\$ 171	13%	\$ 272	\$ 989
Software royalties and amortization	348	8	267	9	52	4	81	215
Intellectual property licenses	315	7	219	7	9	1	96	210
MMORPG	212	5	193	7	204	15	19	(11)

For the year ended December 31, 2009, cost of sales increased as compared to 2008 primarily due to:

Post-Business Combination product costs of \$530 million, software royalties and amortization of \$151 million, and intellectual property licenses of \$112 million from businesses previously operated by Activision, Inc., for the six month period ended June 30, 2009 were included in 2009, but not in 2008; and

Incremental investments made by Blizzard for customer service.

These factors were partially offset by a change in business mix with lower cost of sales resulting from our shift to selling more software versus hardware, and selling more of our owned franchise and titles versus affiliated titles.

For the year ended December 31, 2008, cost of sales increased as compared to 2007 primarily due to:

The consummation of the Business Combination, which resulted in cost of sales from Activision, Inc. of approximately \$1,416 million being included from the date of the Business Combination, but not in 2007;

Edgar Filing: Activision Blizzard, Inc. - Form 10-K

Table of Contents

The price of oil increased sharply before production of the hardware peripherals for Guitar Hero. This resulted in higher raw material and logistic costs for the production of *Guitar Hero: World Tour* band bundle products consisting of a package of guitar, drum, microphone, and software;

Write-down of our remaining inventory of Gibson guitars resulting from the expiration of our licensing agreement on January 31, 2009;

Amortization of intangible assets and other purchase price accounting related adjustments of \$15 million, \$95 million, and \$140 million included in cost of sales product costs, cost of sales software royalties and amortization, and cost of sales intellectual property licenses, respectively;

Higher product costs due to an increase in business mix from affiliated LucasArts title *Star Wars: The Force Unleashed* in Europe and Asia Pacific in the fourth quarter of 2008 and the catalog title, *Lego: Indiana Jones the Original Adventures*;

Higher royalties expenses for released titles during the year ended December 31, 2008, such as *The Bourne Conspiracy* and *James Bond: Quantum of Solace*; and

Pre-release impairments on certain titles of \$18 million for the year ended December 31, 2008.

Product Development (amounts in millions)

	Year ended December 31, 2009	% of consolidated net revenues	Year ended December 31, 2008	% of consolidated net revenues	Year ended December 31, 2007	% of consolidated net revenues	Increase/ (decrease) 2009 v 2008	Increase/ (decrease) 2008 v 2007
Product development	\$ 627	15%	\$ 592	20%	\$ 397	29%	\$ 35	\$ 195

For the year ended December 31, 2009, product development costs increased as compared to 2008 primarily due to post-Business Combination product development costs of \$143 million from businesses previously operated by Activision, Inc., for the six month period ended June 30, 2009 were included in 2009, but not in 2008. The increase in product development expense was partially offset by the complete wind down of Non-Core operations resulting in lower product development expense from Non-Core operations for the year ended December 31, 2009 as compared to 2008, such as the write off capitalized software development costs of canceled titles in the amount of \$71 million in 2008 from our rationalization of our title portfolio.

For the year ended December 31, 2008, product development costs increased as compared to 2007 primarily due to the following:

The consummation of the Business Combination, which resulted in product development expenses from Activision, Inc. of approximately \$187 million being included from the date of the Business Combination, but not in 2007;

Included in the Non-Core exit operations, a write-off of capitalized software development costs of canceled titles in the amount of \$71 million in 2008, as a result of the rationalization of our title portfolio; and

Increased product development investment costs for our slate of future titles.

Edgar Filing: Activision Blizzard, Inc. - Form 10-K

Table of Contents

Sales and Marketing (amounts in millions)

	Year ended December 31, 2009	% of total consolidated net revs.	Year ended December 31, 2008	% of total consolidated net revs.	Year ended December 31, 2007	% of total consolidated net revs.	Increase/ (decrease) 2009 v 2008	Increase/ (decrease) 2008 v 2007
Sales and marketing	\$ 544	13%	\$ 464	15%	\$ 172	13%	\$ 80	\$ 292

For year ended December 31, 2009, sales and marketing expense increased as compared to 2008 primarily due to post-Business Combination sales and marketing expenses of \$147 million from businesses previously operated by Activision, Inc., for the six month period ended June 30, 2009 were included in 2009, but not in 2008. This increase was partially offset by a decrease primarily due to the amortization of intangible assets of \$40 million related to retail customer relationships for the year ended December 31, 2008 and the complete wind down of Non-Core operations.

For the year ended December 31, 2008, sales and marketing expenses increased as compared to 2007 primarily due to:

The consummation of the Business Combination, which resulted in sales and marketing expenses from Activision, Inc. of approximately \$282 million being included from the date of the Business Combination, but not in 2007; and

Increased number of titles and skus published by Activision Blizzard as compared to Vivendi Games.

General and Administrative (amounts in millions)

	Year ended December 31, 2009	% of total consolidated net revs.	Year ended December 31, 2008	% of total consolidated net revs.	Year ended December 31, 2007	% of total consolidated net revs.	Increase/ (decrease) 2009 v 2008	Increase/ (decrease) 2008 v 2007
General and administrative	\$ 395	9%	\$ 271	9%	\$ 166	12%	\$ 124	\$ 105

For year ended December 31, 2009, general and administrative expense increased as compared to 2008 primarily due to:

Post-Business Combination general and administrative expenses of \$114 million from businesses previously operated by Activision, Inc., for the six month period ended June 30, 2009 were included in 2009, but not in 2008;

Increases in stock-based compensation expense; and

Foreign exchange losses from revaluation of our transaction exposures.

These factors were partially offset by the cost containment strategy we implemented and synergies resulting from our restructuring efforts from the Business Combination including the complete wind down of our Non-Core operations.

For the year ended December 31, 2008, general and administrative costs increased in absolute amount and decreased as percentage of consolidated net revenues as compared to 2007. The increase was primarily due to the consummation of the Business Combination, which resulted in general and administrative expenses from Activision, Inc. of approximately \$125 million, (including integration and transaction expenses of \$29 million) being included from the date of the Business Combination, but not in 2007. The increase was partially offset by reduced salary and benefit costs as a result of the implementation of our organizational restructuring.

Table of Contents

Impairment of Intangible Assets (amounts in millions)

	Year ended December 31, 2009	% of total consolidated net revs.	Year ended December 31, 2008	% of total consolidated net revs.	Year ended December 31, 2007	% of total consolidated net revs.	Increase/ (decrease) 2009 v 2008	Increase/ (decrease) 2008 v 2007
Impairment of intangible assets	\$ 409	10%	\$	%	\$	%	\$ 409	\$

In the fourth quarter of 2009, with the franchise and industry results of the holiday season, our outlook for the console platforms was significantly revised. With the continued economic downturn within our industry in 2009 and the change in the buying habits of casual consumers, we reassessed our overall expectations. We considered these economic changes during our 2010 planning process conducted during the months of November and December, which resulted in a strategy change to focus on fewer title releases in the casual and music genres. As a result, we updated our future projected revenue streams for the franchises in the casual games and music genres. We performed recoverability and, where applicable, impairment tests on the related intangible assets in accordance with ASC Subtopic 360-10. Based on the analysis performed, we recorded impairment charges of \$24 million, \$12 million and \$373 million to license agreements, game engines and internally developed franchises intangible assets, respectively for the year ended December 31, 2009 within our Activision segment. See Note 12 of the Notes to Consolidated Financial Statements included in Item 8 of this Annual Report on Form 10-K for additional information regarding the determination of the impairment charges recorded for the year ended December 31, 2009.

Restructuring (amounts in millions)

	Year ended December 31, 2009	% of total consolidated net revs.	Year ended December 31, 2008	% of total consolidated net revs.	Year ended December 31, 2007	% of total consolidated net revs.	Increase/ (decrease) 2009 v 2008	Increase/ (decrease) 2008 v 2007
Restructuring	\$ 23	1%	\$ 93	3%	\$ (1)	%	(\$ 70)	\$ 94

In the third quarter of 2008, we implemented an organizational restructuring as a result of the Business Combination. This organizational restructuring was to integrate different operations and to streamline the combined Activision Blizzard organization. The implementation of the organizational restructuring resulted in the following restructuring charges: severance costs; contract termination costs; fixed asset write-off on disposals; impairment charges on acquired trade names, prepaid royalties, intellectual property licenses; impairment charges on goodwill; and loss on disposal of assets/liabilities. At June 30, 2009, we had completed the majority of our organizational restructuring activities as a result of the Business Combination. See Note 8 of the Notes to Consolidated Financial Statements included in Item 8 of this Annual Report on Form 10-K for more detail and a rollforward of the restructuring liability that includes the beginning and ending liability, costs incurred, cash payments and non cash write downs.

Investment and Other Income (Loss), Net (amounts in millions)

	Year ended December 31, 2009	% of total consolidated net revs.	Year ended December 31, 2008	% of total consolidated net revs.	Year ended December 31, 2007	% of total consolidated net revs.	Increase/ (decrease) 2009 v 2008	Increase/ (decrease) 2008 v 2007
Investment and other income (loss), net	\$ 18	1%	\$ 46	2%	\$ (4)	%	(\$ 28)	\$ 50

Investment and other income (loss), net decreased for the year ended December 31, 2009 as compared to 2008 primarily as a result of lower interest rates, losses on foreign exchange derivative contracts in 2009 as compared with gains in 2008, and certain investment-related gains in 2008. Partially

Edgar Filing: Activision Blizzard, Inc. - Form 10-K

Table of Contents

offsetting these decreases was an \$8 million increase due to the reduction in fair value of our other financial liability for the year ended December 31, 2009.

Our cash, cash equivalents, and short-term investments, comprised primarily of cash and cash equivalents, was \$3.2 billion and \$3 billion at December 31, 2009 and 2008, respectively. Vivendi Games maintained a net payable balance with Vivendi at December 31, 2007. Investment income for the year ended December 31, 2008 was primarily derived from the interest income from investments in money market funds, mark-to-market gains on our outstanding currency forward contracts, and an unrealized gain on auction rate securities rights from UBS AG ("UBS"), compared with net interest expense for the year ended December 31, 2007.

Income Tax Benefit (amounts in millions)

	Year ended December 31, 2009	% of Pretax income	Year ended December 31, 2008	% of Pretax income	Year ended December 31, 2007	% of Pretax income	Increase/ (decrease) 2009 v 2008	Increase/ (decrease) 2008 v 2007
Income Tax Benefit	\$ (121)	NM	\$ (80)	(43)%	\$ (52)	(30)%	\$ 41	\$ 28

For the year ended December 31, 2009, the loss from the impairment of intangible assets resulted in a book tax benefit at the U.S. statutory rate, while foreign income taxes at lower rates, the release of valuation allowances on net operating losses, the recognition of research and development credits and IRC 199 domestic production deductions provided additional benefit on both a book and taxable income basis. These collective factors resulted in an aggregated book tax benefit of \$121 million for calendar year 2009. For the years ended December 31, 2008 and 2007, the tax benefit as a result of net income (loss) before income taxes was offset by tax benefits from net operating losses surrendered and the release of valuation allowances.

Liquidity and Capital Resources

Sources of Liquidity (amounts in millions)

	For the years ended December 31,		
	2009	2008	Increase/ (decrease) 2009 v 2008
Cash and cash equivalents	\$ 2,768	\$ 2,958	\$ (190)
Short-term investments	477	44	433
	\$ 3,245	\$ 3,002	\$ 243

Percentage of total assets 24% 21%

	For the years ended December 31,				
	2009	2008	2007	Increase/ (decrease) 2009 v 2008	Increase/ (decrease) 2008 v 2007
Cash flows provided by operating activities	\$ 1,183	\$ 379	\$ 431	\$ 804	\$ (52)
Cash flows provided by (used in) investing activities	(443)	1,101	(68)	(1,544)	1,169
Cash flows provided by (used in) financing activities	(949)	1,488	(371)	(2,437)	1,859
Effect of foreign exchange rate changes	19	(72)	2	91	(74)
Net increase (decrease) in cash and cash equivalents	\$ (190)	\$ 2,896	\$ (6)	\$ (3,086)	\$ 2,902

For the year ended December 31, 2009, the primary drivers of cash flows provided by operating activities included the collection of customer receivables generated by the sale of our products and our subscription revenues, partially offset by payments to vendors for the manufacture, distribution and

Table of Contents

marketing of our products, payments to third-party developers and intellectual property holders, tax liability, and payments to our workforce. Cash flows used in investing activities reflect that we purchased short-term investments totaling \$425 million, made capital expenditures of \$69 million primarily for property and equipment, and received \$44 million upon the maturity of investments, the majority of which largely consisted of our U.S. government agency securities during the year ended December 31, 2009. Cash flows used in financing activities primarily reflect our repurchase of 101 million shares of our common stock for \$1.1 billion under the stock repurchase program, partially offset by \$81 million of proceeds from issuance of shares of common stock to employees pursuant to stock option exercises.

In addition to cash flows provided by operating activities, our primary source of liquidity was \$3.2 billion of cash and cash equivalents and short-term investments at December 31, 2009. With our cash and cash equivalents and expected cash flows provided by operating activities, we believe that we have sufficient liquidity to meet daily operations in the foreseeable future. We also believe that we have sufficient working capital (approximately \$2.8 billion at December 31, 2009), as well as availability under our credit facilities, to finance our operational requirements for at least the next twelve months, including purchases of inventory and equipment, the funding of the development, production, marketing and sale of new products, to finance the acquisition of intellectual property rights for future products from third parties, to fund a new stock repurchase program, and to pay dividends to our shareholders.

On April 29, 2008, Activision, Inc. entered into a senior unsecured credit agreement with Vivendi (as lender). Borrowings under the agreement became available upon consummation of the Business Combination. At December 31, 2009, the credit agreement provides for a revolving credit facility of up to \$475 million, bearing interest at LIBOR plus 1.20% per annum. Any unused amount under the revolving credit facility is subject to a commitment fee of 0.42% per annum. No borrowings were outstanding at December 31, 2009.

On November 5, 2008, we announced that our Board of Directors authorized a stock repurchase program under which we may repurchase up to \$1 billion worth of our common stock. On July 31, 2009, our Board of Directors authorized an increase of \$250 million to the stock repurchase program bringing the total authorization to \$1.25 billion.

Through December 31, 2009, we repurchased 114 million shares of our common stock for \$1,235 million under the program. In addition, we had agreed to repurchase 1.3 million shares of our common stock at an average price per share of \$11.32 for a value of \$15 million that had not yet settled at December 31, 2009. This completed our initial \$1.25 billion stock repurchase program.

On February 10, 2010, we announced that our Board of Directors authorized a new stock repurchase program under which we may repurchase up to \$1 billion of our common stock on terms and conditions to be determined by the Company until the earlier of December 31, 2010 or a determination by the Board of Directors to discontinue the repurchase program.

Additionally, on February 10, 2010, Activision Blizzard's Board of Directors declared a cash dividend of \$0.15 per common share payable on April 2, 2010 to shareholders of record at the close of business on February 22, 2010.

Cash Flows from Operating Activities

The primary drivers of cash flows from operating activities have typically included the collection of customer receivables generated by the sale of our products and our subscription revenues, offset by payments for taxes and to vendors for the manufacture, distribution and marketing of our products, third-party developers and intellectual property holders, and to our workforce. A significant operating use of our cash relates to our continued investment in software development and intellectual property

Table of Contents

licenses. We expect that we will continue to make significant expenditures relating to our investment in software development and intellectual property licenses.

Cash Flows from Investing Activities

The primary drivers of cash flows used in investing activities have typically included capital expenditures, acquisitions and the net effect of purchases and sales/maturities of short-term investments.

Cash Flows from Financing Activities

The primary drivers of cash flows provided by financing activities have historically related to transactions involving our common stock, including the issuance of our common stock to employees and the public and the purchase of treasury shares. We have not utilized debt financing as a source of cash flows. However, if needed, we may access and utilize the credit facilities that are described in "Credit Facilities" in Note 18 of the Notes to Consolidated Financial Statements included in Item 8 of this Annual Report on Form 10-K.

For the year ended December 31, 2009, cash flows used in financing activities included \$1.1 billion used to purchase Activision Blizzard stock under the stock repurchase program described above.

Capital Requirements

For the year ending December 31, 2010, we anticipate total capital expenditures of approximately \$145 million. Capital expenditures will be primarily for computer hardware and software purchases and various corporate projects.

Commitments

In the normal course of business, we enter into contractual arrangements with third-parties for non-cancelable operating lease agreements for our offices, for the development of products, and for the rights to intellectual property ("IP"). Under these agreements, we commit to provide specified payments to a lessor, developer or intellectual property holder, as the case may be, based upon contractual arrangements. The payments to third-party developers are generally conditioned upon the achievement by the developers of contractually specified development milestones. Further, these payments to third-party developers and intellectual property holders typically are deemed to be advances and are recoupable against future royalties earned by the developer or intellectual property holder based on the sale of the related game. Additionally, in connection with certain intellectual property rights acquisitions and development agreements, we commit to spend specified amounts for marketing support for the related game(s) which is to be developed or in which the intellectual property will be utilized. Assuming all contractual provisions are met, the total future minimum

Table of Contents

commitments for these and other contractual arrangements in place at December 31, 2009 are scheduled to be paid as follows (amounts in millions):

	Contractual Obligations(1)			
	Facility and equipment leases	Developer and IP	Marketing	Total
For the year ending December 31,				
2010	\$ 37	\$ 113	\$ 27	\$ 177
2011	25	41	25	91
2012	21	18	13	52
2013	18	22		40
2014	15	10		25
Thereafter	32			32
Total	\$ 148	\$ 204	\$ 65	\$ 417

- (1) We have omitted uncertain income tax liabilities from this table due to the inherent uncertainty regarding the timing of potential issue resolution. Specifically, either the underlying positions have not been fully enough developed under audit to quantify at this time or, the years relating to the issues for certain jurisdictions are not currently under audit. At December 31, 2009, we had \$139 million of unrecognized tax benefits.

Off-Balance Sheet Arrangements

At December 31, 2009 and 2008, Activision Blizzard had no relationships with unconsolidated entities or financial parties, such as entities often referred to as structured finance or special purpose entities, which would have been established for the purpose of facilitating off-balance sheet arrangements or other contractually narrow or limited purposes, that have or are reasonably likely to have a material future effect on our financial condition, changes in financial condition, revenues or expenses, results of operation, liquidity, capital expenditure, or capital resources.

Financial Disclosure

We maintain internal control over financial reporting, which generally includes those controls relating to the preparation of our financial statements in conformity with accounting principles generally accepted in the United States of America ("U.S. GAAP"). We also are focused on our "disclosure controls and procedures," which as defined by the Securities and Exchange Commission (the "SEC") are generally those controls and procedures designed to ensure that financial and non-financial information required to be disclosed in our reports filed with the SEC is reported within the time periods specified in the SEC's rules and forms, and that such information is communicated to management, including our principal executive and financial officers, as appropriate, to allow timely decisions regarding required disclosure.

Our Disclosure Committee, which operates under the Board-approved Disclosure Committee Charter and Disclosure Controls & Procedures Policy, includes senior management representatives and assists executive management in its oversight of the accuracy and timeliness of our disclosures, as well as in implementing and evaluating our overall disclosure process. As part of our disclosure process, senior finance and operational representatives from all of our corporate divisions and business units prepare quarterly reports regarding their current quarter operational performance, future trends, subsequent events, internal controls, changes in internal controls and other accounting and disclosure-relevant information. These quarterly reports are reviewed by certain key corporate finance executives. These corporate finance representatives also conduct quarterly interviews on a rotating basis with the preparers of selected quarterly reports. The results of the quarterly reports and related interviews are

Table of Contents

reviewed by the Disclosure Committee. Finance representatives also conduct reviews with our senior management team, our internal and external counsel and other appropriate personnel involved in the disclosure process, as appropriate. Additionally, senior finance and operational representatives provide internal certifications regarding the accuracy of information they provide that is utilized in the preparation of our periodic public reports filed with the SEC. Financial results and other financial information also are reviewed with the Audit Committee of the Board of Directors on a quarterly basis. As required by applicable regulatory requirements, the principal executive and financial officers review and make various certifications regarding the accuracy of our periodic public reports filed with the SEC, our disclosure controls and procedures, and our internal control over financial reporting. With the assistance of the Disclosure Committee, we will continue to assess and monitor, and make refinements to, our disclosure controls and procedures, and our internal control over financial reporting.

Critical Accounting Policies and Estimates

The preparation of financial statements in conformity with GAAP requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates. The impact and any associated risks related to these policies on our business operations is discussed throughout Management's Discussion and Analysis of Financial Condition and Results of Operations where such policies affect our reported and expected financial results. The estimates 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 because 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 estimates are described in the following paragraphs.

Revenue Recognition. We recognize revenue from the sale of our products upon the transfer of title and risk of loss to our customers, and once any performance obligations have been completed. Certain products are sold to customers with a street date (the earliest date these products may be sold by retailers). For these products we recognize revenue on the later of the street date or the sale date. Revenue from product sales is recognized after deducting the estimated allowance for returns and price protection.

Some of our software products provide limited online features at no additional cost to the consumer. Generally, we consider such features to be incidental to the overall product offering and an inconsequential deliverable. Accordingly, we recognize revenue related to products containing these limited online features upon the transfer of title and risk of loss to our customer. In instances where online features or additional functionality is considered more than an inconsequential separate deliverable in addition to the software product, we take this into account when applying our revenue recognition policy. This evaluation is performed for each software product and any online transactions, such as electronic downloads of titles with product add-ons when it is released.

