

MAJESCO ENTERTAINMENT CO
Form 10-K
January 29, 2008

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 October 31, 2007

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 No. 000-51128

MAJESCO ENTERTAINMENT COMPANY

(Exact name of registrant as specified in its charter)

DELAWARE

06-1529524 (State or other jurisdiction of
incorporation or organization) (I.R.S. Employer
Identification No.)

160 Raritan Center Parkway
Edison, New Jersey 08837

(Address of principal executive office)

Registrant's telephone number, including area code (732) 225-8910

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

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

Common Stock, Par Value \$0.001
(Title of class)

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 if disclosure of delinquent filers pursuant to Item 405 of Regulation S-K (§ 229.405 of this chapter) is not contained herein, and will not be contained, to the best of 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, or a non-accelerated filer. See definition of "accelerated filer and large accelerated filer" in Rule 12b-2 of the Exchange Act. (Check one):

filer Accelerated filer Non-accelerated filer Large accelerated

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 common stock held by non-affiliates as of April 30, 2007 was \$16.3 million.

The outstanding number of shares of common stock as of January 29, 2008 was 28,709,135.

The Registrant's proxy or information statement is incorporated by reference into Part III of this Annual Report on Form 10-K.

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Item 1. Business.

Forward-looking Statements

Statements in this annual report on Form 10-K that are not historical facts constitute forward-looking statements which are made pursuant to the safe harbor provisions of Section 21E of the Securities Exchange Act of 1934. These statements relate to future events or our future financial performance and involve known and unknown risks, uncertainties and other factors that may cause our or our industry's actual results, levels of activity, performance or achievements to be materially different from any future results, levels of activity, performance or achievements expressed or implied by these forward-looking statements. Those factors include, among other things, those listed under "Risk Factors" and elsewhere in this annual report. In some cases, you can identify forward-looking statements by terminology such as "may," "will," "should," "expects," "plans," "anticipates," "believes," "estimates," "predicts," "or the negative of these terms or other comparable terminology. These statements are only predictions. Actual events or results may differ materially. Moreover, neither we nor any other person assumes responsibility for the accuracy or completeness of these statements. We are under no duty to update any of the forward-looking statements after the date of this annual report to conform these statements to actual results.

Introduction

We are a provider of interactive entertainment products. Our products allow us to capitalize on the large and growing installed base of interactive entertainment platforms and an increasing number of interactive entertainment enthusiasts. We sell our products primarily to large retail chains, specialty retail stores, video game rental outlets and distributors. We also sell our products internationally through distribution agreements with international publishers. Over the past two years, our product emphasis has been on games for the mass market with a focus on developing and publishing a wide range of casual and family oriented video games. We have developed our retail and distribution network relationships over our 20-year history.

We publish video games for almost all major current generation interactive entertainment hardware platforms, including Nintendo's DS, Game Boy Advance, or GBA, Micro GameCube and Wii, Sony's PlayStation 2, or PS2, and PlayStation Portable, or PSP®, Microsoft's Xbox and Xbox 360 and the personal computer, or PC. In addition, we have manufactured and marketed stand alone plug and play video game systems and peripheral devices targeted at the mass market.

Our video game titles are targeted at various demographics at a range of price points, from lower-priced "value" titles to more expensive "premium" titles. In some instances, these titles are based on licenses of well known properties, and in other cases based on original properties. We collaborate and enter into agreements with content providers and video game development studios for the creation of our video games.

Due to the larger budget requirements for developing and marketing premium console titles, we focus on publishing games for handheld systems and value products. Nintendo's Wii console has captured the mass market game audience while allowing for video game titles that fit within our more conservative cost structure. As such, we have expanded our strategic focus to capitalize on the growing installed base of the Wii system, and currently have eight Wii games in development.

Revised Business Model Update

During the second half of fiscal year