In instances where the online service is considered more than an inconsequential separate deliverable in addition to the software product, we take this into account when applying our revenue recognition policy. This evaluation is performed for each software product together with any online transactions, such as electronic downloads of titles or product add-ons when it is released. When we determine that a software title contains online functionality that constitutes a more-than-inconsequential separate service deliverable in addition to the product, principally because of its importance to game play, we consider that our performance obligations for this title extend beyond the sale of the game. Vendor-specific objective evidence of fair value does not exist for the online functionality, as we do not separately charge for this component of the title. As a result, we recognize all of the revenue from the sale of the title ratably over an estimated service period, which is estimated to begin the month after the sale date or the street date of the title, whichever is later. In addition, we defer the costs of sales for the title

Table of Contents

(excluding intangible asset amortization) to match revenues. Cost of sales includes manufacturing costs, software royalties and amortization, and intellectual property licenses.

We recognize *World of Warcraft* boxed product, expansion packs and other value added service revenues each with the related subscription service revenue ratably over the estimated service periods beginning upon activation of the software and delivery of the services. Revenues attributed to the sale of *World of Warcraft* boxed software and related expansion packs are classified as product sales and revenues attributable to subscription and other value added services are classified as subscription, licensing and other revenues.

We currently estimate the service periods over which revenues are recognized range from a minimum of five months to a maximum of less than a year.

Determining whether the online service for a particular game constitutes more than an inconsequential deliverable is subjective and requires management's judgment. Determining the estimated service periods and product life over which to recognize the revenue and related costs of sales is also subjective and involves management's judgment.

Allowances for Returns, Price Protection, Doubtful Accounts, and Inventory Obsolescence. We may permit product returns from, or grant price protection to, our customers under certain conditions. In general, price protection refers to the circumstances in which we elect to decrease the wholesale price of a product by a certain amount and, when granted and applicable, allows customers a credit against amounts owed by such customers to us with respect to open and/or future invoices. The conditions our customers must meet to be granted the right to return products or price protection include, among other things, compliance with applicable trading and payment terms, and consistent return of inventory and delivery of sell-through reports to us. We may also consider other factors, including the facilitation of slow-moving inventory and other market factors. Management must make estimates of potential future product returns and price protection related to current period product revenue. We estimate the amount of future returns and price protection for current period product revenue utilizing historical experience and information regarding inventory levels and the demand and acceptance of our products by the end consumer. The following factors are used to estimate the amount of future returns and price protection for a particular title: historical performance of titles in similar genres; historical performance of the hardware platform; historical performance of the franchise; console hardware life cycle; sales force and retail customer feedback; industry pricing; weeks of on-hand retail channel inventory; absolute quantity of on-hand retail channel inventory; our warehouse on-hand inventory levels; the title's recent sell-through history (if available); marketing trade programs; and competing titles. The relative importance of these factors varies among titles depending upon, among other items, genre, platform, seasonality, and sales strategy. Significant management judgments and estimates must be made and used in connection with establishing the allowance for returns and price protection in any accounting period. Based upon historical experience, we believe that our estimates are reasonable. However, actual returns and price protection could vary materially from our allowance estimates due to a number of reasons including, among others, a lack of consumer acceptance of a title, the release in the same period of a similarly themed title by a competitor, or technological obsolescence due to the emergence of new hardware platforms. Material differences may result in the amount and timing of our revenue for any period if factors or market conditions change or if management makes different judgments or utilizes different estimates in determining the allowances for returns and price protection. For example, a 1% change in our December 31, 2009 allowance for returns and price protection would impact net revenues by approximately \$3 million.

Similarly, management must make estimates of the uncollectibility of our accounts receivable. In estimating the allowance for doubtful accounts, we analyze the age of current outstanding account balances, historical bad debts, customer concentrations, customer creditworthiness, current economic trends, and changes in our customers' payment terms and their economic condition, as well as whether

Table of Contents

we can obtain sufficient credit insurance. Any significant changes in any of these criteria would affect management's estimates in establishing our allowance for doubtful accounts.

We regularly review inventory quantities on-hand and in the retail channel. We write down inventory based on excess or obsolete inventories determined primarily by future anticipated demand for our products. Inventory write-downs are measured as the difference between the cost of the inventory and market value, based upon assumptions about future demand, which are inherently difficult to assess. At the point of a loss recognition, a new, lower cost basis for that inventory is established, and subsequent changes in facts and circumstances do not result in the restoration or increase in that newly established basis.

Software Development Costs and Intellectual Property Licenses. Software development costs include payments made to independent software developers under development agreements, as well as direct costs incurred for internally developed products.

We account for software development costs in accordance with the FASB guidance for the costs of computer software to be sold, leased, or otherwise marketed ("ASC Subtopic 985-20"). Software development costs are capitalized once the technological feasibility of a product is established and such costs are determined to be recoverable. Technological feasibility of a product encompasses both technical design documentation and game design documentation, or the completed and tested product design and working model. Significant management judgments and estimates are utilized in the assessment of when technological feasibility is established. For products where proven technology exists, this may occur early in the development cycle. Technological feasibility is evaluated on a product-by-product basis. Prior to a product's release, we expense, as part of "cost of sales software royalties and amortization," capitalized costs when we believe such amounts are not recoverable. Capitalized costs for those products that are cancelled or abandoned are charged to product development expense in the period of cancellation. Amounts related to software development which are not capitalized are charged immediately to product development expense.

Commencing upon product release, capitalized software development costs are amortized to "cost of sales software royalties and amortization" based on the ratio of current revenues to total projected revenues for the specific product, generally resulting in an amortization period of six months or less.

Intellectual property license costs represent license fees paid to intellectual property rights holders for use of their trademarks, copyrights, software, technology, music, or other intellectual property or proprietary rights in the development of our products. Depending upon the agreement with the rights holder, we may obtain the rights to use acquired intellectual property in multiple products over multiple years, or alternatively, for a single product. Prior to the related product's release, we expense, as part of "cost of sales intellectual property licenses," capitalized intellectual property costs when we believe such amounts are not recoverable. Capitalized intellectual property costs for those products that are cancelled or abandoned are charged to product development expense in the period of cancellation.

Commencing upon the related product's release, capitalized intellectual property license costs are amortized to "cost of sales intellectual property licenses" based on the ratio of current revenues for the specific product to total projected revenues for all products in which the licensed property will be utilized. As intellectual property license contracts may extend for multiple years, the amortization of capitalized intellectual property license costs relating to such contracts may extend beyond one year.

We evaluate the future recoverability of capitalized software development costs and intellectual property licenses on a quarterly basis. For products that have been released in prior periods, the primary evaluation criterion is actual title performance. For products that are scheduled to be released in future periods, recoverability is evaluated based on the expected performance of the specific products to which the costs relate or in which the licensed trademark or copyright is to be used. Criteria used to evaluate expected product performance include: historical performance of comparable

Table of Contents

products developed with comparable technology; orders for the product prior to its release; and, for any sequel product, estimated performance based on the performance of the product on which the sequel is based. Further, as many of our capitalized intellectual property licenses extend for multiple products over multiple years, we also assess the recoverability of capitalized intellectual property license costs based on certain qualitative factors, such as the success of other products and/or entertainment vehicles utilizing the intellectual property, whether there are any future planned theatrical releases or television series based on the intellectual property, and the rights holder's continued promotion and exploitation of the intellectual property.

Significant management judgments and estimates are utilized in the assessment of the recoverability of capitalized costs. In evaluating the recoverability of capitalized costs, the assessment of expected product performance utilizes forecasted sales amounts and estimates of additional costs to be incurred. If revised forecasted or actual product sales are less than the original forecasted amounts utilized in the initial recoverability analysis, the net realizable value may be lower than originally estimated in any given quarter, which could result in an impairment charge. Material differences may result in the amount and timing of charges for any period if management makes different judgments or utilizes different estimates in evaluating these qualitative factors.

Income Taxes. We record a tax provision for the anticipated tax consequences of the reported results of operations. In accordance with FASB income tax guidance ("ASC Topic 740"), the provision for income taxes is computed using the asset and liability method, under which deferred tax assets and liabilities are recognized for the expected future tax consequences attributable to differences between the financial statement carrying amounts of existing assets and liabilities and their respective tax bases and operating losses and tax credit carryforwards. Deferred tax assets and liabilities are measured using enacted tax rates expected to apply to taxable income in the years in which those temporary differences are expected to be recovered or settled. We record a valuation allowance to reduce deferred tax assets to the amount that is believed more likely than not to be realized.

Management believes it is more likely than not that forecasted income, including income that may be generated as a result of certain tax planning strategies, together with the tax effects of the deferred tax liabilities, will be sufficient to fully recover the remaining deferred tax assets. In the event that all or part of the net deferred tax assets are determined not to be realizable in the future, an adjustment to the valuation allowance would be charged to earnings in the period such determination is made. In addition, the calculation of tax liabilities involves significant judgment in estimating the impact of uncertainties in the application of ASC Topic 740 and other complex tax laws. Resolution of these uncertainties in a manner inconsistent with management's expectations could have a material impact on our financial condition and operating results.

Fair Value Estimates

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

There are various valuation techniques used to estimate fair value. These include (1) the market approach where market transactions for identical or comparable assets or liabilities are used to determine the fair value, (2) the income approach, which uses valuation techniques to convert future amounts (for example, future cash flows or future earnings) to a single present amount, and (3) the cost approach, which is based on the amount that would be required to replace an asset. For many of our fair value estimates, including our estimates of the fair value of acquired intangible assets, we use the income approach. Using the income approach requires the use of financial models, which require

Table of Contents

us to make various estimates including, but not limited to (1) the potential future cash flows for the asset, liability or equity instrument being measured, (2) the timing of receipt or payment of those future cash flows, (3) the time value of money associated with the delayed receipt or payment of such cash flows, and (4) the inherent risk associated with the cash flows (risk premium). Making these cash flow estimates is inherently difficult and subjective, and, if any of the estimates used to determine the fair value using the income approach turns out to be inaccurate, our financial results may be negatively impacted. Furthermore, relatively small changes in many of these estimates can have a significant impact on the estimated fair value resulting from the financial models or the related accounting conclusion reached. For example, a relatively small change in the estimated fair value of an asset may change a conclusion as to whether an asset is impaired. While we are required to make certain fair value assessments associated with the accounting for several types of transactions, the following areas are the most sensitive to the assessments:

Business Combinations. We must estimate the fair value of assets acquired and liabilities assumed in a business combination. Our assessment of the estimated fair value of each of these can have a material effect on our reported results as intangible assets are amortized over various lives. Furthermore, a change in the estimated fair value of an asset or liability often has a direct impact on the amount to recognize as goodwill, which is an asset that is not amortized. Often determining the fair value of these assets and liabilities assumed requires an assessment of expected use of the asset, the expected cost to extinguish the liability or our expectations related to the timing and the successful completion of development of an acquired in-process technology. Such estimates are inherently difficult and subjective and can have a material impact on our financial statements.

Assessment of Impairment of Assets. Management evaluates the recoverability of our identifiable intangible assets and other long-lived assets in accordance with FASB literature related to accounting for the impairment or disposal of long-lived assets within ASC Subtopic 360-10, which generally requires the assessment of these assets for recoverability when events or circumstances indicate a potential impairment exists. We considered certain events and circumstances in determining whether the carrying value of identifiable intangible assets and other long-lived assets may not be recoverable including, but not limited to: significant changes in performance relative to expected operating results; significant changes in the use of the assets; significant negative industry or economic trends; a significant decline in our stock price for a sustained period of time; and changes in our business strategy. In determining whether an impairment exists, we estimate the undiscounted cash flows to be generated from the use and ultimate disposition of these assets. If an impairment is indicated based on a comparison of the assets' carrying values and the undiscounted cash flows, the impairment loss is measured as the amount by which the carrying amount of the assets exceeds the fair value of the assets.

During 2009, we recorded an impairment charge of \$409 million to our finite-lived intangible assets. See Note 12 of the Notes to Consolidated Financial Statements included in Item 8 of this Annual Report on Form 10-K for additional information regarding the determination of the impairment charges recorded for the year ended December 31, 2009.

FASB literature related to the accounting for goodwill and other intangibles within ASC Topic 350 requires a two-step approach to testing goodwill for impairment for each reporting unit. Our reporting units are determined by the components of our operating segments that constitute a business for which both (1) discrete financial information is available and (2) segment management regularly reviews the operating results of that component. ASC Topic 350 requires that the impairment test be performed at least annually by applying a fair-value-based test. The first step measures for impairment by applying fair-value-based tests at the reporting unit level. The second step (if necessary) measures the amount of impairment by applying fair-value-based tests to the individual assets and liabilities within each reporting unit.

Table of Contents

To determine the fair values of the reporting units used in the first step, we use a discounted cash flow approach. Each step requires us to make judgments and involves the use of significant estimates and assumptions. These estimates and assumptions include long-term growth rates and operating margins used to calculate projected future cash flows, risk-adjusted discount rates based on our weighted average cost of capital, and future economic and market conditions. These estimates and assumptions have to be made for each reporting unit evaluated for impairment. Our estimates for market growth, our market share and costs are based on historical data, various internal estimates and certain external sources, and are based on assumptions that are consistent with the plans and estimates we are using to manage the underlying business. If future forecasts are revised, they may indicate or require future impairment charges. We base our fair value estimates on assumptions we believe to be reasonable but that are unpredictable and inherently uncertain. Actual future results may differ from those estimates.

Stock-Based Compensation. We estimate the value of share-based payment awards on the measurement date using a binomial-lattice model. Our determination of fair value of share-based payment awards on the date of grant using an option-pricing model is affected by our stock price as well as assumptions regarding a number of highly complex and subjective variables. These variables include, but are not limited to, our expected stock price volatility over the term of the awards, and actual and projected employee stock option exercise behaviors.

For a detailed discussion of the application of these and other accounting policies see Note 2 of the Notes to Consolidated Financial Statements included in Item 8 of this Annual Report on Form 10-K.

Recently Issued Accounting Standards

In June 2009, the FASB issued an amendment to the accounting and disclosure requirements for the consolidation of variable interest entities (VIEs), which amends the evaluation criteria used to identify the primary beneficiary of a variable interest entity. Additionally, this amendment requires ongoing reassessments of whether an enterprise is the primary beneficiary of the variable interest entity. This amendment is effective for financial statements issued for fiscal years beginning after November 15, 2009. The adoption of this FASB amendment does not have any impact on our consolidated financial statements.

In October 2009, the FASB issued an update to *Revenue Recognition Multiple-Deliverable Revenue Arrangements*. This update establishes the accounting and reporting guidance for arrangements including multiple revenue-generating activities. This update provides amendments to the criteria for separating deliverables, measuring and allocating arrangement consideration to one or more units of accounting. The amendments in this update also establish a selling price hierarchy for determining the selling price of a deliverable. Significantly enhanced disclosures are also required to provide information about a vendor's multiple-deliverable revenue arrangements, including information about the nature and terms, significant deliverables, and its performance within arrangements. The amendments also require providing information about the significant judgments made and changes to those judgments and about how the application of the relative selling-price method affects the timing or amount of revenue recognition. The amendments in this update are effective prospectively for revenue arrangements entered into or materially modified in the fiscal years beginning on or after June 15, 2010. Early application is permitted. We are currently evaluating the impact, if any, of this new accounting update on our consolidated financial statements.

In October 2009, the FASB issued an update to *Software Certain Revenue Arrangements That Include Software Elements*. This update changes the accounting model for revenue arrangements that include both tangible products and software elements that are "essential to the functionality," and excludes these products from the scope of current software revenue guidance. The new guidance will

Table of Contents

include factors to help companies determine which software elements are considered "essential to the functionality." The amendments will now subject software-enabled products to other revenue guidance and disclosure requirements, such as guidance surrounding revenue arrangements with multiple-deliverables. The amendments in this update are effective prospectively for revenue arrangements entered into or materially modified in the fiscal years beginning on or after June 15, 2010. Early application is permitted. We are currently evaluating the impact, if any, of this new accounting update on our consolidated financial statements.

In January 2010, the FASB issued an update to *Fair Value Measurements and Disclosures*. This update provides amendments to ASC Subtopic 820-10 requiring new disclosures regarding (1) transfers in and out of Levels 1 and 2, in which the Company should disclose separately the amounts of significant transfers in and out of Level 1 and Level 2 fair value measurements and describe the reasons for the transfers, and (2) the reconciliation for fair value measurements using significant unobservable inputs (Level 3), in which the Company should present separately information about purchases, sales, issuances, and settlements (on a gross basis rather than as one net number). In addition the update provides clarification of existing disclosures regarding the level of disaggregation and disclosures about inputs and valuation techniques. The new disclosures and clarifications of existing disclosures are effective for interim and annual reporting periods beginning after December 15, 2009, except for the disclosures about purchase, sales, issuances, and settlements in the roll forward activity in Level 3 fair value measurements. Those disclosures are effective for fiscal years beginning after December 15, 2010 and for interim periods within those fiscal years. We are currently evaluating the impact, if any, of this new accounting update on our consolidated financial statements.

Item 7A. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

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

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 to manage interest rate risk in our investment portfolio. Our investment portfolio consists primarily of debt instruments with high credit quality and relatively short average maturities and money market funds that invest in such securities. As short-term securities mature relatively quickly and must be reinvested at the then-current market rates, interest income on a portfolio consisting of cash, cash equivalents, or short-term securities is more subject to market fluctuations than a portfolio of longer term securities. Conversely, the fair value of such a portfolio is less sensitive to market fluctuations than a portfolio of longer term securities. At December 31, 2009, our \$2,768 million of cash and cash equivalents were comprised primarily of money market funds. At December 31, 2009, our \$477 million of short-term investments included \$389 million of U.S. government agency securities, \$2 million of mortgage-backed securities, \$54 million of auction rate securities classified as trading, and \$32 million of restricted cash. We had \$23 million in auction rate securities at fair value classified as long-term investments at December 31, 2009. Most of our investment portfolio is invested in short-term or variable rate securities. Accordingly, we believe that a sharp change in interest rates would not have a material effect on our short-term investment portfolio.

Foreign Currency Exchange Rate Risk

We transact business in many different foreign currencies and may be exposed to financial market risk resulting from fluctuations in foreign currency exchange rates. Currency volatility is monitored frequently throughout the year. We enter into currency forward contracts and swaps with Vivendi, generally with maturities of twelve months or less, to mitigate our risk associated with our foreign

Table of Contents

currency exchange rate exposure resulting from our foreign currency denominated financial assets and liabilities (e.g. intercompany receivables and payables) and earnings. We expect to continue to use economic hedge programs in the future to reduce financial market risks if it is determined that such hedging activities are appropriate to reduce risk. We do not hold or purchase any foreign currency contracts for trading or speculative purposes. All foreign currency economic hedging transactions are backed, in amount and by maturity, by an identified economic underlying item.

The gross notional amount of outstanding foreign exchange swaps was \$120 million at December 31, 2009. The notional amounts of outstanding forward foreign exchange contracts and foreign exchange swaps were \$126 million and \$118 million, respectively, at December 31, 2008. A pre-tax net unrealized loss of \$2 million and gain of \$3 million for the years ended December 31, 2009 and 2008, respectively, resulted from the foreign exchange contracts and swaps with Vivendi and were recognized in the Consolidated Statements of Operations.

Item 8. FINANCIAL STATEMENTS AND SUPPLEMENTARY DATA

<u>Reports of Independent Registered Public Accounting Firms</u>	<u>F-1</u>
<u>Consolidated Balance Sheets at December 31, 2009 and 2008</u>	<u>F-3</u>
<u>Consolidated Statements of Operations for the Years Ended December 31, 2009, 2008, and 2007</u>	<u>F-4</u>
<u>Consolidated Statements of Changes in Shareholders' Equity for the Years Ended December 31, 2009, 2008, and 2007</u>	<u>F-5</u>
<u>Consolidated Statements of Cash Flows for the Years Ended December 31, 2009, 2008, and 2007</u>	<u>F-7</u>
<u>Notes to Consolidated Financial Statements</u>	<u>F-8</u>
<u>Schedule II Valuation and Qualifying Accounts at December 31, 2009, 2008, and 2007</u>	<u>F-68</u>

Other financial statement schedules are omitted because the information called for is not applicable or is shown either in the Consolidated Financial Statements or the Notes thereto.

Item 9. CHANGES IN AND DISAGREEMENTS WITH ACCOUNTANTS ON ACCOUNTING AND FINANCIAL DISCLOSURE

None.

Item 9A. CONTROLS AND PROCEDURES

Definition and Limitations of Disclosure Controls and Procedures.

Our disclosure controls and procedures (as such term is defined in Rules 13a-15(e) and 15d-15(e) under the Exchange Act) are designed to reasonably ensure that information required to be disclosed in our reports filed under the Exchange Act is (i) recorded, processed, summarized, and reported within the time periods specified in the SEC's rules and forms and (ii) accumulated and communicated to management, including our principal executive officer and principal financial officer, as appropriate, to allow timely decisions regarding required disclosures. A control system, no matter how well designed and operated, can provide only reasonable assurance that it will detect or uncover failures within the Company to disclose material information otherwise required to be set forth in our periodic reports. Inherent limitations to any system of disclosure controls and procedures include, but are not limited to, the possibility of human error and the circumvention or overriding of such controls by one or more persons. In addition, we have designed our system of controls based on certain assumptions, which we believe are reasonable, about the likelihood of future events, and our system of controls may therefore not achieve its desired objectives under all possible future events.

Table of Contents

Evaluation of Disclosure Controls and Procedures.

Our management, with the participation of our principal executive officer and principal financial officer, has evaluated the effectiveness of our disclosure controls and procedures at December 31, 2009, the end of the period covered by this report. Based on this evaluation, the principal executive officer and principal financial officer concluded that, at December 31, 2009, our disclosure controls and procedures were effective to provide reasonable assurance that information required to be disclosed by the Company in the reports that it files or submits under the Exchange Act is (i) recorded, processed, summarized, and reported on a timely basis, and (ii) accumulated and communicated to management, including our principal executive officer and principal financial officer, as appropriate, to allow timely decisions regarding required disclosures.

Management's Report on Internal Control Over Financial Reporting

Our management is responsible for establishing and maintaining adequate internal control over financial reporting as such term is defined in Rules 13a-15(f) and 15d-15(f) under the Exchange Act. Our management, with the participation of our principal executive officer and principal financial officer, conducted an evaluation of the effectiveness, as of December 31, 2009, of our internal control over financial reporting using the criteria set forth by the Committee of Sponsoring Organizations of the Treadway Commission ("COSO") in Internal Control Integrated Framework. Based on this evaluation, our management concluded that our internal control over financial reporting was effective as of December 31, 2009.

Because of its inherent limitations, internal control over financial reporting may not prevent or detect misstatements. Also, projections of any evaluation of effectiveness to future periods are subject to the risks that controls may become inadequate because of changes in conditions, or that the degree of compliance with the policies and procedures may deteriorate.

The effectiveness of our internal control over financial reporting as of December 31, 2009 has been audited by PricewaterhouseCoopers LLP, an independent registered public accounting firm, as stated in their report included in this annual report on Form 10-K.

Changes in Internal Control Over Financial Reporting

There have not been any changes in our internal control over financial reporting during the most recent fiscal quarter that have materially affected or are reasonably likely to materially affect our internal control over financial reporting.

Item 9B. OTHER INFORMATION

In the fourth quarter of 2009, we submitted the following matter to a vote of security holders. (Information previously required by Item 4, now omitted in accordance with recent SEC rules).

We held a special meeting of the Company's stockholders on December 17, 2009 in Santa Monica, California. At the special meeting, our stockholders voted on the following proposal and cast their votes as follows:

Proposal: To approve an amendment to the Activision Blizzard, Inc. 2008 Incentive Plan to increase the number of shares reserved for issuance thereunder and the number of shares that may be granted pursuant to certain types of awards thereunder.

For	Against	Abstain
983,029,550	72,073,832	296,016

Table of Contents

PART III

Item 10. DIRECTORS, EXECUTIVE OFFICERS, AND CORPORATE GOVERNANCE

The information required by this Item is incorporated by reference to the sections of our definitive Proxy Statement for our 2010 Annual Meeting of Shareholders, entitled "Proposal 1 Election of Directors," "Executive Officers and Key Employees," "Section 16(a) Beneficial Ownership Reporting Compliance," "Corporate Governance Matters Code of Ethics for Senior Executive and Senior Financial Officers" and "Corporate Governance Matters Board of Directors and Committees Audit Committee" to be filed with the Securities and Exchange Commission.

Item 11. EXECUTIVE COMPENSATION

The information required by this Item is incorporated by reference to the sections of our definitive Proxy Statement for our 2010 Annual Meeting of Shareholders, entitled "Executive Compensation," "Director Compensation," and "Compensation Committee Report" to be filed with the Securities and Exchange Commission.

Item 12. SECURITY OWNERSHIP OF CERTAIN BENEFICIAL OWNERS AND MANAGEMENT AND RELATED SHAREHOLDER MATTERS

The information required by this Item is incorporated by reference to the sections of our definitive Proxy Statement for our 2010 Annual Meeting of Shareholders, entitled "Equity Compensation Plan Information" and "Security Ownership of Certain Beneficial Owners and Management" to be filed with the Securities and Exchange Commission.

Item 13. CERTAIN RELATIONSHIPS AND RELATED TRANSACTIONS, AND DIRECTOR INDEPENDENCE

The information required by this Item is incorporated by reference to the sections of our definitive Proxy Statement for our 2010 Annual Meeting of Shareholders, entitled "Certain Relationships and Related Transactions" and "Corporate Governance Matters Board of Directors and Committees Director Independence" to be filed with the Securities and Exchange Commission.

Item 14. PRINCIPAL ACCOUNTING FEES AND SERVICES

The information required by this Item is incorporated by reference to the sections of our definitive Proxy Statement for our 2010 Annual Meeting of Shareholders, entitled "Independent Registered Public Accounting Firm's Fees" to be filed with the Securities and Exchange Commission.

Table of Contents

PART IV

Item 15. EXHIBITS AND FINANCIAL STATEMENT SCHEDULE

- (a) 1. *Financial Statements* See Item 8. Consolidated Financial Statements and Supplementary Data for index to Financial Statements and Financial Statement Schedule on page 67 herein.
2. *Financial Statement Schedule* The following financial statement schedule of Activision Blizzard for the calendar years ended December 31, 2009, 2008, and 2007 is filed as part of this report and should be read in conjunction with the consolidated financial statements of Activision Blizzard:

Schedule II Valuation and Qualifying Accounts

Other financial statement schedules are omitted because the information called for is not applicable or is shown either in the Consolidated Financial Statements or the Notes thereto.

3. The exhibits listed on the accompanying index to exhibits immediately following the financial statements are filed as part of, or hereby incorporated by reference into, this Form 10-K.

Table of Contents

SIGNATURES

Pursuant to the requirements of Section 13 or 15(d) of the Securities Exchange Act of 1934, the registrant has duly caused this report to be signed on its behalf by the undersigned, thereunto duly authorized.

Date: March 1, 2010

ACTIVISION BLIZZARD, INC.

By: /s/ ROBERT A. KOTICK

Robert A. Kotick
*Director, President and Chief Executive Officer of Activision
 Blizzard, Inc.
 (Principal Executive Officer)*

Pursuant to the requirements of the Securities Exchange Act of 1934, this report has been signed below by the following persons on behalf of the registrant and in the capacities and on the dates indicated.

By:	<u>/s/ PHILIPPE G. H. CAPRON</u>	Director	March 1, 2010
	(Philippe G. H. Capron)		

By:	<u>/s/ ROBERT J. CORTI</u>	Director	March 1, 2010
	(Robert J. Corti)		

By:	<u>/s/ FRÉDÉRIC R. CRÉPIN</u>	Director	March 1, 2010
	(Frédéric R. Crépin)		

By:	<u>/s/ BRIAN G. KELLY</u>	Co-Chairman and Director	March 1, 2010
	(Brian G. Kelly)		

By:	<u>/s/ ROBERT A. KOTICK</u>	Director, President, Chief Executive Officer and Principal Executive Officer	March 1, 2010
	(Robert A. Kotick)		

By:	<u>/s/ JEAN-BERNARD LÉVY</u>	Chairman and Director	March 1, 2010
	(Jean-Bernard Lévy)		

By:	<u>/s/ ROBERT J. MORGADO</u>	Director	March 1, 2010
	(Robert J. Morgado)		

Edgar Filing: Activision Blizzard, Inc. - Form 10-K

Table of Contents

By:	<u>/s/ DOUGLAS P. MORRIS</u> (Douglas P. Morris)	Director	March 1, 2010
By:	<u>/s/ STÉPHANE ROUSSEL</u> (Stéphane Roussel)	Director	March 1, 2010
By:	<u>/s/ RICHARD SARNOFF</u> (Richard Sarnoff)	Director	March 1, 2010
By:	<u>/s/ THOMAS TIPPL</u> (Thomas Tippl)	Chief Corporate Officer and Chief Financial Officer, Principal Financial and Accounting Officer	March 1, 2010
By:	<u>/s/ RÉGIS TURRINI</u> (Régis Turrini)	Director	March 1, 2010

Table of Contents

REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM

To the Board of Directors and Shareholders of Activision Blizzard, Inc.:

In our opinion, the accompanying consolidated balance sheets and the related consolidated statements of operations, changes in shareholders' equity and cash flows, present fairly, in all material respects, the financial position of Activision Blizzard, Inc. and its subsidiaries at December 31, 2009 and 2008, and the results of their operations and their cash flows for the years then ended in conformity with accounting principles generally accepted in the United States of America. In addition, in our opinion, the financial statement Schedule II Valuation and Qualifying Accounts presents fairly, in all material respects, the information set forth therein for the years ended December 31, 2009 and 2008 when read in conjunction with the related consolidated financial statements. Also in our opinion, the Company maintained, in all material respects, effective internal control over financial reporting as of December 31, 2009, based on criteria established in *Internal Control Integrated Framework* issued by the Committee of Sponsoring Organizations of the Treadway Commission (COSO). The Company's management is responsible for these financial statements and financial statement schedule, for maintaining effective internal control over financial reporting and for its assessment of the effectiveness of internal control over financial reporting, included in Management's Report on Internal Control Over Financial Reporting appearing under Item 9A. Our responsibility is to express opinions on these financial statements, on the financial statement schedule, and on the Company's internal control over financial reporting based on our integrated audits. We conducted our audits in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audits to obtain reasonable assurance about whether the financial statements are free of material misstatement and whether effective internal control over financial reporting was maintained in all material respects. Our audits of the financial statements included examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements, assessing the accounting principles used and significant estimates made by management, and evaluating the overall financial statement presentation. Our audit of internal control over financial reporting included obtaining an understanding of internal control over financial reporting, assessing the risk that a material weakness exists, and testing and evaluating the design and operating effectiveness of internal control based on the assessed risk. Our audits also included performing such other procedures as we considered necessary in the circumstances. We believe that our audits provide a reasonable basis for our opinions.

A company's internal control over financial reporting is a process designed to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles. A company's internal control over financial reporting includes those policies and procedures that (i) pertain to the maintenance of records that, in reasonable detail, accurately and fairly reflect the transactions and dispositions of the assets of the company; (ii) provide reasonable assurance that transactions are recorded as necessary to permit preparation of financial statements in accordance with generally accepted accounting principles, and that receipts and expenditures of the company are being made only in accordance with authorizations of management and directors of the company; and (iii) provide reasonable assurance regarding prevention or timely detection of unauthorized acquisition, use, or disposition of the company's assets that could have a material effect on the financial statements.

Because of its inherent limitations, internal control over financial reporting may not prevent or detect misstatements. Also, projections of any evaluation of effectiveness to future periods are subject to the risk that controls may become inadequate because of changes in conditions, or that the degree of compliance with the policies or procedures may deteriorate.

/s/ PricewaterhouseCoopers LLP

Los Angeles, California
March 1, 2010

Table of Contents

REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM

The Board of Directors and Shareholders of Vivendi Games, Inc.

We have audited the accompanying consolidated statements of operations, changes in shareholders' equity, and cash flows of Vivendi Games, Inc. ("Vivendi Games," as described in Note 1) for the year ended December 31, 2007. Our audit also included the financial statement schedule on page F-68 for the year ended December 31, 2007. These financial statements and financial statement schedule are the responsibility of Vivendi Games' management. Our responsibility is to express an opinion on these financial statements and the financial statement schedule based on our audit.

We conducted our audit in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. We were not engaged to perform an audit of the Company's internal control over financial reporting. Our audit included consideration of internal control over financial reporting as a basis for designing audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Company's internal control over financial reporting. Accordingly, we express no such opinion. An audit also includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements, assessing the accounting principles used and significant estimates made by management, and evaluating the overall financial statement presentation. We believe that our audit provides a reasonable basis for our opinion.

In our opinion, the financial statements referred to above present fairly, in all material respects, the consolidated results of Vivendi Games' operations and its cash flows for the year ended December 31, 2007, in conformity with U.S. generally accepted accounting principles. Also, in our opinion, the related financial statement schedule, when considered in relation to the basic consolidated financial statements taken as a whole, presents fairly in all material respects the information set forth therein.

/s/ Ernst & Young LLP

Los Angeles, California
November 5, 2008

Table of Contents**ACTIVISION BLIZZARD, INC. AND SUBSIDIARIES****CONSOLIDATED BALANCE SHEETS****(Amounts in millions, except share data)**

	At December 31, 2009	At December 31, 2008
Assets		
Current assets:		
Cash and cash equivalents	\$ 2,768	\$ 2,958
Short-term investments	477	44
Accounts receivable, net of allowances of \$317 million and \$268 million at December 31, 2009 and 2008, respectively	739	974
Inventories	241	262
Software development	224	235
Intellectual property licenses	55	35
Deferred income taxes, net	498	536
Intangible assets, net		14
Other current assets	327	201
Total current assets	5,329	5,259
Long-term investments	23	78
Software development	10	1
Intellectual property licenses	28	5
Property and equipment, net	138	149
Other assets	9	30
Intangible assets, net	618	1,283
Trademark and trade names	433	433
Goodwill	7,154	7,227
Total assets	\$ 13,742	\$ 14,465

Liabilities and Shareholders' Equity

Current liabilities:		
Accounts payable	\$ 302	\$ 319
Deferred revenues	1,426	923
Accrued expenses and other liabilities	779	842
Total current liabilities	2,507	2,084
Deferred income taxes, net	270	615
Other liabilities	209	239
Total liabilities	2,986	2,938
Commitments and contingencies (Note 18)		
Shareholders' equity:		
Common stock, \$.000001 par value per share, 2,400,000,000 shares authorized, 1,364,117,675 and 1,325,206,032 shares issued at December 31, 2009 and 2008, respectively		
Additional paid-in capital	12,376	12,170
Less: Treasury stock, at cost, 113,686,498 and 12,967,265 shares at December 31, 2009 and 2008, respectively	(1,235)	(126)
Accumulated deficit	(361)	(474)
Accumulated other comprehensive loss	(24)	(43)

Edgar Filing: Activision Blizzard, Inc. - Form 10-K

Total shareholders' equity	10,756	11,527
----------------------------	--------	--------

Total liabilities and shareholders' equity	\$ 13,742	\$ 14,465
--	-----------	-----------

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

F-3

Table of Contents**ACTIVISION BLIZZARD, INC. AND SUBSIDIARIES****CONSOLIDATED STATEMENTS OF OPERATIONS**

(Amounts in millions, except per share data)

	For the years ended December 31,		
	2009	2008	2007
Net revenues			
Product sales	\$ 3,080	\$ 1,872	\$ 457
Subscription, licensing, and other revenues	1,199	1,154	892
Total net revenues	4,279	3,026	1,349
Costs and expenses			
Cost of sales product costs	1,432	1,160	171
Cost of sales software royalties and amortization	348	267	52
Cost of sales intellectual property licenses	315	219	9
Cost of sales massively multi-player online role-playing game ("MMORPG")	212	193	204
Product development	627	592	397
Sales and marketing	544	464	172
General and administrative	395	271	166
Impairment of intangible assets	409		
Restructuring	23	93	(1)
Total costs and expenses	4,305	3,259	1,170
Operating income (loss)	(26)	(233)	179
Investment and other income (loss), net	18	46	(4)
Income (loss) before income tax benefit	(8)	(187)	175
Income tax benefit	(121)	(80)	(52)
Net income (loss)	\$ 113	\$ (107)	\$ 227
Earnings (loss) per common share			
Basic	\$ 0.09	\$ (0.11)	\$ 0.38
Diluted	\$ 0.09	\$ (0.11)	\$ 0.38
Weighted average number of shares outstanding			
Basic	1,283	946	591
Diluted	1,311	946	591

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

Table of Contents

ACTIVISION BLIZZARD, INC. AND SUBSIDIARIES

CONSOLIDATED STATEMENTS OF CHANGES IN SHAREHOLDERS' EQUITY

For the years ended December 31, 2009, 2008 and 2007

(Amounts in millions)

	Common Stock		Additional Paid-In Capital		Treasury Stock		Net Payable to Accumulated Vivendi Deficit		Accumulated Other Comprehensive Income (Loss)	Total Shareholders' Equity
	Shares	Amount	Capital	Shares	Amount					
Balance at December 31, 2006(1)	591	\$	\$ 535		\$	\$ 372	\$ (594)	\$	34	\$ 347
Net transfers to Vivendi			(45)			(295)				(340)
Components of comprehensive income:										
Net income							227			227
Foreign currency translation adjustment									6	6
Total comprehensive income										233
Balance at December 31, 2007(1)	591		490			77	(367)		40	240
Settlement of payable to Vivendi (see Note 23)			(2)			(77)				(79)
Components of comprehensive loss:										
Net loss							(107)			(107)
Unrealized depreciation on short-term investments, net of taxes									(2)	(2)
Foreign currency translation adjustment									(81)	(81)
Total comprehensive loss										(190)
Purchase consideration upon the business combination	602		9,919							9,919
Issuance of additional common stock related to the Business Combination(see Note 1)	126		1,731							1,731
Tender offer (see Note 1)			(2)							(2)
Issuance of common stock pursuant to employee stock options and restricted stock rights	6		22							22
Stock-based compensation expense related to employee stock options and restricted stock rights			89							89
Excess tax benefit associated with employee stock options and restricted stock rights			2							2
Shares repurchased (see Note 20)				(13)	(126)					(126)
			(79)							(79)

Return of capital to
Vivendi (see Note 23)

F-5

Table of Contents

ACTIVISION BLIZZARD, INC. AND SUBSIDIARIES

CONSOLIDATED STATEMENTS OF CHANGES IN SHAREHOLDERS' EQUITY (Continued)

For the years ended December 31, 2009, 2008 and 2007

(Amounts in millions)

	Common Stock		Additional	Treasury Stock		Net	Accumulated		Other	Total
	Shares	Amount	Paid-In	Shares	Amount	Payable	Accumulated	Comprehensive	Income	Shareholders'
			Capital			to Vivendi	Deficit	(Loss)		Equity
Balance at December 31, 2008	1,325		12,170	(13)	(126)		(474)		(43)	11,527
Components of comprehensive income:										
Net income							113			113
Foreign currency translation adjustment									19	19
Total comprehensive income										132
Issuance of common stock pursuant to employee stock options and restricted stock rights	36		81							81
Stock-based compensation expense related to employee stock options and restricted stock rights			154							154
Tax shortfall from employee stock option exercises and restricted stock rights			(1)							(1)
Issuance of contingent considerations	3		2							2
Shares repurchased (see Note 20)				(101)	(1,109)					(1,109)
Return of capital to Vivendi related to settlement of pre-Business Combination taxes (see Note 16)			(30)							(30)
Balance at December 31, 2009	1,364	\$	\$ 12,376	(114)	\$ (1,235)	\$	\$ (361)	\$	(24)	\$ 10,756

(1)

The number of shares issued reflects the number of split adjusted shares received by Vivendi, former parent company of Vivendi Games.

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

Table of Contents**ACTIVISION BLIZZARD, INC. AND SUBSIDIARIES****CONSOLIDATED STATEMENTS OF CASH FLOWS**

(Amounts in millions)

	For the years ended December 31,		
	2009	2008	2007
Cash flows from operating activities:			
Net income (loss)	\$ 113	\$ (107)	\$ 227
Adjustments to reconcile net income (loss) to net cash provided by operating activities:			
Deferred income taxes	(256)	(430)	(77)
Impairment (see Notes 8 and 12)	409	26	
Depreciation and amortization	347	385	63
Unrealized (gain)/loss on auction rate securities classified as trading securities	(3)	7	
Unrealized loss on ARS rights from UBS	3	2	
Loss on disposal of property and equipment (see Note 8)	2	1	1
Amortization and write-off of capitalized software development costs and intellectual property licenses(1)	281	176	54
Stock-based compensation expense(2)	156	89	138
Excess tax benefits from stock option exercises	(79)	(21)	
Changes in operating assets and liabilities:			
Accounts receivable	235	(428)	25
Inventories	21	(20)	7
Software development and intellectual property licenses	(308)	(181)	(102)
Other assets	(110)	(165)	(6)
Deferred revenues	503	726	79
Accounts payable	(18)	86	(12)
Accrued expenses and other liabilities	(113)	233	34
Net cash provided by operating activities	1,183	379	431
Cash flows from investing activities:			
Capital expenditures	(69)	(46)	(68)
Net proceeds from disposal of assets restructuring (see Note 8)		9	
Cash acquired through Business Combination, net of cash payments to effect acquisitions		1,120	
Proceeds from sale of available-for-sale investments	2		
Proceeds from maturities of investments	44		
Purchase of short-term investments	(425)		
Decrease in restricted cash	5	18	
Net cash provided by (used in) investing activities	(443)	1,101	(68)
Cash flows from financing activities:			
Proceeds from issuance of common stock to employees	81	22	
Repurchase of common stock through tender offer		(2)	
Return of capital to Vivendi		(79)	
Issuance of additional common stock related to the Business Combination		1,731	
Repurchase of common stock	(1,109)	(126)	
Settlement of payable to Vivendi		(79)	(371)
Excess tax benefits from stock option exercises	79	21	
Net cash provided by (used in) financing activities	(949)	1,488	(371)
Effect of foreign exchange rate changes on cash and cash equivalents	19	(72)	2
Net increase (decrease) in cash and cash equivalents	(190)	2,896	(6)
Cash and cash equivalents at beginning of year	2,958	62	68

Edgar Filing: Activision Blizzard, Inc. - Form 10-K

Cash and cash equivalents at end of year	\$	2,768	\$	2,958	\$	62
--	----	-------	----	-------	----	----

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

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

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

F-7

Table of Contents

ACTIVISION BLIZZARD, INC. AND SUBSIDIARIES

Notes to Consolidated Financial Statements

1. Business and Business Combination

Business

Activision Blizzard, Inc. is a worldwide online, personal computer ("PC"), console and handheld game publisher. The terms "Activision Blizzard," the "Company," "we," "us," and "our" are used to refer collectively to Activision Blizzard, Inc. and its subsidiaries. Based upon our current organizational structure, we operate three operating segments as follows:

(i) Activision Publishing, Inc.

Activision Publishing, Inc. ("Activision") is a leading international publisher of interactive software products and peripherals. Activision develops and publishes video games on various consoles, handheld platforms and the PC platform through internally developed franchises and license agreements. Activision currently offers games that operate on the Sony Computer Entertainment, Inc. ("Sony") PlayStation 2 ("PS2"), Sony PlayStation 3 ("PS3"), Nintendo Co. Ltd. ("Nintendo") Wii ("Wii"), and Microsoft Corporation ("Microsoft") Xbox 360 ("Xbox 360") console systems; the Sony PlayStation Portable ("PSP") and Nintendo Dual Screen ("NDS") handheld devices; the PC; the Apple iPhone; and the new handheld game system Nintendo DSi. Our Activision business involves the development, marketing, and sale of products directly, by license, or through our affiliate label program with certain third-party publishers. Activision's products cover diverse game categories including action/adventure, action sports, racing, role-playing, simulation, first-person action, music, and strategy. Activision's target customer base ranges from casual players to core gamers, and children to adults.

(ii) Blizzard Entertainment, Inc.

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

(iii) Activision Blizzard Distribution

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

Table of Contents

ACTIVISION BLIZZARD, INC. AND SUBSIDIARIES

Notes to Consolidated Financial Statements (Continued)

1. Business and Business Combination (Continued)

Business Combination

On July 9, 2008, a business combination (the "Business Combination") by and among Activision, Inc., Sego Merger Corporation, a wholly-owned subsidiary of Activision, Inc., Vivendi S.A. ("Vivendi"), VGAC LLC, a wholly-owned subsidiary of Vivendi, and Vivendi Games, Inc. ("Vivendi Games"), a wholly-owned subsidiary of VGAC LLC, was consummated. As a result of the consummation of the Business Combination, Activision, Inc. was renamed Activision Blizzard, Inc. ("Activision Blizzard"). For accounting purposes, the Business Combination was treated as a "reverse acquisition," with Vivendi Games deemed to be the acquirer. The historical financial statements of Activision Blizzard prior to July 10, 2008 are those of Vivendi Games.

In connection with the Business Combination, we issued approximately 717 million shares of common stock to VGAC LLC including approximately 126 million shares of common stock purchased by Vivendi for \$1.7 billion. Immediately following the consummation of the Business Combination, VGAC owned 54% of Activision Blizzard's issued and outstanding common stock. Further, in accordance with the terms of the Business Combination Agreement, on July 16, 2008, Activision Blizzard commenced a tender offer to purchase up to 293 million shares of its common stock at a price of \$13.75 per share. The tender offer expired on August 13, 2008. We purchased 171,832 shares of our common stock as a result of the tender offer. These shares were accounted for using the treasury method and were retired and cancelled.

The common stock of Activision Blizzard is traded on NASDAQ under the ticker symbol "ATVI." Vivendi owned approximately 57% of Activision Blizzard's outstanding common stock at December 31, 2009.

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

Activision Blizzard's non-core exit operations

Activision Blizzard's non-core exit operations ("Other" or "Non-Core") represent legacy Vivendi Games' divisions or business units that we have exited, divested or wound down as part of our restructuring and integration efforts as a result of the Business Combination described above, but that do not meet the criteria for separate reporting of discontinued operations. Prior to July 1, 2009, Non-Core activities were managed as a stand-alone operating segment; however, in light of the minimal activities and insignificance of Non-Core activities, as of that date we ceased their management as a separate operating segment and consequently we are no longer providing separate operating segment disclosure and have reclassified our prior periods' segment presentation so that it conforms to the current period's presentation.

2. Summary of significant accounting policies

Basis of Consolidation and Presentation

The accompanying consolidated financial statements include the accounts and operations of the Company. All intercompany accounts and transactions have been eliminated. The consolidated financial statements have been prepared in conformity with accounting principles generally accepted in the United States of America ("U.S. GAAP"). The preparation of the consolidated financial statements in

Table of Contents

ACTIVISION BLIZZARD, INC. AND SUBSIDIARIES

Notes to Consolidated Financial Statements (Continued)

2. Summary of significant accounting policies (Continued)

conformity with U.S. GAAP requires management to make estimates and assumptions that affect the amounts reported in the consolidated financial statements. Actual results could differ from these estimates and assumptions.

The prior year consolidated balance sheet at December 31, 2008 and consolidated statement of cash flows for the year ended December 31, 2008 have been adjusted to correct immaterial errors related to the elimination of intercompany receivables and payables. The corrections reduced the accounts receivable and accounts payable line items in the December 31, 2008 consolidated balance sheet by \$236 million, which correspondingly impacted the change in accounts receivable and accounts payable in the consolidated statement of cash flows for the year ended December 31, 2008 by \$236 million. These corrections had no impact on net income, earnings (loss) per share, working capital or net cash provided by operating, investing and financing activities.

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

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

Cash, Cash Equivalents and Investment Securities

We consider all money market funds and highly liquid investments with maturities of three months or less when purchased to be cash equivalents.

Investments designated as available-for-sale securities are carried at fair value based on quoted market prices or estimated based on quoted market prices of financial instruments with similar characteristics. Unrealized gains and losses of the Company's available-for-sale securities are excluded from earnings and reported as a component of other comprehensive income (loss), when credit losses are not expected and the Company does not intend, or it is more likely than not that the Company will not be required, to sell the security prior to recovery of the security's amortized cost basis.

In general, investments with original maturities greater than 90 days and remaining maturities of less than one year are classified as short-term investments. In addition, investments with maturities beyond one year may be classified as short-term based on their highly liquid nature and because such investments represent the investment of cash that is available for current operations.

The specific identification method is used to determine the cost of securities disposed with realized gains and losses reflected in investment and other income (loss), net in the consolidated statements of operations.

The Company's investments include auction rate securities ("ARS"). These ARS are variable rate bonds tied to short-term interest rates with long-term maturities. ARS have interest rates which reset through a modified Dutch auction at predetermined short-term intervals, typically every 7, 28, or 35 days. Interest on ARS is generally paid at the end of each auction process and is based upon the interest rate determined for the prior auction. The majority of our ARS are AAA/Aaa rated, and are typically collateralized by student loans guaranteed by the U.S. government under the Federal Family Education Loan Program or backed by monoline bond insurance companies.

Table of Contents

ACTIVISION BLIZZARD, INC. AND SUBSIDIARIES

Notes to Consolidated Financial Statements (Continued)

2. Summary of significant accounting policies (Continued)

Our ARS held through UBS AG ("UBS") are classified as trading securities. Investments designated as trading securities are reported at fair value, with unrealized gains and losses recognized in earnings.

On November 14, 2008, we accepted an offer from UBS, providing us with rights related to our ARS held through UBS (the "Rights"). The Rights permit us to require UBS to purchase our ARS held through UBS at par value, which is defined as the price equal to the liquidation preference of the ARS plus accrued but unpaid dividends or interest, at any time during the period between June 30, 2010 and July 2, 2012. Conversely, UBS has the right, in its discretion, to purchase or sell our ARS at any time until July 2, 2012, so long as we receive payment at par value upon any sale or disposition. If auctions continue to fail, we expect to sell our ARS under the Rights. However, if the Rights are not exercised before July 2, 2012 they will expire and UBS will have no further rights or obligation to buy our ARS. So long as we hold our ARS, they will continue to accrue interest as determined by the auction process or by the terms of the Rights if the auction process continues to fail.

UBS's obligations under the Rights are not secured by its assets and do not require UBS to obtain any financing to support its performance obligations under the Rights. UBS has disclaimed any assurance that it will have sufficient financial resources to satisfy its obligations under the Rights.

The Rights represent a firm agreement in accordance with the Financial Accounting Standards Board ("FASB") Accounting Standards Codification ("ASC") Topic 815, regarding derivatives and hedging ("ASC Topic 815"), which defines a firm agreement as an agreement binding on both parties and usually legally enforceable, with the following characteristics: (a) the agreement specifies all significant terms, including the quantity to be exchanged, the fixed price, and the timing of the transaction, and (b) the agreement includes a disincentive for nonperformance that is sufficiently large to make performance probable. The enforceability of the Rights should be recognized as a free standing asset separate from the ARS. The Rights do not meet the definition of a derivative instrument under ASC Topic 815, because the underlying securities are not readily convertible to cash. Therefore, we have elected to measure the Rights at fair value under ASC Subtopic 825-10 regarding the fair value option for financial assets and financial liabilities, which permits an entity to measure certain items at fair value, to mitigate volatility in reported earnings from the changes in the fair value of the ARS. As a result, unrealized gains and losses will be included in earnings in future periods. We expect that future changes in the fair value of the Rights will largely mitigate fair value movements in the related ARS. At December 31, 2009, we have classified our investment in ARS held through UBS as a current asset as the expected settlement is June 30, 2010.

Restricted Cash Compensating Balances

Most of our restricted cash relates to a standby letter of credit required by one of our inventory manufacturers to qualify for payment terms on our inventory purchases. Under the terms of this arrangement, we are required to maintain with the issuing bank a compensating balance, restricted as to use, of not less than the sum of the available amount of the letter of credit plus the aggregate amount of any drawings under the letter of credit that have been honored thereunder, but not reimbursed. Restricted cash is included in short-term investments.

Table of Contents

ACTIVISION BLIZZARD, INC. AND SUBSIDIARIES

Notes to Consolidated Financial Statements (Continued)

2. Summary of significant accounting policies (Continued)

Financial Instruments

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

Activision Blizzard transacts business in various foreign currencies and has significant international sales and expenses denominated in foreign currencies, subjecting Activision Blizzard to foreign currency risk. Activision Blizzard utilizes foreign exchange forward contracts and swaps to mitigate foreign currency exchange rate risk associated with foreign currency denominated assets and liabilities. The foreign exchange forward contracts generally have contractual terms of less than a year. Activision Blizzard does not use foreign exchange forward contracts for speculative or trading purposes. None of Activision Blizzard's foreign exchange forward contracts were designated as hedging instruments under ASC Topic 815. Accordingly, gains or losses resulting from changes in the fair values of the foreign exchange forward contracts are reported as investment and other income (loss), net in the consolidated statements of operations.

Other-Than-Temporary Impairments

On April 1, 2009, we adopted prospectively a new accounting standard addressing the evaluation of fixed maturity securities for other-than-temporary impairments. These requirements have altered our policies and procedures for determining impairment charges recognized through earnings. The new standard requires a company to recognize a credit component (a credit impairment) of an other-than-temporary impairment of a fixed maturity security in earnings and the non-credit component in accumulated other comprehensive income (loss) if the company does not intend, or it is more likely than not that the company will not be required, to sell the security prior to recovery of the security's amortized cost basis. The new standard also changes the threshold for determining when an other-than-temporary impairment has occurred on a fixed maturity security with respect to intent and ability to hold the security until recovery and requires additional disclosures. A credit impairment, which is recognized in earnings when it occurs, is the difference between the amortized cost of the fixed maturity security and the estimated present value of cash flows expected to be collected (recovery value), as determined by management. The difference between fair value and amortized cost that is not related to a credit impairment is recognized as a separate component of accumulated other comprehensive income (loss), net of taxes. The adoption of this standard did not have a material impact on our consolidated financial statements.

Concentration of Credit Risk

Financial instruments which potentially subject us to concentration of credit risk consist principally of cash and cash equivalents and accounts receivable. We place our cash and cash equivalents with financial institutions. At various times, we had deposits in excess of coverage by the Federal Deposit

Table of Contents

ACTIVISION BLIZZARD, INC. AND SUBSIDIARIES

Notes to Consolidated Financial Statements (Continued)

2. Summary of significant accounting policies (Continued)

Insurance Corporation ("FDIC"), or the equivalent agencies in overseas jurisdictions, at these financial institutions.

Our customer base includes retail outlets and distributors, including mass-market retailers, consumer electronics stores, discount warehouses, and game specialty stores in the United States and countries worldwide. We perform ongoing credit evaluations of our customers and maintain allowances for potential credit losses. We generally do not require collateral or other security from our customers. We had two customers, Wal-Mart and GameStop, who each accounted for approximately 10% of the consolidated revenues for the year ended December 31, 2009 and accounted for approximately 18% and 10% of consolidated gross receivables at December 31, 2009, respectively.

For the year ended December 31, 2008, we had two customers, Wal-Mart and GameStop, who each accounted for approximately 11% of the consolidated net revenues and accounted for approximately 15% and 9% of consolidated gross receivables at December 31, 2008, respectively.

Software Development Costs and Intellectual Property Licenses

Software development costs include payments made to independent software developers under development agreements, as well as direct costs incurred for internally developed products.

We account for software development costs in accordance with the FASB guidance for the costs of computer software to be sold, leased, or otherwise marketed ("ASC Subtopic 985-20"). Software development costs are capitalized once the technological feasibility of a product is established and such costs are determined to be recoverable. Technological feasibility of a product encompasses both technical design documentation and game design documentation, or the completed and tested product design and working model. Significant management judgments and estimates are utilized in the assessment of when technological feasibility is established. For products where proven technology exists, this may occur early in the development cycle. Technological feasibility is evaluated on a product-by-product basis. Prior to a product's release, we expense, as part of "cost of sales software royalties and amortization", capitalized costs when we believe such amounts are not recoverable. Capitalized costs for those products that are cancelled or abandoned are charged to product development expense in the period of cancellation. Amounts related to software development which are not capitalized are charged immediately to product development expense.

Commencing upon product release, capitalized software development costs are amortized to "cost of sales software royalties and amortization" based on the ratio of current revenues to total projected revenues for the specific product, generally resulting in an amortization period of six months or less.

Intellectual property license costs represent license fees paid to intellectual property rights holders for use of their trademarks, copyrights, software, technology, music or other intellectual property or proprietary rights in the development of our products. Depending upon the agreement with the rights holder, we may obtain the rights to use acquired intellectual property in multiple products over multiple years, or alternatively, for a single product. Prior to the related product's release, we expense, as part of "cost of sales intellectual property licenses," capitalized intellectual property costs when we believe such amounts are not recoverable. Capitalized intellectual property costs for those products that are cancelled or abandoned are charged to product development expense in the period of cancellation.

Commencing upon the related product's release, capitalized intellectual property license costs are amortized to "cost of sales intellectual property licenses" based on the ratio of current revenues for

Table of Contents

ACTIVISION BLIZZARD, INC. AND SUBSIDIARIES

Notes to Consolidated Financial Statements (Continued)

2. Summary of significant accounting policies (Continued)

the specific product to total projected revenues for all products in which the licensed property will be utilized. As intellectual property license contracts may extend for multiple years, the amortization of capitalized intellectual property license costs relating to such contracts may extend beyond one year.

We evaluate the future recoverability of capitalized software development costs and intellectual property licenses on a quarterly basis. For products that have been released in prior periods, the primary evaluation criterion is actual title performance. For products that are scheduled to be released in future periods, recoverability is evaluated based on the expected performance of the specific products to which the costs relate or in which the licensed trademark or copyright is to be used. Criteria used to evaluate expected product performance include: historical performance of comparable products developed with comparable technology; orders for the product prior to its release; and, for any sequel product, estimated performance based on the performance of the product on which the sequel is based. Further, as many of our capitalized intellectual property licenses extend for multiple products over multiple years, we also assess the recoverability of capitalized intellectual property license costs based on certain qualitative factors, such as the success of other products and/or entertainment vehicles utilizing the intellectual property, whether there are any future planned theatrical releases or television series based on the intellectual property, and the rights holder's continued promotion and exploitation of the intellectual property.

Significant management judgments and estimates are utilized in the assessment of the recoverability of capitalized costs. In evaluating the recoverability of capitalized costs, the assessment of expected product performance utilizes forecasted sales amounts and estimates of additional costs to be incurred. If revised forecasted or actual product sales are less than the original forecasted amounts utilized in the initial recoverability analysis, the net realizable value may be lower than originally estimated in any given quarter, which could result in an impairment charge. Material differences may result in the amount and timing of charges for any period if management makes different judgments or utilizes different estimates in evaluating these qualitative factors.

Inventories

Inventories consist of materials (including manufacturing royalties paid to console manufacturers), labor and freight-in and are stated at the lower of cost (weighted average method) or market value.

Long-Lived Assets

Property and Equipment. Property and equipment are recorded at cost and depreciated on a straight-line basis over the shorter of the estimated useful lives or the lease term: buildings, 25 to 33 years; computer equipment, office furniture and other equipment, 2 to 5 years; leasehold improvements, the shorter of 5 years or the life of the lease. When assets are retired or disposed of, the cost and accumulated depreciation thereon are removed and any resulting gains or losses are included in the accompanying consolidated statements of operations.

Goodwill and Other Indefinite-Lived Assets. We account for goodwill using the provisions within ASC Topic 350. Under ASC Topic 350, goodwill is considered to have an indefinite life, and is carried at cost. Acquired trade names are assessed as indefinite lived assets as there are no foreseeable limits on the periods of time over which they are expected to contribute cash flows. Goodwill and acquired trade names are not amortized, but are subject to an impairment test annually and in between annual

Table of Contents

ACTIVISION BLIZZARD, INC. AND SUBSIDIARIES

Notes to Consolidated Financial Statements (Continued)

2. Summary of significant accounting policies (Continued)

tests when events or circumstances indicate that the carrying value may not be recoverable. We perform our annual impairment testing at December 31.

We have determined our reporting units based on the guidance within ASC Subtopic 350-20. As of December 31, 2009 and 2008, the Company's reporting units consisted of Activision, Blizzard, and Distribution. We test goodwill for possible impairment by first determining the fair value of the related reporting unit and comparing this value to the recorded net assets of the reporting unit, including goodwill. Fair value is determined using a combination of a discounted cash flow model and market comparable valuations of peer companies. The estimated fair values of each of our reporting units exceeded their carrying values by a range of approximately \$0.1 billion to \$5.9 billion as of December 31, 2009. The estimated fair values exceed their respective reporting units carrying values by a range of approximately 20% to 480% as of December 31, 2009. As such, we have determined that no impairment has occurred at December 31, 2009 based upon a set of assumptions regarding discounted future cash flows, which represent our best estimate of future performance at this time. In determining the fair value of our reporting units, we assumed a discount rate between 11.5% and 13%.

In completing our goodwill impairment analysis, we test the appropriateness of our reporting units' estimated fair value by reconciling the aggregate reporting units' fair values with our market capitalization. Our impairment analysis indicated that the aggregate fair values of our reporting units exceeded our December 31, 2009 market capitalization by approximately \$3.9 billion or 26%.

The fair value of an entity can be greater than its market capitalization for various reasons, one of which is the concept of control premium. A control premium is the amount that a buyer is willing to pay over the current market price of a company to acquire a controlling interest. Substantial value may arise from the ability to take advantages of synergies, such as the expected increase in cash flow resulting from cost savings and revenue enhancements, and other benefits could be achieved by controlling another entity. However, changes in our assumptions underlying our estimates of fair value, which will be a function of our future financial performance and changes in economic conditions, could result in future impairment charges.

We test acquired trade names for possible impairment by using a discounted cash flow model to estimate fair value. As of December 31, 2009, the estimated fair values of each of our acquired trade names exceeded their carrying values by a range of approximately \$4 million to \$124 million, which exceeds their respective carrying values by a range of approximately 1% to 260%. As such, we have determined that no impairment has occurred at December 31, 2009 based upon a set of assumptions regarding discounted future cash flows, which represent our best estimate of future performance at this time. In determining the fair value of our trade names, we assumed a discount rate between 11.5% and 12%, and royalty saving rates of approximately 1%. A one percentage point increase in the discount rate would have reduced the indicated fair values of each of our acquired trade names by a range of approximately \$22 million to \$52 million, and would yield an impairment charge in the case of one of our trade names. Changes in our assumptions underlying our estimates of fair value, which will be a function of our future financial performance and changes in economic conditions, could result in future impairment charges.

Amortizable Intangible Assets. Intangible assets subject to amortization are carried at cost less accumulated amortization. Intangible assets subject to amortization are amortized over the estimated useful life in proportion to the economic benefits received.

Table of Contents

ACTIVISION BLIZZARD, INC. AND SUBSIDIARIES

Notes to Consolidated Financial Statements (Continued)

2. Summary of significant accounting policies (Continued)

Management evaluates the recoverability of our identifiable intangible assets and other long-lived assets in accordance with FASB guidance within ASC Subtopic 360-10, which generally requires the assessment of these assets for recoverability when events or circumstances indicate a potential impairment exists. We considered certain events and circumstances in determining whether the carrying value of identifiable intangible assets and other long-lived assets may not be recoverable including, but not limited to: significant changes in performance relative to expected operating results; significant changes in the use of the assets; significant negative industry or economic trends; a significant decline in our stock price for a sustained period of time; and changes in our business strategy. In determining whether an impairment exists, we estimate the undiscounted cash flows to be generated from the use and ultimate disposition of these assets. If an impairment is indicated based on a comparison of the assets' carrying values and the undiscounted cash flows, the impairment loss is measured as the amount by which the carrying amount of the assets exceeds the fair value of the assets.

During 2009, we recorded impairment charges of \$24 million, \$12 million and \$373 million to license agreements, game engines and internally developed franchises intangible assets, respectively (see Note 12).

Revenue Recognition

Product Sales

We recognize revenue from the sale of our products upon the transfer of title and risk of loss to our customers, and once any performance obligations have been completed. Certain products are sold to customers with a street date (the earliest date these products may be sold by retailers). For these products we recognize revenue on the later of the street date or the sale date. Revenue from product sales is recognized after deducting the estimated allowance for returns and price protection.

Some of our software products provide limited online features at no additional cost to the consumer. Generally, we consider such features to be incidental to the overall product offering and an inconsequential deliverable. Accordingly, we recognize revenue related to products containing these limited online features upon the transfer of title and risk of loss to our customer. In instances where online features or additional functionality is considered more than an inconsequential separate deliverable in addition to the software product, we take this into account when applying our revenue recognition policy. This evaluation is performed for each software product and any online transactions, such as electronic downloads of titles or product add-ons when it is released. When we determine that a software title contains online functionality that constitutes a more-than-inconsequential separate service deliverable in addition to the product, principally because of its importance to game play, we consider that our performance obligations for this title extend beyond the sale of the game. Vendor-specific objective evidence ("VSOE") of fair value does not exist for the online functionality, as we do not separately charge for this component of the title. As a result, we recognize all of the revenue from the sale of the title ratably over the estimated service period, which is estimated to begin the month after either the sale date or the street date of the title, whichever is later. In addition, we defer the costs of sales for the title (excluding intangible asset amortization) to match revenues. Cost of sales includes manufacturing costs, software royalties and amortization, and intellectual property licenses.

We recognize *World of Warcraft* boxed product, expansion packs and other value added service revenues each with the related subscription service revenue ratably over the estimated service periods beginning upon activation of the software and delivery of the services. Revenues attributed to the sale

Table of Contents

ACTIVISION BLIZZARD, INC. AND SUBSIDIARIES

Notes to Consolidated Financial Statements (Continued)

2. Summary of significant accounting policies (Continued)

of *World of Warcraft* boxed software and related expansion packs are classified as product sales and revenues attributable to subscription and other value added services are classified as subscription, licensing and other revenues.

We currently estimate the service periods over which revenues are recognized range from a minimum of five months to a maximum of less than a year.

With respect to online transactions, such as electronic downloads of titles or product add-ons that do not include a more-than-inconsequential separate service deliverable, revenue is recognized when the fee is paid by the online customer to purchase online content and the product is available for download. In addition, persuasive evidence of an arrangement must exist and collection of the related receivable must be probable.

Sales incentives and other consideration given by us to our customers are considered adjustments of the selling price of our products, such as rebates and product placement fees, and are reflected as reductions to revenue. Sales incentives and other consideration that represent costs incurred by us for assets or services received, such as the appearance of our products in a customer's national circular ad, are reflected as sales and marketing expenses when the benefit from the sales incentive is separable from sales to the same customer and we can reasonably estimate the fair value of the benefit.

Subscription Revenues

Subscription revenues are derived from *World of Warcraft*, a game that is playable through Blizzard's servers on a subscription-only basis. After the first month of free usage that is included with the *World of Warcraft* boxed software, the *World of Warcraft* end user may enter into a subscription agreement for additional future access. Revenues associated with the sale of subscriptions via packaged software and prepaid subscription cards, as well as prepaid subscriptions sales, are deferred until the subscription service is activated by the consumer and recognized ratably over the subscription period. Revenue from Internet gaming rooms in Asia is recognized upon usage of the time packages sold. Value added service revenues associated with subscriptions are recognized ratably over the estimated customer life.

Licensing Revenues

Third-party licensees in Russia, China and Taiwan distribute and host Blizzard's *World of Warcraft* game in their respective countries under license agreements with Blizzard. We receive royalties from the licensees as a result. We recognize these royalties as revenues based on the end users' activation of the underlying prepaid time, if all other performance obligations have been completed or based on usage by the end user when we have continuing service obligations. We recognize any upfront licensing fee received over the term of the contracts.

With respect to license agreements that provide customers the right to make multiple copies in exchange for guaranteed amounts, revenue is generally recognized upon delivery of a master copy. Per copy royalties on sales that exceed the guarantee are recognized as earned. In addition, persuasive evidence of an arrangement must exist and collection of the related receivable must be probable.

Table of Contents

ACTIVISION BLIZZARD, INC. AND SUBSIDIARIES

Notes to Consolidated Financial Statements (Continued)

2. Summary of significant accounting policies (Continued)

Breakage Revenues

World of Warcraft boxed product sales and subscription revenues are recognized upon activation of the game. For certain products, activation has not occurred, which led us to analyze historical activation patterns over an extended period of time, to determine when the likelihood of activation ever occurring becomes remote. We recognize revenues from subscriptions that have not yet been activated, prepaid subscription cards, as well as prepaid subscription sales, when the likelihood of future activation occurring is remote (defined as "breakage revenues"). In 2008, we recognized breakage revenues for the first time since the initial launch of *World of Warcraft*. For the years ended December 31, 2009 and 2008, we recorded \$5 million and \$6 million, respectively of breakage revenues from the sale of packaged software in product sales, and \$8 million and \$16 million, respectively of prepaid and subscription breakage revenues in subscription, licensing and other revenues in the consolidated statements of operations.

Other Revenues

Other revenues primarily include value added service sales of non-software related products. It includes licensing activity of intellectual property other than software to third-parties. Revenue is recorded upon receipt of licensee statements, or upon the receipt of cash, provided the license period has begun.

Allowances for Returns, Price Protection, Doubtful Accounts, and Inventory Obsolescence

We closely monitor and analyze the historical performance of our various titles, the performance of products released by other publishers, and the anticipated timing of other releases to assess future demand of current and upcoming titles. Initial volumes shipped upon title launch and subsequent reorders are evaluated with the goal of ensuring that quantities are sufficient to meet the demand from the retail markets, but at the same time are controlled to prevent excess inventory in the channel. We benchmark units to be shipped to our customers using historical and industry data.

We may permit product returns from, or grant price protection to, our customers under certain conditions. In general, price protection refers to the circumstances in which we elect to decrease the wholesale price of a product by a certain amount and, when granted and applicable, allows customers a credit against amounts owed by such customers to us with respect to open and/or future invoices. The conditions our customers must meet to be granted the right to return products or price protection include, among other things, compliance with applicable trading and payment terms, and consistent return of inventory and delivery of sell-through reports to us. We may also consider other factors, including the facilitation of slow-moving inventory and other market factors. Management must make estimates of potential future product returns and price protection related to current period product revenue. We estimate the amount of future returns and price protection for current period product revenue utilizing historical experience and information regarding inventory levels and the demand and acceptance of our products by the end consumer. The following factors are used to estimate the amount of future returns and price protection for a particular title: historical performance of titles in similar genres; historical performance of the hardware platform; historical performance of the franchise; console hardware life cycle; sales force and retail customer feedback; industry pricing; weeks of on-hand retail channel inventory; absolute quantity of on-hand retail channel inventory; our warehouse on-hand inventory levels; the title's recent sell-through history (if available); marketing trade

Table of Contents

ACTIVISION BLIZZARD, INC. AND SUBSIDIARIES

Notes to Consolidated Financial Statements (Continued)

2. Summary of significant accounting policies (Continued)

programs; and competing titles. The relative importance of these factors varies among titles depending upon, among other items, genre, platform, seasonality, and sales strategy. Significant management judgments and estimates must be made and used in connection with establishing the allowance for returns and price protection in any accounting period. Based upon historical experience, we believe that our estimates are reasonable. However, actual returns and price protection could vary materially from our allowance estimates due to a number of reasons including, among others, a lack of consumer acceptance of a title, the release in the same period of a similarly themed title by a competitor, or technological obsolescence due to the emergence of new hardware platforms. Material differences may result in the amount and timing of our revenue for any period if factors or market conditions change or if management makes different judgments or utilizes different estimates in determining the allowances for returns and price protection. For example, a 1% change in our December 31, 2009 allowance for returns and price protection would impact net revenues by approximately \$3 million.

Similarly, management must make estimates of the uncollectibility of our accounts receivable. In estimating the allowance for doubtful accounts, we analyze the age of current outstanding account balances, historical bad debts, customer concentrations, customer creditworthiness, current economic trends, and changes in our customers' payment terms and their economic condition, as well as whether we can obtain sufficient credit insurance. Any significant changes in any of these criteria would affect management's estimates in establishing our allowance for doubtful accounts.

We regularly review inventory quantities on-hand and in the retail channel. We write down inventory based on excess or obsolete inventories determined primarily by future anticipated demand for our products. Inventory write-downs are measured as the difference between the cost of the inventory and net realizable value, based upon assumptions about future demand, which are inherently difficult to assess. At the point of a loss recognition, a new, lower cost basis for that inventory is established, and subsequent changes in facts and circumstances do not result in the restoration or increase in that newly established basis.

Shipping and Handling

Shipping and handling costs, which consist primarily of packaging and transportation charges incurred to move finished goods to customers, are included in "cost of sales product costs."

Advertising Expenses

We expense advertising as incurred, except for production costs associated with media advertising which are deferred and charged to expense the first time the related ad is run. Advertising expenses for the years ended December 31, 2009, 2008, and 2007 were \$366 million, \$241 million, and \$73 million, respectively, and are included in sales and marketing expense in the consolidated statements of operations.

Income Taxes

We account for income taxes using ASC Topic 740, *Income Taxes*. Under ASC Topic 740, income taxes are accounted for under the asset and liability method. Deferred tax assets and liabilities are recognized for the future tax consequences attributable to differences between the financial statement carrying amounts of existing assets and liabilities and their respective tax bases and operating loss and tax credit carryforwards. Deferred tax assets and liabilities are measured using enacted tax rates

Table of Contents

ACTIVISION BLIZZARD, INC. AND SUBSIDIARIES

Notes to Consolidated Financial Statements (Continued)

2. Summary of significant accounting policies (Continued)

expected to apply to taxable income in the years in which those temporary differences are expected to be recovered or settled. The effect on deferred tax assets and liabilities of a change in tax rates is recognized in income in the period that includes the enactment date.

ASC Topic 740 includes accounting guidance which clarifies the accounting for the uncertainty in recognizing income taxes in an organization by providing detailed guidance for financial statement recognition, measurement and disclosure involving uncertain tax positions. This guidance requires an uncertain tax position to meet a more-likely-than-not recognition threshold at the effective date to be recognized both upon the adoption of the related guidance and in subsequent periods.

Foreign Currency Translation

All assets and liabilities of our foreign subsidiaries are translated into U.S. dollars at the exchange rate in effect at the balance sheet date, and revenue and expenses are translated at average exchange rates during the period. The resulting translation adjustments are reflected as a component of accumulated other comprehensive income (loss) in shareholders' equity.

Earnings (Loss) Per Common Share

Basic earnings (loss) per common share is computed by dividing income (loss) available to common shareholders by the weighted average number of common shares outstanding for the periods presented. Diluted earnings per share is computed by dividing income (loss) available to common shareholders by the weighted average number of common shares outstanding, increased by the weighted average number of common stock equivalents. Common stock equivalents are calculated using the treasury stock method and represent incremental shares issuable upon exercise of our outstanding options. However, potential common shares are not included in the denominator of the diluted earnings per share calculation when inclusion of such shares would be anti-dilutive, such as in a period in which a net loss is recorded. Earnings (loss) per common share for periods prior to the Business Combination are retrospectively adjusted to reflect the number of split adjusted shares received by Vivendi, former parent company of Vivendi Games.

On January 1, 2009, we adopted the new accounting guidance for determining whether instruments granted in share-based payment transactions are participating securities, and as a result, unvested share-based awards which include the right to receive non-forfeitable dividends or dividend equivalents are considered to participate with common stock in undistributed earnings. Companies that issue share-based awards considered to be participating securities are required to calculate basic and diluted earnings per common share amounts under the two-class method. The two-class method excludes from earnings per common share calculations any dividends paid or owed to participating securities and any undistributed earnings considered to be attributable to participating securities. The accounting guidance requires retrospective application to all prior-period earnings per share data presented. The adoption of the accounting guidance did not change our basic or diluted earnings per common share for the years ended December 31, 2008 and 2007.

Stock-Based Compensation

We account for stock-based compensation in accordance with ASC Topic 718-10, *Compensation-Stock Compensation* and ASC Subtopic 505-50, *Equity-Based Payments to Non-Employees* ("ASC stock-based compensation guidance"). Stock-based compensation expense recognized during the requisite

Table of Contents

ACTIVISION BLIZZARD, INC. AND SUBSIDIARIES

Notes to Consolidated Financial Statements (Continued)

2. Summary of significant accounting policies (Continued)

services period is based on the value of share-based payment awards after reduction for estimated forfeitures. Forfeitures are estimated at the time of grant and are revised, if necessary, in subsequent periods if actual forfeitures differ from those estimates. Stock-based compensation expense recognized in our consolidated statement of operations for the years ended December 31, 2009 and 2008 included compensation expense for share-based payment awards granted by Activision, Inc. prior to, but not yet vested as of July 9, 2008, based on the revalued fair value estimated at July 9, 2008, and compensation expense for the share-based payment awards granted subsequent to July 9, 2008.

We estimate the value of share-based payment awards on the measurement date using a binomial-lattice model. Our determination of fair value of share-based payment awards on the date of grant using an option-pricing model is affected by our stock price as well as assumptions regarding a number of highly complex and subjective variables. These variables include, but are not limited to, our expected stock price volatility over the term of the awards, and actual and projected employee stock option exercise behaviors.

Prior to the Business Combination, Vivendi Games had equity incentive plans that were equity-settled and cash-settled. Vivendi Games used a binomial model to assess the value of these equity incentive awards. Equity-settled awards include stock options and restricted shares granted by Vivendi, and the cash-settled awards include stock appreciation rights and restricted stock units granted by both Vivendi and under the Blizzard Equity Plan ("BEP"). The Company records a liability and recognizes changes in fair value of the liability that occur during the period as compensation cost over the requisite service period. Changes in the fair value of the liability that occur after the end of the requisite service period are compensation cost of the period in which the change occurs. Any differences between the amount for which the liability is settled and its fair value at the settlement date as estimated is an adjustment of compensation cost in the period of settlement. See Note 19 of the notes to consolidated financial statements.

3. Acquisitions

Reverse Acquisition

The Business Combination (See Note 1 of the notes to consolidated financial statements) is accounted for as a reverse acquisition under the purchase method of accounting. For this purpose, Vivendi Games was deemed to be the accounting acquirer and Activision, Inc. was deemed to be the accounting acquiree.

Table of Contents**ACTIVISION BLIZZARD, INC. AND SUBSIDIARIES****Notes to Consolidated Financial Statements (Continued)****3. Acquisitions (Continued)**

The purchase price of Activision, Inc. consists of the following items (amounts in millions):

Fair market value of Activision, Inc.'s outstanding common stock immediately prior to the Business Combination at the closing price	\$ 9,057
Fair value of Activision, Inc.'s existing vested and unvested stock awards at the closing price*	861
Transaction expenses	1
 Total consideration	 \$ 9,919

*

The fair value of the existing vested and unvested stock award is comprised of the following (amounts in millions):

Fair value of Activision, Inc. existing vested stock awards	\$ 713
Fair value of Activision, Inc. unvested stock awards	296
Less: Unearned stock-based compensation	(148)
	\$ 861

The fair value of Activision, Inc.'s stock awards was determined using the fair value of Activision, Inc.'s common stock of \$15.04 per share, which was the closing price at July 9, 2008, and using a binomial-lattice model and the following assumptions: (a) varying volatility ranging from 42.38% to 51.50%, (b) a risk free interest rate of 3.97%, (c) an expected life ranging from 3.22 years to 4.71 years, (d) risk adjusted stock return of 8.89%, and (e) an expected dividend yield of 0.0%.

The Company's allocation of the purchase price of Activision, Inc. is as follows (amounts in millions):

	Amount
Working capital, excluding inventories	\$ 1,192
Inventories	221
Property and equipment	64
Deferred tax asset	62
Other long term assets	129
	F-22

Table of Contents**ACTIVISION BLIZZARD, INC. AND SUBSIDIARIES****Notes to Consolidated Financial Statements (Continued)****3. Acquisitions (Continued)**

	Estimated useful life	
Intangible assets:		
License agreements	3 - 10 years	207
Developed software	1 - 2 years	68
Game engines	2 - 5 years	128
Internally developed franchises	11 - 12 years	1,124
Retail customer relationships	< 1 year	40
Favorable leases	1 - 4 years	5
Distribution agreements	4 years	17
Activision trade name	Indefinite	385
Goodwill	Indefinite	7,044
Long term liabilities		(24)
Deferred tax liability		(743)
Total consideration		\$ 9,919

Goodwill arises from the Business Combination due to the acquired work force of Activision, Inc., and the expected synergies from the Business Combination.

The following table summarizes unaudited pro forma financial information assuming the Business Combination had occurred at the beginning of the periods presented. This pro forma financial information is for informational purposes only and does not reflect any operating efficiencies or inefficiencies which may result from the Business Combination and therefore is not necessarily indicative of results that would have been achieved had the businesses been combined during the periods presented (amounts in millions, except per share data):

	For the years ended December 31,	
	2008	2007
Pro forma net revenues	\$ 4,336	\$ 3,957
Pro forma net income (loss)	(111)	260
Pro forma net income (loss) per share		
- basic	(0.08)	0.20
- diluted	(0.08)	0.19

Comparative Period Following the consummation of the Business Combination, the historical financial statements of Activision Blizzard for periods prior to the consummation of the Business Combination are those of Vivendi Games. Activision, Inc.'s businesses were included in Activision Blizzard's financial statements for all periods subsequent to the consummation of the Business Combination only.

The historical financial statements of Vivendi Games comprised Vivendi Games, Inc. and its subsidiaries, as well as Universal Interactive, Inc. ("UI"), which had historically been under the common control of Vivendi. During 2006, Vivendi transferred UI to Vivendi Games, at which time UI became a wholly-owned subsidiary of Vivendi Games.

Table of Contents**ACTIVISION BLIZZARD, INC. AND SUBSIDIARIES****Notes to Consolidated Financial Statements (Continued)****3. Acquisitions (Continued)**

Vivendi Games' shareholders' equity represents the difference between the identifiable assets and liabilities of these entities under Vivendi Games' control and includes the net transfers between Vivendi Games and Vivendi and Vivendi's affiliated companies, under a cash management pool agreement. The consolidated statements of operations and consolidated statements of changes in shareholders' equity include certain expenses for corporate services and overhead that are allocated from or to Vivendi and its affiliated companies (see Note 23 of the notes to consolidated financial statements). These expenses have been allocated based on the specific nature of the expense and/or a formula, which management believes reasonably allocates expenses to or from Vivendi Games; however, such amounts may have been different had Vivendi Games operated as a separate stand-alone entity during periods presented.

2008 Acquisitions

On September 11, 2008, we completed an acquisition of Freestyle Games, Ltd. ("Freestyle"), a premier United Kingdom based video game developer specializing in the music based genre. Additionally, on November 10, 2008, we acquired Budcat Creations, LLC ("Budcat"), a privately-owned video game developer based in Iowa City, Iowa. Budcat is an award-winning development studio with expertise on the Wii and NDS. Pro forma consolidated statements of operations for these acquisitions are not shown, as they would not differ materially from reported results.

4. Investment and other income (loss), net

Investment and other income (loss), net is comprised of the following (amounts in millions):

	For the years ended December 31,		
	2009	2008	2007
Interest income	\$ 15	\$ 36	\$ 1
Interest expense	(4)	(3)	(3)
Unrealized gain (loss) on trading securities	3	(7)	
Unrealized gain (loss) on ARS rights from UBS	(3)	10	
Net realized gain on investments		4	
Change in fair value of other financial liability	8		
Net realized and unrealized gain (loss) on foreign exchange contracts with Vivendi	(1)	6	(2)
Investment and other income (loss), net	\$ 18	\$ 46	\$ (4)

5. Cash and Cash Equivalents

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

Table of Contents**ACTIVISION BLIZZARD, INC. AND SUBSIDIARIES****Notes to Consolidated Financial Statements (Continued)****5. Cash and Cash Equivalents (Continued)**

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

	At December 31,	
	2009	2008
Cash and time deposits	\$ 464	\$ 349
Money market funds	2,304	2,609
Total cash and cash equivalents	\$ 2,768	\$ 2,958

6. Investments

The following table summarizes our short-term and long-term investments at December 31, 2009 (amounts in millions):

At December 31, 2009	Amortized cost	Gross unrealized gains	Gross unrealized losses	Fair value
Short-term investments:				
Available-for-sale investments:				
Mortgage-backed securities	\$ 2	\$	\$	\$ 2
U.S. government agency securities	389			389
Total short-term available-for-sale investments	\$ 391	\$	\$	391
Trading investments:				
Auction rate securities held through UBS				54
Restricted cash				32
Total short-term investments				\$ 477
Long-term investments:				
Available-for-sale investments:				
Auction rate securities held through Morgan Stanley Smith Barney LLC	\$ 27	\$	\$ (4)	\$ 23

Table of Contents**ACTIVISION BLIZZARD, INC. AND SUBSIDIARIES****Notes to Consolidated Financial Statements (Continued)****6. Investments (Continued)**

	Amortized cost	Gross unrealized gains	Gross unrealized losses	Fair value
At December 31, 2008				
Short-term investments:				
Available-for-sale investments:				
Mortgage-backed securities	\$ 8	\$	\$ (1)	\$ 7
Total short-term available-for-sale investments	\$ 8	\$	\$ (1)	\$ 7
Restricted cash				37
Total short-term investments				\$ 44
Long-term investments:				
Available-for-sale investments:				
Auction rate securities held through Citigroup, Inc.	\$ 27	\$	\$ (4)	\$ 23
Trading investments:				
Auction rate securities held through UBS				55
Total long-term investments				\$ 78

The following table illustrates the gross unrealized losses on available-for-sale securities and the fair value of those securities, aggregated by investment categories at December 31, 2009 and 2008. The table also illustrates the length of time that they have been in a continuous unrealized loss position at December 31, 2009 and 2008 (amounts in millions):

	Less than 12 months		12 months or more		Total	
At December 31, 2009	Unrealized losses	Fair value	Unrealized losses	Fair value	Unrealized losses	Fair value
Taxable auction rate securities	\$	\$	\$ (4)	\$ 23	\$ (4)	\$ 23

	Less than 12 months		12 months or more		Total	
At December 31, 2008	Unrealized losses	Fair value	Unrealized losses	Fair value	Unrealized losses	Fair value
Mortgage-backed securities	\$ (1)	\$ 7	\$	\$	\$ (1)	\$ 7
Taxable auction rate securities	(4)	23			(4)	23
Total	\$ (5)	\$ 30	\$	\$	\$ (5)	\$ 30

The total unrealized loss of \$4 million at December 31, 2009 is due to failed auctions of taxable ARS held through Morgan Stanley Smith Barney LLC, which is 51% owned by Morgan Stanley and 49% owned by Citigroup, Inc. The ARS were held directly through a wholly owned subsidiary of Citigroup, Inc. until the Morgan Stanley Smith Barney LLC joint-venture closed in the second quarter 2009. Our investments in ARS are all backed by higher education student loans.

Table of Contents**ACTIVISION BLIZZARD, INC. AND SUBSIDIARIES****Notes to Consolidated Financial Statements (Continued)****6. Investments (Continued)**

Based upon our analysis of the available-for-sale investments with unrealized losses, we have concluded that the gross unrealized losses of \$4 million at December 31, 2009 were temporary in nature. We do not intend to sell the investment securities that are in an unrealized loss position and do not consider that it is more-likely-than-not that we will be required to sell the investment securities before recovery of their amortized cost basis, which may be maturity. We have not identified any issues related to the ultimate repayment of principal as a result of credit concerns on these securities. However, facts and circumstances may change which could result in a decline in fair value considered to be other-than-temporary in the future.

The following table summarizes the contractually stated maturities of our short- and long-term investments classified as available-for-sale at December 31, 2009 (amounts in millions):

At December 31, 2009	Amortized cost	Fair value
U.S. government agency securities due in 1 year or less	\$ 389	\$ 389
Due after ten years	29	25
	\$ 418	\$ 414

Trading Investments

We continue to monitor the ARS market and consider its impact (if any) on the fair value of our ARS held through UBS. If the market conditions deteriorate further, we may be required to record additional unrealized losses in earnings, which may be offset by corresponding increases in value of the UBS arrangement.

In 2008, prior to accepting the UBS offer (see Note 2 of the notes to consolidated financial statements), we classified our investment in ARS held through UBS as available-for-sale. We recorded unrealized gains and losses on our available-for-sale securities, net of tax, in accumulated other comprehensive income (loss) in the shareholders' equity section of our consolidated balance sheets. The unrealized loss did not reduce net income for the applicable accounting period.

In connection with our acceptance of the UBS offer in November 2008, resulting in our right to require UBS to purchase our ARS at par value beginning on June 30, 2010, we transferred our investments in ARS held through UBS from available-for-sale to trading securities. The transfer to trading securities reflects management's intent to exercise the Rights during the period between June 30, 2010 and July 3, 2012, which results in the securities being held for the purpose of selling them in the near future. Prior to our agreement with UBS, our intent was to hold the ARS until the market recovered. At the time of transfer, the unrealized loss on our ARS was \$5 million. This unrealized loss was included in accumulated other comprehensive income (loss). Upon transfer to trading securities, we immediately recognized in investment income, net, the \$5 million unrealized loss not previously recognized in earnings. Subsequently, we recognized an additional decline in fair value of \$2 million for a total unrealized loss of \$7 million, included in investment and other income (loss), net, in the consolidated statements of operations for the year ended December 31, 2008.

Table of Contents**ACTIVISION BLIZZARD, INC. AND SUBSIDIARIES****Notes to Consolidated Financial Statements (Continued)****7. Software Development Costs and Intellectual Property Licenses**

At December 31, 2009, capitalized software development costs included \$182 million of internally developed software costs and \$52 million of payments made to third-party software developers. At December 31, 2008, capitalized software development costs included \$173 million of internally developed software costs and \$63 million of payments made to third-party software developers. Capitalized intellectual property licenses were \$83 million and \$40 million at December 31, 2009 and December 31, 2008, respectively. Amortization of capitalized software development costs and intellectual property licenses for the years ended December 31, 2009, 2008 and 2007 were \$314 million, \$90 million and \$10 million, respectively. Write-offs and impairments were \$21 million, \$89 million and \$7 million for the years ended December 31, 2009, 2008 and 2007, respectively.

8. Restructuring

We have substantially completed our implementation of our organizational restructuring plan as a result of the Business Combination described in Note 1 of the notes to consolidated financial statements. This organizational restructuring plan included the integration of different operations to streamline the combined organization of Activision Blizzard.

The primary goals of the organizational restructuring are to rationalize the title portfolio and consolidate certain corporate functions to realize synergies from the Business Combination.

The following table details the amount of restructuring reserves included in accrued expenses and other liabilities in the consolidated balance sheets at December 31, 2009 and 2008 (amounts in millions):

	Severance	Facilities costs	Asset write-down	Contract termination costs	Loss on disposal of assets/liabilities	Total
Balance at December 31, 2007	\$	\$	\$	\$	\$	\$
Costs charged to expense	54	7	26	5	1	93
Costs paid or otherwise settled	(18)			(3)		(21)
Non-cash write-down:						
Fixed asset disposals			(5)			(5)
Impairment of acquired trade name			(5)			(5)
Impairment of goodwill			(16)			(16)
Foreign exchange and other	1			(2)	(1)	(2)
Balance at December 31, 2008	37	7				44
Costs charged to expense	19	4				23
Costs paid or otherwise settled	(48)	(8)				(56)
Foreign exchange and other		(2)				(2)
Balance at December 31, 2009	\$ 8	\$ 1	\$	\$	\$	\$ 9

Table of Contents**ACTIVISION BLIZZARD, INC. AND SUBSIDIARIES****Notes to Consolidated Financial Statements (Continued)****8. Restructuring (Continued)**

The total restructuring reserve balances and the net restructuring charges are presented below by operating segment (amounts in millions):

	Restructuring Reserve Balance		Restructuring Charges	
	At December 31, 2009	At December 31, 2008	Year ended December 31, 2009	Year ended December 31, 2008
Activision	\$ 9	\$	\$ 2	\$ 2
Blizzard				
Distribution			3	
Total operating segments	9		5	2
Other(i)		44	18	91
Total	\$ 9	\$ 44	\$ 23	\$ 93

(i)

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

9. Inventories

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

	At December 31,	
	2009	2008
Finished goods	\$ 201	\$ 251
Purchased parts and components	40	11
	\$ 241	\$ 262

Table of Contents**ACTIVISION BLIZZARD, INC. AND SUBSIDIARIES****Notes to Consolidated Financial Statements (Continued)****10. Property and Equipment, Net**

Property and equipment, net was comprised of the following (amounts in millions):

	At December 31,	
	2009	2008
Land	\$ 1	\$ 1
Buildings	6	5
Leasehold improvements	54	45
Computer equipment	311	293
Office furniture and other equipment	65	52
 Total cost of property and equipment	 437	 396
Less accumulated depreciation	(299)	(247)
 Property and equipment, net	 \$ 138	 \$ 149

Depreciation expense for the years ended December 31, 2009, 2008, and 2007 was \$76 million, \$79 million, and \$59 million, respectively.

11. Goodwill

The changes in the carrying amount of goodwill by operating segments for the years ended December 31, 2009 and 2008 are as follows (amounts in millions):

	Activision	Blizzard	Distribution	Activision Blizzard's core operations	Other(i)	Total
Balance at December 31, 2007	\$	\$ 178	\$	\$ 178	\$ 25	\$ 203
Goodwill acquired	7,043		12	7,055		7,055
Issuance of contingent consideration	9			9	6	15
Goodwill re-assignment	7			7	(7)	
Disposal					(8)	(8)
Impairment charge					(16)	(16)
Tax benefit credited to goodwill	(19)			(19)		(19)
Foreign exchange	(3)			(3)		(3)
 Balance at December 31, 2008	 7,037	 178	 12	 7,227		 7,227
Goodwill acquired	3			3		3
Issuance of contingent consideration	6			6		6
Purchase accounting adjustments	(6)			(6)		(6)
Tax benefit credited to goodwill	(78)			(78)		(78)
Foreign exchange	2			2		2
 Balance at December 31, 2009	 \$ 6,964	 \$ 178	 \$ 12	 \$ 7,154	 \$	 \$ 7,154

Table of Contents**ACTIVISION BLIZZARD, INC. AND SUBSIDIARIES****Notes to Consolidated Financial Statements (Continued)****11. Goodwill (Continued)**

	Activision	Blizzard	Distribution	Activision Blizzard's core operations	Other(i)	Total
Balance at December 31, 2007:						
Goodwill	\$	\$ 178	\$	\$ 178	\$ 27	\$ 205
Accumulated impairment losses					(2)	(2)
Total		178		178	25	203
Balance at December 31, 2008:						
Goodwill	7,037	178	12	7,227	18	7,245
Accumulated impairment losses					(18)	(18)
Total	7,037	178	12	7,227		7,227
Balance at December 31, 2009:						
Goodwill	6,964	178	12	7,154	18	7,172
Accumulated impairment losses					(18)	(18)
Total	\$ 6,964	\$ 178	\$ 12	\$ 7,154	\$	\$ 7,154

(i)

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

Issuance of contingent consideration consists of additional purchase consideration paid or accrued during 2009 and 2008 in relation to previous acquisitions. The tax benefit credited to goodwill represents the tax deduction resulting from the exercise of stock options that were outstanding and vested at the consummation of the Business Combination and included in the purchase price of Activision, Inc. to the extent that the tax deduction did not exceed the fair value of those options. Conversely, to the extent that the tax deduction did exceed the fair value of those options, the tax benefit is credited to accumulated paid in capital.

Table of Contents**ACTIVISION BLIZZARD, INC. AND SUBSIDIARIES****Notes to Consolidated Financial Statements (Continued)****12. Intangible Assets, Net**

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

At December 31, 2009					
	Estimated useful lives	Gross carrying amount	Accumulated amortization	Impairment charge	Net carrying amount
Acquired definite-lived intangible assets:					
License agreements	3 - 10 years	\$ 209	\$ (77)	\$ (24)	\$ 108
Developed software	1 - 2 years	288	(288)		
Game engines	2 - 5 years	134	(94)	(12)	28
Internally developed franchises	11 - 12 years	1,124	(278)	(373)	473
Favorable leases	1 - 4 years	5	(4)		1
Distribution agreements	4 years	18	(10)		8
Other intangibles	0 - 2 years	5	(5)		
Acquired indefinite-lived intangible assets:					
Activision trademark	Indefinite	386			386
Acquired trade names	Indefinite	47			47
Total		\$ 2,216	\$ (756)	\$ (409)	\$ 1,051

At December 31, 2008					
	Estimated useful lives	Gross carrying amount	Accumulated amortization	Impairment charge (See Note 8)	Net carrying amount
Acquired definite-lived intangible assets:					
License agreements	3 - 10 years	\$ 207	\$ (34)	\$	\$ 173
Developed software	1 - 2 years	286	(272)		14
Game engines	2 - 5 years	134	(42)		92
Internally developed franchises	11 - 12 years	1,124	(123)		1,001
Favorable leases	1 - 4 years	5	(1)		4
Distribution agreements	4 years	17	(5)		12
Other intangibles	0 - 2 years	5	(4)		1
Acquired indefinite-lived intangible assets:					
Activision trademark	Indefinite	386			386
Acquired trade names	Indefinite	52		(5)	47
Total		\$ 2,216	\$ (481)	\$ (5)	\$ 1,730

Amortization expense of intangible assets was \$271 million, \$306 million, and \$4 million for the years ended December 31, 2009, 2008, and 2007, respectively.

Table of Contents**ACTIVISION BLIZZARD, INC. AND SUBSIDIARIES****Notes to Consolidated Financial Statements (Continued)****12. Intangible Assets, Net (Continued)**

At December 31, 2009, future amortization of finite-lived intangible assets is estimated as follows (amounts in millions):

2010	\$ 117
2011	98
2012	88
2013	62
2014	54
Thereafter	199
Total	\$ 618

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

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

[Table of Contents](#)**ACTIVISION BLIZZARD, INC. AND SUBSIDIARIES****Notes to Consolidated Financial Statements (Continued)****13. Current Accrued Expenses and Other Liabilities**

Current accrued expenses and other liabilities were comprised of the following (amounts in millions):

	At December 31,	
	2009	2008
Accrued royalties payable	\$ 64	\$ 88
Accrued selling and marketing costs	128	128
Current income tax payable		136
Accrued payroll related costs	271	208
Other	316	282
Total current accrued expenses and other liabilities	\$ 779	\$ 842

14. Operating Segments and Geographic Area

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

Currently, we operate under three operating segments: (i) Activision, which publishes interactive entertainment software and peripherals, and which includes businesses operated by Activision Publishing, Inc. prior to the Business Combination and studios, assets, and titles previously included in Vivendi Games' Sierra Entertainment operating segment prior to the Business Combination, (ii) Blizzard, which publishes real-time strategy, role-playing PC games and online subscription-based games in the MMORPG category, and (iii) Distribution, which distributes interactive entertainment software and hardware products.

Prior to July 1, 2009 we operated a fourth operating segment, Non-Core, which represented legacy Vivendi Games' divisions or business units that the Company had exited, divested, or wound down as part of its restructuring and integration efforts as a result of the Business Combination. At July 1, 2009 in light of the minimal activities and insignificance of Non-Core activities, we ceased management of Non-Core as a separate operating segment and consequently we are no longer providing separate operating segment disclosure with respect to Non-Core and have reclassified our prior periods' segment presentation so that it conforms to the current period's presentation.

As the historical financial statements prior to July 10, 2008 are those of Vivendi Games, segment net revenues and segment income (loss) from the business operated by Activision, Inc. prior to the Business Combination are not included for the period January 1, 2008 through July 9, 2008. Also, the Activision operating segment includes Vivendi Games titles retained after the Business Combination.

The CODM reviews segment performance exclusive of the impact of the deferred net revenues and related cost of sales, stock-based compensation expense, restructuring income (expense), amortization of intangible assets and purchase price accounting related adjustments, impairment of intangible assets, integration and transaction costs, and other*. Information on the operating segments and reconciliations of total net revenues and total segment income (loss) from operations to

Table of Contents**ACTIVISION BLIZZARD, INC. AND SUBSIDIARIES****Notes to Consolidated Financial Statements (Continued)****14. Operating Segments and Geographic Area (Continued)**

consolidated net revenues and operating income (loss) for the years ended December 31, 2009, 2008, and 2007 are presented below (amounts in millions):

	For the years ended December 31,			For the years ended December 31,		
	2009	2008	2007	2009	2008	2007
	Net revenues			Income (loss) from operations		
Activision	\$ 3,156	\$ 2,152	\$ 272	\$ 663	\$ 307	\$ (13)
Blizzard	1,196	1,343	1,107	555	704	568
Distribution	423	227		16	22	
Operating segments total	4,775	3,722	1,379	1,234	1,033	555
Reconciliation to consolidated net revenues / operating income (loss):						
Net effect from deferral of net revenues and related cost of sales	(497)	(713)	(40)	(383)	(496)	(38)
Stock-based compensation expense				(154)	(90)	(137)
Restructuring income (expense)				(23)	(93)	1
Amortization of intangible assets and purchase price accounting related adjustments				(259)	(292)	(4)
Impairment of intangible assets				(409)		
Integration and transaction costs				(24)	(29)	
Other*	1	17	10	(8)	(266)	(198)
Consolidated net revenues / operating income (loss)	\$ 4,279	\$ 3,026	\$ 1,349	\$ (26)	\$ (233)	\$ 179

Geographic information for the years ended December 31, 2009, 2008, and 2007 is based on the location of the selling entity. Net revenues from external customers by geographic areas were as follows (amounts in millions):

	For the years ended December 31,		
	2009	2008	2007
North America	\$ 2,217	\$ 1,494	\$ 620
Europe	1,798	1,288	555
Asia Pacific	263	227	164
Total geographic area net revenues	4,278	3,009	1,339
Other*	1	17	10
Total consolidated net revenues	\$ 4,279	\$ 3,026	\$ 1,349

Table of Contents**ACTIVISION BLIZZARD, INC. AND SUBSIDIARIES****Notes to Consolidated Financial Statements (Continued)****14. Operating Segments and Geographic Area (Continued)**

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

	For the years ended December 31,		
	2009	2008	2007
MMORPG	\$ 1,248	\$ 1,152	\$ 1,024
Console	2,199	1,294	156
Handheld	244	237	65
PC and other	164	99	94
Total platforms revenues	3,855	2,782	1,339
Distribution	423	227	
Other*	1	17	10

Total consolidated net revenues	\$ 4,279	\$ 3,026	\$ 1,349
---------------------------------	----------	----------	----------

*

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

See "Concentration of Credit Risk" in Note 2 of the notes to consolidated financial statements for information regarding significant customers.

Table of Contents**ACTIVISION BLIZZARD, INC. AND SUBSIDIARIES****Notes to Consolidated Financial Statements (Continued)****15. Computation of Earnings (Loss) Per Basic/Diluted Common Share**

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

	For the Years ended December 31,		
	2009	2008	2007
Numerator:			
Consolidated net income (loss)	\$ 113	\$ (107)	\$ 227
Net income allocated to unvested share-based awards that participate in earnings	(1)		
Numerator for basic and diluted earnings per common share income (loss) available to common shareholders	\$ 112	\$ (107)	\$ 227
Denominator:			
Denominator for basic earnings per common share weighted-average common shares outstanding	1,283	946	591
Effect of potential dilutive common shares under treasury stock method:			
Employee stock options	28		
Denominator for diluted earnings per common share weighted-average common shares outstanding plus potential dilutive effect of employee stock options	1,311	946	591
Basic earnings (loss) per common share	\$ 0.09	\$ (0.11)	\$ 0.38
Diluted earnings (loss) per common share	\$ 0.09	\$ (0.11)	\$ 0.38

Our unvested restricted stock rights (including restricted stock units, restricted stock awards, and performance shares) are considered participating securities since these securities have non-forfeitable rights to dividends or dividend equivalents during the contractual period of the award. Since the unvested restricted stock rights are considered participating securities, we are required to use the two-class method in our computation of basic and diluted net earnings per common share. For the year ended December 31, 2009, we had outstanding unvested restricted stock rights with respect to 10 million shares of common stock on a weighted-average basis.

According to the terms of our restricted stock plans, our unvested restricted stock rights do not participate with common stock in undistributed losses. Therefore, the two-class method in our computation of basic and diluted net earnings per common share for the year ended December 31, 2008 does not apply as there were losses during this period.

Edgar Filing: Activision Blizzard, Inc. - Form 10-K

In July 2008, the Board of Directors approved a two-for-one split of our outstanding common stock effected in the form of a stock dividend ("the split"). The split was paid September 5, 2008 to shareholders of record as of August 25, 2008. The par value of our common stock was maintained at the pre-split amount of \$.000001 per share. The consolidated financial statements and Notes thereto, including all share and per share data, have been restated as if the split had occurred as of the earliest period presented.

On July 9, 2008, Vivendi obtained control of Activision, Inc. through acquisition of the majority of the outstanding common stock of Activision, Inc. For accounting purposes, Vivendi Games is deemed

F-37

Table of Contents

ACTIVISION BLIZZARD, INC. AND SUBSIDIARIES

Notes to Consolidated Financial Statements (Continued)

15. Computation of Earnings (Loss) Per Basic/Diluted Common Share (Continued)

to be the acquirer (as the transaction was a "reverse acquisition" see Note 1 of the notes to consolidated financial statements). As such, the historical financial statements prior to July 10, 2008, are those of Vivendi Games. Further, earnings per common share for periods prior to the Business Combination are retrospectively adjusted to reflect the number of split adjusted shares received by Vivendi, the former parent of Vivendi Games.

Potential common shares are not included in the denominator of the diluted earnings per common share calculation when inclusion of such shares would be anti-dilutive. Therefore, options to acquire 20 million and 40 million shares of common stock were not included in the calculation of diluted earnings per common share for the years ended December 31, 2009 and 2008, respectively, as the effect of their inclusion would be anti-dilutive.

16. Income Taxes

Through July 9, 2008, Vivendi Games' results were included in the consolidated federal and certain foreign, state and local income tax returns filed by Vivendi or its affiliates. However, the income tax provision is reflected in our consolidated statements of operations, including the impact of U.S. net operating losses carried forward, as if the amounts were computed on a separate stand-alone basis.

Under Vivendi group policy, any U.S. net operating losses generated by Vivendi Games were surrendered to Vivendi or Vivendi's subsidiaries in the year of loss with no benefit for such losses being recorded in Vivendi Games' income tax provision. Vivendi Games' remaining separate U.S. net operating loss carry forward tax benefit of \$79 million was recognized in 2007 through a reduction in the valuation allowance.

Table of Contents**ACTIVISION BLIZZARD, INC. AND SUBSIDIARIES****Notes to Consolidated Financial Statements (Continued)****16. Income Taxes (Continued)**

Domestic and foreign income before income taxes and details of the income tax expense (benefit) are as follows (amounts in millions):

	For the years ended December 31,		
	2009	2008	2007
Income (loss) before income tax benefit:			
Domestic	\$ (237)	\$ (131)	\$ 144
Foreign	229	(56)	31
	\$ (8)	\$ (187)	\$ 175
Income tax expense (benefit):			
Current:			
Federal	\$ 237	\$ 251	\$ 90
State	46	49	7
Foreign	14	41	24
Total current	297	341	121
Deferred:			
Federal	(309)	(294)	(55)
State	(75)	(67)	(2)
Foreign	(12)	(62)	(7)
Release of valuation allowance	(22)		(30)
Change in valuation allowance related to net operating loss surrendered			(79)
Total deferred	(418)	(423)	(173)
Add back benefit credited to additional paid-in capital:			
Excess tax benefit associated with stock options		2	
Income tax benefit	\$ (121)	\$ (80)	\$ (52)

For the year ended December 31, 2009, we have a pretax domestic loss of \$237 million and foreign pretax income of \$229 million. The U.S. pretax loss is primarily driven by stock option expense, intangible asset amortization recorded domestically as well as an impairment of intangible assets in the current year.

Table of Contents**ACTIVISION BLIZZARD, INC. AND SUBSIDIARIES****Notes to Consolidated Financial Statements (Continued)****16. Income Taxes (Continued)**

The items accounting for the difference between income taxes computed at the U.S. federal statutory income tax rate and the income tax expense (benefit) for each of the years are as follows:

	For the years ended December 31,					
	2009		2008		2007	
Federal income tax provision at statutory rate	\$	(3)	(35)%	\$	(65)	(35)%
State taxes, net of federal benefit		(17)	(219)		(6)	(3)
Research and development credits		(24)	(302)		(31)	(17)
Domestic production activity deduction		(7)	(89)		(12)	(6)
Foreign rate differential		(82)	(1,040)		(2)	(1)
Change in valuation allowance		(22)	(286)		6	3
Change in tax reserves		34	440		11	6
Foreign withholding tax		2	24		8	4
Foreign tax credits		(3)	(41)		(15)	(8)
Goodwill impairment					7	4
Shortfall from employee stock option exercises		2	27			
Return to provision adjustment					12	6
Change in valuation allowance related to net operating loss surrendered						
Other		(1)	(13)		7	4
	\$	(121)	(1,534)%	\$	(80)	(43)%
					\$	(52)
						(30)%

Table of Contents**ACTIVISION BLIZZARD, INC. AND SUBSIDIARIES****Notes to Consolidated Financial Statements (Continued)****16. Income Taxes (Continued)**

Deferred income taxes reflect the net tax effects of temporary differences between the amounts of assets and liabilities for accounting purposes and the amounts used for income tax purposes. The components of the net deferred tax assets (liabilities) are as follows (amounts in millions):

	As of December 31,	
	2009	2008
Deferred tax assets:		
Reserves and allowances	\$ 36	\$ 35
Allowance for sales returns and price protection	64	59
Inventory reserve	17	13
Accrued expenses	53	46
Accrued legal and professional fees	3	28
Accrued restructuring	1	15
Deferred revenue	292	326
Deferred compensation	4	1
Depreciation		9
Tax credit carryforwards	61	30
Net operating loss carryforwards	18	24
State taxes		19
Stock-based compensation	119	58
Foreign deferred assets	27	27
Other	9	4
Deferred tax assets	704	694
Valuation allowance		(22)
Deferred tax assets, net of valuation allowance	704	672
Deferred tax liabilities:		
Intangibles	(407)	(691)
Prepaid royalties	(5)	(10)
Capitalized software development expenses	(56)	(50)
State taxes	(8)	
Deferred tax liabilities	(476)	(751)
Net deferred tax assets (liabilities)	\$ 228	\$ (79)

As of December 31, 2009, our available federal net operating loss carryforward of approximately \$1 million is subject to certain limitations as defined under Section 382 of the Internal Revenue Code. The net operating loss carryforward will begin to expire in 2023. We have various state net operating loss carryforwards totaling \$17 million which are not subject to limitations under Section 382 of the Internal Revenue Code and will begin to expire in 2013. We have tax credit carryforwards of \$6 million and \$55 million for federal and state purposes, respectively, which begin to expire in fiscal 2016.

Through our foreign operations, we have approximately \$18 million in net operating loss carryforwards at December 31, 2009, attributed mainly to losses in France, Ireland, and Sweden. We evaluate our deferred tax assets, including net operating losses, to determine if a valuation

allowance is

F-41

Table of Contents**ACTIVISION BLIZZARD, INC. AND SUBSIDIARIES****Notes to Consolidated Financial Statements (Continued)****16. Income Taxes (Continued)**

required. We assess whether a valuation allowance should be established or released based on the consideration of all available evidence using a "more likely than not" standard. In making such judgments, significant weight is given to evidence that can be objectively verified. At December 31, 2008 we had a foreign net operating loss valuation allowance of \$22 million. During 2009, we determined that such net operating losses were likely to be realized through taxable income; therefore, we released a valuation allowance of \$22 million against our deferred tax assets. At December 31, 2009 there are no valuation allowances on deferred tax assets.

Realization of the U.S. deferred tax assets is dependent upon the continued generation of sufficient taxable income prior to expiration of tax credits and loss carryforwards. Although realization is not assured, management believes it is more likely than not that the net carrying value of the U.S. deferred tax assets will be realized.

Cumulative undistributed earnings of foreign subsidiaries for which no deferred taxes have been provided approximated \$498 million at December 31, 2009. Deferred income taxes on these earnings have not been provided as these amounts are considered to be permanent in duration. It is not practical to estimate the amount of tax that would be payable upon distribution of these earnings.

As of December 31, 2009, we had approximately \$139 million in total unrecognized tax benefits of which \$131 million would affect our effective tax rate if recognized. A reconciliation of unrecognized tax benefits for the years ended December 31, 2009, 2008 and 2007 is as follows (amounts in millions):

	At December 31,		
	2009	2008	2007
Unrecognized tax benefits balance at January 1	\$ 103	\$ 13	\$
Assumption of unrecognized tax benefits upon the Business Combination		73	
Gross increase for tax positions of prior years	3	12	1
Gross decrease for tax positions of prior years	(1)	(2)	
Gross increase for tax positions of current year	35	7	12
Gross decrease for tax positions of current year			
Settlements			
Lapse of statute of limitations	(1)		
Unrecognized tax benefits balance at December 31	\$ 139	\$ 103	\$ 13

In addition, as of December 31, 2009 and 2008, we reflected \$123 million and \$81 million, respectively, of income tax liabilities as non-current liabilities because payment of cash or settlement is not anticipated within one year of the balance sheet date. These non-current income tax liabilities are recorded in other liabilities in the consolidated balance sheets as of December 31, 2009 and 2008.

We recognize interest and penalties related to uncertain tax positions in income tax expense. As of December 31, 2009 and 2008, we had approximately \$8 million and \$2 million, respectively, of accrued interest and penalties related to uncertain tax positions. For the years ended December 31, 2009 and 2008, we recorded \$6 million and \$1 million of interest expense related to uncertain tax positions, respectively.

Table of Contents

ACTIVISION BLIZZARD, INC. AND SUBSIDIARIES

Notes to Consolidated Financial Statements (Continued)

16. Income Taxes (Continued)

Vivendi Games results for the period January 1, 2008 through July 9, 2008 are included in the consolidated federal and certain foreign, state and local income tax returns filed by Vivendi or its affiliates while Vivendi Games results for the period July 10, 2008 through December 31, 2008 are included in the consolidated federal and certain foreign, state and local income tax returns filed by Activision Blizzard. Vivendi Games is no longer subject to U.S. federal income tax examinations for tax years before 2002. Vivendi Games is also no longer subject to state examinations for tax years before 2000. Activision Blizzard's tax years 2006 through 2008 remain open to examination by the major taxing jurisdictions to which we are subject, including the United States of America ("U.S.") and non-U.S. locations. Activision Blizzard is currently under audit by the California Franchise Tax Board for the tax years 1996 through 2004, and it is reasonably possible that the current portion of our unrecognized tax benefits will significantly decrease within the next twelve months due to the outcome of these audits.

On July 9, 2008, Activision Blizzard entered into a Tax Sharing Agreement (the "Tax Sharing Agreement") with Vivendi. The Tax Sharing Agreement generally governs Activision Blizzard's and Vivendi's respective rights, responsibilities and obligations with respect to the ordinary course of business taxes. Currently, under the Tax Sharing Agreement, with certain exceptions, Activision Blizzard generally is responsible for the payment of U.S. and certain non-U.S. income taxes that are required to be paid to tax authorities on a stand-alone Activision Blizzard basis. In the event that Activision Blizzard joins Vivendi in the filing of a group tax return, Activision Blizzard will pay its share of the tax liability for such group tax return to Vivendi, and Vivendi will pay the tax liability for the entire group to the appropriate tax authority. Vivendi will indemnify Activision Blizzard for any tax liability imposed upon it due to Vivendi's failure to pay any group tax liability. Activision Blizzard will indemnify Vivendi for any tax liability imposed on Vivendi (or any of its subsidiaries) due to Activision Blizzard's failure to pay any taxes it owes under the Tax Sharing Agreement.

Prior to the Business Combination, Vivendi Games' income taxes are presented in the financial statements as if Vivendi Games were a stand-alone taxpayer even though Vivendi Games' operating results are included in the consolidated federal, certain foreign, and state and local income tax returns of Vivendi or Vivendi's subsidiaries. Based on the subsequent filing of these tax returns by Vivendi or Vivendi's subsidiaries, we determined that the amount paid by Vivendi Games was greater than the actual amount due (and settled) based upon filing of these returns for the year ended December 31, 2008. This difference between the amount paid and the actual amount due (and settled) represents a return of capital to Vivendi, which was required in accordance with the terms of the Business Combination agreement immediately prior to the close of the Business Combination. This difference has resulted in no additional payment to Vivendi and no impact to our consolidated statement of cash flows for the year ended December 31, 2009.

Within the next twelve months, it is reasonably possible we will reduce approximately \$22 million of previously unrecognized tax benefits due to the expiration of statutes of limitation and anticipated closure of income tax examinations.

[Table of Contents](#)**ACTIVISION BLIZZARD, INC. AND SUBSIDIARIES****Notes to Consolidated Financial Statements (Continued)****17. Fair Value Measurements**

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

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

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

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

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

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

Table of Contents

ACTIVISION BLIZZARD, INC. AND SUBSIDIARIES

Notes to Consolidated Financial Statements (Continued)

17. Fair Value Measurements (Continued)

	As of December 31, 2008	Fair Value Measurements at Reporting Date Using			Balance Sheet Classification
		Quoted Prices in Active Markets for Identical Financial Instruments (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)	
Financial assets:					
Money market funds	\$ 2,609	\$ 2,609	\$	\$	Cash and cash equivalents
Mortgage backed securities	7		7		Short-term investments
Auction rate securities held through UBS and Citigroup, Inc	78			78	Long-term investments
ARS rights from UBS	10			10	Other assets non-current
Foreign exchange contract derivatives	5		5		Other assets current
Total financial assets at fair value	\$ 2,709	\$ 2,609	\$ 12	\$ 88	
Financial liabilities:					
Foreign exchange contract derivatives	\$ (2)	\$	(2)	\$	Other liabilities current
Other financial liability	(31)			(31)	Other liabilities current
Total financial liabilities at fair value	\$ (33)	\$	(2)	(31)	

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

[Table of Contents](#)
ACTIVISION BLIZZARD, INC. AND SUBSIDIARIES
Notes to Consolidated Financial Statements (Continued)
17. Fair Value Measurements (Continued)

The following table provides a reconciliation of the beginning and ending balances of our financial assets and financial liabilities classified as Level 3 by major categories (amounts in millions):

		Auction rate securities (a)	ARS rights from UBS (b)	Level 3 Total financial assets at fair value	Other financial liabilities
Balance at January 1, 2009	\$	78	\$ 10	\$ 88	\$ (31)
Total gains or (losses) (realized/unrealized)					
Included in earnings		3	(3)		8
Purchases or acquired sales, issuances and settlements		(4)		(4)	
Balance at December 31, 2009	\$	77	\$ 7	\$ 84	\$ (23)

The amount of total gains or (losses) for the period included in earnings attributable to the change in unrealized gains or losses relating to assets still held at December 31, 2009	\$	3	\$ (3)	\$	8
---	----	---	--------	----	---

		Auction rate securities (a)	ARS rights from UBS (b)	Level 3 Total financial assets at fair value	Other financial liabilities
Balance at January 1, 2008	\$	\$	\$	\$	\$
Total gains or (losses) (realized/unrealized)					
Included in earnings		(6)	10	4	
Included in other comprehensive income		(4)		(4)	
Purchases or acquired sales, issuances and settlements					(1)
Purchases via the Business Combination		88		88	(30)
Balance at December 31, 2008	\$	78	\$ 10	\$ 88	\$ (31)

The amount of total gains or (losses) for the period included in earnings attributable to the change in unrealized gains or losses relating to assets still held at December 31, 2008	\$	(6)	\$ 10	\$ 4	\$
---	----	-----	-------	------	----

(a)

Liquidity for these auction rate securities is typically provided by an auction process which allows holders to sell their notes and resets the applicable interest rate at pre-determined intervals, usually every 7 to 35 days. On an industry-wide basis, many auctions have failed, and there is, as yet, no meaningful secondary market for these instruments. Each of the auction rate securities in our investment portfolio at December 31, 2009 has experienced a failed auction and there is no assurance that future auctions for these securities will succeed. An auction failure means that the parties wishing to sell their securities could not be matched with an adequate volume of

Edgar Filing: Activision Blizzard, Inc. - Form 10-K

buyers. In the event that there is a failed auction, the indenture governing the security requires the issuer to pay interest at a contractually defined rate that is generally above market rates for other types of similar instruments. The securities for which auctions have failed will continue to earn interest at the contractual rate and be auctioned every 7 to 35 days until the auction succeeds, the issuer calls the securities or they mature. As a result, our ability to liquidate and fully recover the carrying value of our auction rate securities in the near term may be limited or non-existent.

F-46

Table of Contents**ACTIVISION BLIZZARD, INC. AND SUBSIDIARIES****Notes to Consolidated Financial Statements (Continued)****17. Fair Value Measurements (Continued)**

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

(b)

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

The table below segregates all assets and liabilities that are measured at fair value on a non-recurring basis during the period into the most appropriate level within the fair value hierarchy based on the inputs used to determine the fair value at the measurement date (amounts in millions):

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

In accordance with the provisions of the impairment of long-lived assets subsections of ASC Subtopic 360-10, intangible assets with a carrying value of \$687 million were written down to their fair value of \$278 million. The write down resulted in impairment charges of \$24 million, \$12 million, and \$373 million of license agreements, game engines and internally developed franchises intangible assets, respectively (see Note 12). The impairment charge of \$409 million is included in net income for the year ended December 31, 2009.

18. Commitments and Contingencies*Credit Facilities*

At December 31, 2009 and 2008, we maintained a \$30 million and \$35 million irrevocable standby letter of credit, respectively. The standby letter of credit is required by one of our inventory manufacturers to qualify for payment terms on our inventory purchases. Under the terms of this arrangement, we are required to maintain on deposit with the bank a compensating balance, restricted as to use, of not less than the sum of the available amount of the letter of credit plus the aggregate amount of any drawings under the letter of credit that have been honored thereunder but not reimbursed. The letter of credit was undrawn at December 31, 2009 and 2008.

Table of Contents

ACTIVISION BLIZZARD, INC. AND SUBSIDIARIES

Notes to Consolidated Financial Statements (Continued)

18. Commitments and Contingencies (Continued)

At December 31, 2009 and 2008, our publishing subsidiary located in the U.K. maintained a EUR 30 million (\$43 million) and EUR 25 million (\$35 million) irrevocable standby letter of credit, respectively. The standby letter of credit is required by one of our inventory manufacturers to qualify for payment terms on our inventory purchases. The standby letter of credit does not require a compensating balance and expires in March 2010. No amounts were outstanding at December 31, 2009 and 2008.

On April 29, 2008, Activision, Inc. entered into a senior unsecured credit agreement with Vivendi (as lender). Borrowings under the agreement became available upon consummation of the Business Combination. At December 31, 2009 and 2008, the credit agreement provides for a revolving credit facility of up to \$475 million, bearing interest at LIBOR plus 1.20% per annum. Any unused amount under the revolving credit facility is subject to a commitment fee of 0.42% per annum.

The revolving credit facility is subject to customary negative covenants, in each case subject to certain exceptions and qualifications, including limitations on: indebtedness; liens; investments, mergers, consolidations and acquisitions; transactions with affiliates; issuance of preferred stock by subsidiaries; sale and leaseback transactions; restricted payments; and certain restrictions with respect to subsidiaries. The limitation on indebtedness provides that Activision Blizzard cannot incur consolidated indebtedness, net of unrestricted cash, in excess of \$1.5 billion, and that no additional indebtedness may be incurred as long as the ratio of Activision Blizzard's consolidated indebtedness (including the indebtedness to be incurred) minus the amount of unrestricted cash to Activision Blizzard's consolidated earnings before interest, taxes, depreciation and amortization for its most recently ended four quarters would be greater than 1.50 to 1.0. This limitation does not, however, affect Activision Blizzard's ability to borrow under the revolving credit facility or to incur certain types of limited debt. The revolving credit facility also imposes a requirement on Activision Blizzard that the ratio of (i) consolidated indebtedness (net of certain cash) to (ii) the sum of its shareholder's equity plus consolidated indebtedness (net of certain cash) not exceed 20% at any time.

No borrowings under revolving credit facility with Vivendi were outstanding at December 31, 2009 and 2008.

Commitments

In the normal course of business, we enter into contractual arrangements with third parties for non-cancelable operating lease agreements for our offices, for the development of products, and for the rights to intellectual property. Under these agreements, we commit to provide specified payments to a lessor, developer or intellectual property holder, as the case may be, based upon contractual arrangements. The payments to third-party developers are generally conditioned upon the achievement by the developers of contractually specified development milestones. Further, these payments to third-party developers and intellectual property holders typically are deemed to be advances and are recoupable against future royalties earned by the developer or intellectual property holder based on the sale of the related game. Additionally, in connection with certain intellectual property rights acquisitions and development agreements, we will commit to spend specified amounts for marketing support for the related game(s) which is to be developed or in which the intellectual property will be utilized. Assuming all contractual provisions are met, the total future minimum commitments for these

Table of Contents**ACTIVISION BLIZZARD, INC. AND SUBSIDIARIES****Notes to Consolidated Financial Statements (Continued)****18. Commitments and Contingencies (Continued)**

and other contractual arrangements in place at December 31, 2009 are scheduled to be paid as follows (amounts in millions):

	Contractual Obligations(1)			
	Facility and equipment leases	Developer and Intellectual Properties	Marketing	Total
For the years ending December 31,				
2010	\$ 37	\$ 113	\$ 27	\$ 177
2011	25	41	25	91
2012	21	18	13	52
2013	18	22		40
2014	15	10		25
Thereafter	32			32
 Total	 \$ 148	 \$ 204	 \$ 65	 \$ 417

(1)

We have omitted uncertain tax liabilities from this table due to the inherent uncertainty regarding the timing of potential issue resolution. Specifically, either (a) the underlying positions have not been fully developed under audit to quantify at this time or, (b) the years relating to the issues for certain jurisdictions are not currently under audit. At December 31, 2009, we had \$139 million of unrecognized tax benefits.

Legal Proceedings

On February 8, 2008, the Wayne County Employees' Retirement System filed a lawsuit challenging the Business Combination in the Delaware Court of Chancery. The suit is a putative class action filed against the parties to the Business Combination Agreement as well as certain current and former members of our Board of Directors. The plaintiff alleged, among other things, that our current and former directors named therein failed to fulfill their fiduciary duties with regard to the Business Combination by "surrendering" the negotiating process to "conflicted management," that those breaches were aided and abetted by Vivendi and those of its subsidiaries named in the complaint, and that the preliminary proxy statement filed by the Company on January 31, 2008 contains certain statements that the plaintiff alleges are false and misleading. The plaintiff sought an order from the court that, among other things, certifies the case as a class action, enjoins the Business Combination, requires the defendants to disclose all material information, declares that the Business Combination is in breach of the directors' fiduciary duties and therefore unlawful and unenforceable, awards the plaintiff and the putative class damages for all profits and special benefits obtained by the defendant in connection with the Business Combination and tender offer, and awards the plaintiff its cost and expense, including attorney's fees.

After various initial motions were filed and ruled upon, on May 8, 2008, the plaintiff filed an amended complaint that, among other things, added allegations relating to a revised preliminary proxy statement filed by the Company on April 30, 2008. Additional motions were then filed, including a motion for preliminary injunction filed by the plaintiff and a motion to dismiss filed by Vivendi and its subsidiaries. On June 14, 2008, the plaintiff filed a motion for leave to file a second amended complaint. On June 30, 2008, the court granted Vivendi and its subsidiaries' motion to dismiss,

Table of Contents

ACTIVISION BLIZZARD, INC. AND SUBSIDIARIES

Notes to Consolidated Financial Statements (Continued)

18. Commitments and Contingencies (Continued)

pursuant to a stipulation with the plaintiff, and on July 1, 2008, denied the plaintiff's motion for preliminary injunction.

On December 23, 2008, the plaintiff filed an amended motion for leave to file a second amended complaint. The court granted the motion on January 14, 2009 and the second amended complaint was deemed filed on the same date. The second amended complaint asserts claims similar to the ones made in the original complaint, challenging Activision's Board of Directors' actions in connection with the negotiation and approval of the Business Combination, as well as disclosures made to our stockholders and certain amendments made to our certificate of incorporation in connection therewith. In addition, the second amended complaint asserts that Activision's Board of Directors breached its fiduciary duties in approving and recommending those amendments to the certificate of incorporation. Among other things, the plaintiff seeks certification of the action as a class action, a declaration that amendments made to the certificate of incorporation are invalid and unenforceable, a declaration that our directors breached their fiduciary duties, rescission of the Business Combination and related transactions, and damages, interest, fees and costs. On July 24, 2009, the court granted the Company's motion to dismiss the complaint for failure to state a claim.

On August 21, 2009, the plaintiff filed a notice of appeal of the court's dismissal. Appellate briefing has been completed and a hearing on the appeal occurred before a panel of the Delaware Supreme Court on January 13, 2010. The court has now scheduled an additional hearing before the entire court on March 31, 2010. No amounts have been recorded in the statements of operations for this matter as losses are not probable.

In November 2009, the Company released Call of Duty: Modern Warfare 2, a game developed by one of the Company's wholly-owned studios, Infinity Ward. As noted above, Modern Warfare 2 was the best selling console title in the U.S. and Europe in 2009. Consistent with past practice, the Company intends to release a Call of Duty game in 2010 developed by another wholly-owned studio. The Company is concluding an internal human resources inquiry into breaches of contract and insubordination by two senior employees at Infinity Ward. This matter is expected to involve the departure of key personnel and litigation. At present, the Company does not expect this matter to have a material impact on the Company.

In addition, we are party to other routine claims and suits brought by us and against us in the ordinary course of business, including disputes arising over the ownership of intellectual property rights, contractual claims, employment laws, regulations and relationships, and collection matters. In the opinion of management, after consultation with legal counsel, the outcome of such routine claims and lawsuits will not have a material adverse effect on our business, financial condition, results of operations, or liquidity.

19. Stock-Based Compensation

Equity Incentive Plans

The Activision Blizzard Inc. 2008 Incentive Plan was adopted by our Board on July 28, 2008, approved by our stockholders and amended and restated by our Board on September 24, 2008, further amended and restated by our Board with stockholder approval on June 3, 2009 and further amended and restated by the Compensation Committee of our Board with stockholder approval on December 17, 2009 (as so amended and restated, the "2008 Plan"). The 2008 Plan authorizes the Compensation Committee of our Board of Directors to provide equity-based compensation in the form

Table of Contents

ACTIVISION BLIZZARD, INC. AND SUBSIDIARIES

Notes to Consolidated Financial Statements (Continued)

19. Stock-Based Compensation (Continued)

of stock options, share appreciation rights, restricted stock, restricted stock units, performance shares, performance units and other performance- or value-based awards structured by the Compensation Committee within parameters set forth in the 2008 Plan, including custom awards that are denominated or payable in, valued in whole or in part by reference to, or otherwise based on or related to, shares of our common stock, or factors that may influence the value of our common stock or that are valued based on our performance or the performance of any of our subsidiaries or business units or other factors designated by the Compensation Committee, as well as incentive bonuses, for the purpose of providing incentives and rewards for performance to the directors, officers, and employees of, and consultants to, Activision Blizzard and its subsidiaries.

While the Compensation Committee has broad discretion to create equity incentives, our equity-based compensation program for the most part currently utilizes a combination of options and restricted stock units. Such awards generally have time-based vesting schedules, vesting annually over periods of three to five years, or vest in their entirety on an anniversary of the date of grant, subject to possible earlier vesting if certain performance measures are met, and all such awards which are options generally expire ten years from the grant date. In addition, under the terms of the 2008 Plan, the exercise price for the options must be equal to or greater than the closing price per share of our common stock on the date the award is granted, as reported on NASDAQ.

Upon the effective date of the 2008 Plan, we ceased to make awards under the following equity incentive plans (collectively, the "Prior Plans"), although such plans will remain in effect and continue to govern outstanding awards: (i) Activision, Inc. 1998 Incentive Plan, as amended; (ii) Activision, Inc. 1999 Incentive Plan, as amended; (iii) Activision, Inc. 2001 Incentive Plan, as amended; (iv) Activision, Inc. 2002 Incentive Plan, as amended; (v) Activision, Inc. 2002 Executive Incentive Plan, as amended; (vi) Activision, Inc. 2002 Studio Employee Retention Incentive Plan, as amended; (vii) Activision, Inc. 2003 Incentive Plan, as amended; and (viii) Activision, Inc. 2007 Incentive Plan.

Pursuant to the 2008 Plan as adopted, 30 million shares of our common stock were made available for issuance. The 2008 plan was amended with stockholder approval on December 17, 2009 to increase the number of shares of our common stock available for issuance thereunder by 14 million. The number of shares of our common stock reserved for issuance under the 2008 Plan may be further increased from time to time by: (i) the number of shares relating to awards outstanding under any Prior Plan that: (a) expire, or are forfeited, terminated or cancelled, without the issuance of shares; (b) are settled in cash in lieu of shares; or (c) are exchanged, prior to the issuance of shares of our common stock, for awards not involving our common stock; and (ii) if the exercise price of any option outstanding under any Prior Plan is, or the tax withholding requirements with respect to any award outstanding under any Prior Plan are, satisfied by withholding shares otherwise then deliverable in respect of the award or the actual or constructive transfer to the Company of shares already owned, the number of shares equal to the withheld or transferred shares. At December 31, 2009, we had approximately 16 million shares of our common stock reserved for future issuance under the 2008 Plan. Shares issued in connection with awards made under the 2008 Plan are generally issued as new stock issuances.

Modification of Awards through Business Combination

As a result of the reverse acquisition accounting treatment for the Business Combination, previously issued Activision, Inc. stock options and restricted stock awards granted to employees and directors that were outstanding and unvested at the date of the Business Combination, were accounted

Table of Contents

ACTIVISION BLIZZARD, INC. AND SUBSIDIARIES

Notes to Consolidated Financial Statements (Continued)

19. Stock-Based Compensation (Continued)

for as an exchange of awards. The fair value of the outstanding vested and unvested awards was measured on the date of the acquisition, and for unvested awards which require service subsequent to the date of the Business Combination, a portion of the awards' fair values have been allocated to future service and will be recognized over the remaining future requisite service period.

Employee Stock Purchase Plan

The Employee Stock Purchase Plan was terminated by the Board of Directors and there were no further purchases thereunder after October 1, 2008. Effective October 1, 2005, the Board of Directors of Activision, Inc. approved the Activision, Inc. Third Amended and Restated 2002 Employee Stock Purchase Plan and the Activision, Inc. Second Amended and Restated 2002 Employee Stock Purchase Plan for International Employees (together, the "ESPP"). Before the termination, up to an aggregate of 4,000,000 shares of Activision, Inc. common stock was available for purchase by eligible employees during two six-month offering periods that commenced each April 1 and October 1 (the "Offering Period") at a price per share generally equal to 85% of the lower of the fair market value of our common stock on the first day of the Offering Period and the fair market value of our common stock on the purchase date (the last day of the Offering Period). Employees had been able to purchase shares having a value not exceeding 15% of their gross compensation during an Offering Period and were limited to a maximum of \$10,000 in value for any two purchases within the same calendar year. As a result of the Business Combination the offering period in effect at the time of the Business Combination was assumed by us, and on October 1, 2008, employees purchased 262,002 shares of our common stock at a purchase price of \$11.65 per share under the ESPP.

Restricted Stock Unit, Restricted Stock Awards, and Performance Shares Activities

We grant restricted stock units, restricted stock awards, and performance shares (collectively referred to as "restricted stock rights") under the 2008 Plan to employees around the world, and we have assumed as a result of the Business Combination the restricted stock rights granted by Activision, Inc. Restricted stock awards units entitle the holders thereof to receive shares of our common stock at the end of a specified period of time or otherwise upon a specified occurrence. Restricted stock awards and performance shares are issued and outstanding upon grant; however, holders of restricted stock and performance shares are restricted from selling the shares until they vest. Upon vesting of restricted stock rights, we may withhold shares otherwise deliverable to satisfy tax withholding requirements. Restricted stock rights are subject to forfeiture and transfer restrictions. Vesting for restricted stock rights is contingent upon the holders' continued employment with us and may be subject to other conditions. If the vesting conditions are not met, unvested restricted stock rights will be forfeited.

In connection with the consummation of the Business Combination, on July 9, 2008, Robert A. Kotick, our Chief Executive Officer, received a grant of 2,500,000 performance shares, which vest in 20% increments on each of the first, second, third, and fourth anniversaries of the date of grant, with another 20% vesting on December 31, 2012, the expiration date of Mr. Kotick's employment agreement with the Company, in each case subject to the Company attaining the specified compound annual total shareholder return target for that vesting period. If the Company does not achieve the performance target for a vesting period, no performance shares will vest for that vesting period. If, however, the Company achieves a performance target for a subsequent vesting period, then all of the performance shares that would have vested on the previous vesting date will vest on the vesting date when the performance targets were achieved.

Table of Contents**ACTIVISION BLIZZARD, INC. AND SUBSIDIARIES****Notes to Consolidated Financial Statements (Continued)****19. Stock-Based Compensation (Continued)**

The following table summarizes our restricted stock rights activity for the year ended December 31, 2009 (amounts in thousands except per share amounts):

	Restricted Stock Rights	Weighted- Average Grant Date Fair Value
Balance at December 31, 2008	10,267	\$ 14.52
Granted	2,755	11.80
Vested	(1,539)	11.49
Forfeited	(180)	11.29
Balance at December 31, 2009	11,303	12.69

At December 31, 2009, approximately \$62 million of total unrecognized compensation cost was related to restricted stock rights, of which \$8 million was related to performance shares, which cost is expected to be recognized over a weighted-average period of 1.8 years and 3.5 years, respectively. Total grant date fair value of restricted stock rights vested was \$34 million and \$9 million for the years ended December 31, 2009 and 2008, respectively.

Non-Plan Employee Stock Options

In connection with prior employment agreements between Activision, Inc. and Robert A. Kotick, our Chief Executive Officer, and Brian G. Kelly, our Co-Chairman, Mr. Kotick and Mr. Kelly were previously granted options to purchase common stock of Activision, Inc. which were not awarded under a stockholder- or board-approved plan. These awards were assumed as a result of the Business Combination and accounted for as an exchange for options to purchase our common stock. All non-plan options were exercised during 2009.

Blizzard Equity Plan ("BEP")

In 2006, Blizzard implemented the BEP, an equity incentive plan denominated in U.S. dollars. Under the BEP, restricted shares of Blizzard stock and other cash settled awards were granted to certain key executives and employees of Blizzard.

Under the provisions of the BEP and the Business Combination Agreement, the consummation of the Business Combination was deemed to be a change in control. As such, the outstanding non-vested rights became immediately vested upon the closing of the Business Combination, cancelled and extinguished and converted into a new right to receive an amount in cash eighteen months after the closing upon the terms and subject to the conditions set forth in the BEP and in the Business Combination Agreement, including continued employment through the payment date. The determination of the value of Blizzard shares upon a change in control was equal to the transaction value under the provisions of the BEP. At December 31, 2009, unrecognized compensation expense under the BEP was less than a million, which will be recognized during the three months ended March 31, 2010. At December 31, 2009, other current liabilities in the consolidated balance sheet include \$87 million related to this plan, and at December 31, 2008, other non-current liabilities include \$70 million related to this plan.

Table of Contents**ACTIVISION BLIZZARD, INC. AND SUBSIDIARIES****Notes to Consolidated Financial Statements (Continued)****19. Stock-Based Compensation (Continued)***Stock-based Compensation Expense*

The following table sets forth the total stock-based compensation expense resulting from stock options granted by Activision, Inc. or Activision Blizzard, restricted stock rights awarded by Activision, Inc. or Activision Blizzard, awards made to our employees under the BEP, and awards made to our employees under the Vivendi corporate plans described below included in our consolidated statements of operations for the years ended December 31, 2009, 2008, and 2007 (amounts in millions):

	For the years ended December 31,		
	2009	2008	2007
Cost of sales software royalties and amortization	\$ 34	\$ 4	\$ 3
Product development	40	44	93
Sales and marketing	9	10	8
General and administrative	71	31	34
Restructuring	2		
Stock-based compensation expense before income taxes	156	89	138
Income tax benefit	(61)	(35)	(54)
Total stock-based compensation expense, net of income tax benefit	\$ 95	\$ 54	\$ 84

The following table summarizes stock-based compensation included in our consolidated balance sheets as a component of software development (amounts in millions):

	Software development
Balance at December 31, 2007	\$
Stock-based compensation expense capitalized and deferred during period	54
Amortization of stock-based compensation expense	(12)
Balance at December 31, 2008	42
Stock-based compensation expense capitalized and deferred during period	102
Amortization of stock-based compensation expense	(90)
Balance at December 31, 2009	\$ 54

Method and Assumptions on Valuation of Stock Options

Our employee stock options have features that differentiate them from exchange-traded options. These features include lack of transferability, early exercise, vesting restrictions, pre- and post-vesting termination provisions, blackout dates, and time-varying inputs. In addition, some of the options have non-traditional features, such as accelerated vesting upon the satisfaction of certain performance conditions that must be reflected in the valuation. A binomial-lattice model was selected because it is better able to explicitly address these features than closed-form models such as the Black-Scholes

Table of Contents**ACTIVISION BLIZZARD, INC. AND SUBSIDIARIES****Notes to Consolidated Financial Statements (Continued)****19. Stock-Based Compensation (Continued)**

model, and is able to reflect expected future changes in model inputs, including changes in volatility, during the option's contractual term.

We have estimated expected future changes in model inputs during the option's contractual term. The inputs required by our binomial-lattice model include expected volatility, risk-free interest rate, risk-adjusted stock return, dividend yield, contractual term, and vesting schedule, as well as measures of employees' forfeiture, exercise, and post-vesting termination behavior. Statistical methods were used to estimate employee rank-specific termination rates. These termination rates, in turn, were used to model the number of options that are expected to vest and post-vesting termination behavior. Employee rank-specific estimates of Expected Time-To-Exercise ("ETTE") were used to reflect employee exercise behavior. ETTE was estimated by using statistical procedures to first estimate the conditional probability of exercise occurring during each time period, conditional on the option surviving to that time period and then using those probabilities to estimate ETTE. The model was calibrated by adjusting parameters controlling exercise and post-vesting termination behavior so that the measures output by the model matched values of these measures that were estimated from historical data.

The following tables present the weighted-average assumptions and the weighted-average fair value at grant date using the binomial-lattice model:

	Employee and director options For the year ended December 31, 2009	Employee and director options For the year ended December 31, 2008
Expected life (in years)	5.95	5.28
Risk free interest rate	3.63%	3.98%
Volatility	53.00%	53.88%
Dividend yield		
Weighted-average fair value at grant date	\$ 5.40	\$ 5.92

Upon consummation of the Business Combination the fair value of Activision, Inc.'s stock awards was determined using the fair value of Activision, Inc.'s common stock of \$15.04 per share, which was the closing price at July 9, 2008, and using a binomial-lattice model with the following assumptions: (a) varying volatility ranging from 42.38% to 51.50%, (b) a risk free interest rate of 3.97%, (c) an expected life ranging from 3.22 years to 4.71 years, (d) risk adjusted stock return of 8.89%, and (e) an expected dividend yield of 0.0%.

To estimate volatility for the binomial-lattice model, we use methods that consider the implied volatility method based upon the volatilities for exchange-traded options on our stock to estimate short-term volatility, the historical method (annualized standard deviation of the instantaneous returns on Activision Blizzard's stock) during the option's contractual term to estimate long-term volatility, and a statistical model to estimate the transition or "mean reversion" from short-term volatility to long-term volatility. Based on these methods, for options granted during the year ended December 31, 2009, the expected stock price volatility ranged from 41.56% to 60.77%.

As is the case for volatility, the risk-free rate is assumed to change during the option's contractual term. Consistent with the calculation required by a binomial lattice model, the risk-free rate reflects the interest from one time period to the next ("forward rate") as opposed to the interest rate from the

Table of Contents

ACTIVISION BLIZZARD, INC. AND SUBSIDIARIES

Notes to Consolidated Financial Statements (Continued)

19. Stock-Based Compensation (Continued)

grant date to the given time period ("spot rate"). Since we have not historically paid dividends, we have assumed that the dividend yield is zero. Our future analysis will reflect the Company's expectation on paying dividends annually subsequent to December 31, 2009.

The expected life of employee stock options represents the weighted-average period the stock options are expected to remain outstanding and is an output from the binomial-lattice model. The expected life of employee stock options depends on all of the underlying assumptions and calibration of our model. A binomial-lattice model can be viewed as assuming that employees will exercise their options when the stock price equals or exceeds an exercise boundary. The exercise boundary is not constant, but continually declines as the option's expiration date approaches. The exact placement of the exercise boundary depends on all of the model inputs as well as the measures that are used to calibrate the model to estimated measures of employees' exercise and termination behavior.

As stock-based compensation expense recognized in the consolidated statement of operations for the year ended December 31, 2009 is based on awards ultimately expected to vest, it has been reduced for estimated forfeitures. Forfeitures are estimated at the time of grant and revised, if necessary, in subsequent periods if actual forfeitures differ from those estimates. Forfeitures were estimated based on historical experience.

Accuracy of Fair Value Estimates

We developed the assumptions used in the binomial-lattice model, including model inputs and measures of employees' exercise and post-vesting termination behavior. Our ability to accurately estimate the fair value of share-based payment awards at the grant date depends upon the accuracy of the model and our ability to accurately forecast model inputs as long as ten years into the future. These inputs include, but are not limited to, expected stock price volatility, risk-free rate, dividend yield, and employee termination rates. Although the fair value of employee stock options is determined using an option-pricing model, the estimates that are produced by this model may not be indicative of the fair value observed between a willing buyer and a willing seller. Unfortunately, it is difficult to determine if this is the case, as markets do not currently exist that permit the active trading of employee stock option and other share-based instruments.

Table of Contents**ACTIVISION BLIZZARD, INC. AND SUBSIDIARIES****Notes to Consolidated Financial Statements (Continued)****19. Stock-Based Compensation (Continued)***Stock Option Activities*

Stock option activities for the year ended December 31, 2009 are as follows (amounts in millions, except number of shares, which are in thousands, and per share amounts):

	Shares	Weighted-average exercise price	Weighted-average remaining contractual term	Aggregate intrinsic value
Outstanding at December 31, 2008	97,841	\$ 6.53		
Granted	9,512	11.67		
Exercised	(34,304)	2.60		
Forfeited	(1,231)	9.98		
Outstanding at December 31, 2009	71,818	9.04	6.76	\$ 210
Vested and expected to vest at December 31, 2009	68,647	\$ 8.90	6.16	\$ 208
Exercisable at December 31, 2009	39,256	\$ 7.12	5.56	\$ 175

The aggregate intrinsic value in the table above represents the total pretax intrinsic value (i.e., the difference between our closing stock price on the last trading day of the period and the exercise price, times the number of shares underlying options where the exercise price is below the closing stock price) that would have been received by the option holders had all option holders exercised their options on that date. This amount changes as it is based on the fair market value of our stock. Total intrinsic value of options actually exercised was \$312 million and \$53 million for the years ended December 31, 2009 and 2008, respectively. Total grant date fair value of options vested was \$143 million and \$32 million for the years ended December 31, 2009 and 2008, respectively.

At December 31, 2009, \$81 million of total unrecognized compensation cost related to stock options is expected to be recognized over a weighted-average period of 1.3 years.

Income tax benefit from stock option exercises was \$85 million and \$22 million for the years ended December 31, 2009 and 2008, respectively.

Vivendi Corporate Plans

Prior to the Business Combination, Vivendi granted Vivendi Games' employees incentive awards that were equity-settled and cash-settled. These equity-settled awards include stock options and restricted share awards, and the cash-settled awards include stock appreciation rights and restricted stock units. There were no new grants by Vivendi to Vivendi Games' employees during the years ended December 31, 2009 and 2008. At December 31, 2009 and 2008, we have recorded in our consolidated balance sheets under other liabilities \$9 million and \$14 million, respectively, relating to cash-settled awards granted pursuant to Vivendi's incentive plans. The following paragraphs describe the various plans established by Vivendi in which Vivendi Games' employees participated.

Table of Contents

ACTIVISION BLIZZARD, INC. AND SUBSIDIARIES

Notes to Consolidated Financial Statements (Continued)

19. Stock-Based Compensation (Continued)

(i) Awards granted to non-U.S. resident executives and employees (settled in equity)

Stock Options (settled in equity)

Stock options to acquire Vivendi stock have been granted to Vivendi Games' employees. All stock options granted by Vivendi prior to January 1, 2007, vest annually in one-third tranches over three years from the grant date's anniversary. Two-thirds of those vested options become exercisable at the beginning of the third year from the date of grant, and the remaining one-third becomes exercisable at the beginning of the fourth year from the date of grant. The related compensation cost is accounted for over the required three-year service period using the accelerated multi-tranche method in accordance with the following spread rates: 61% in the first year of the option, 28% in the second year and 11% in the third year.

In 2007, Vivendi Games employees received stock options which cliff vest at the end of a three-year vesting period. The stock-based compensation expense related to these stock options is recognized on a straight-line basis over the vesting period. These options are denominated in euros.

Restricted Share Units (RSUs) (settled in equity)

Restricted share units were awarded to non-U.S. resident executives and employees of Vivendi Games in 2006 and 2007 upon the achievement of certain operating objectives as set forth in Vivendi's annual budget, and RSUs so awarded cliff vested at the end of a two-year vesting period. As the shares issued upon settlement of the RSUs are ordinary shares of the same class as Vivendi outstanding shares, employee shareholders are entitled to dividend and voting rights relating to their shares upon vesting. Recipients are restricted from selling the shares issued upon settlement of the RSUs until after a four-year period from the date of grant. These RSUs are denominated in euros.

Compensation cost recognized is based upon the value of the equity instrument received by the employees which is equal to the difference between the fair value of the shares to be received upon settlement of the RSUs as of the grant date and the discounted value of the dividends expected to be distributed by Vivendi over the two-year vesting period. Compensation cost relating to RSUs is recognized on a straight-line basis over the two-year vesting period.

(ii) Awards granted to U.S. resident executives and employees (settled in cash)

In 2006, in connection with the delisting of Vivendi shares from the New York Stock Exchange, equity awards were granted to Vivendi Games' U.S. resident executives and employees, with economic characteristics similar to those granted to non-U.S. employees as described above. However, these equity instruments are exclusively cash-settled instruments with the following characteristics:

When the equity awards grant entitlement to the appreciation of the value of Vivendi shares, they are known as "stock appreciation rights" ("SARs"), which are the economic equivalent of stock options;

When the equity awards grant entitlement to the value of Vivendi shares, they are known as "restricted stock units" ("RSUs"), which are the economic equivalent of restricted shares;

Vivendi has converted the former American Depositary Shares ("ADS") stock option awards for its U.S. resident employees into SARs awards; and

Table of Contents

ACTIVISION BLIZZARD, INC. AND SUBSIDIARIES

Notes to Consolidated Financial Statements (Continued)

19. Stock-Based Compensation (Continued)

SARs and RSUs are denominated in U.S. dollars.

Stock Appreciation Rights (SARs) awards

Employees granted SARs will receive, upon exercise of the SARs, a cash payment based on the Vivendi share price, equal to the difference between the Vivendi share price upon exercise of the SARs and their strike price as set at the grant date. Similar to stock options awarded before January 1, 2007, SARs vest annually in one-third tranches on the grant date's anniversary. Two-thirds of those vested SARs become exercisable at the beginning of the third anniversary of the grant date and the remaining one-third becomes exercisable at the beginning of the fourth anniversary of the grant date. The compensation cost of the SARs granted before 2007 is recorded over the vesting period but not on a straight-line basis, as the SARs vest in one-third tranches over three years. The expense is accounted for over the required service period using the accelerated multi-tranche metho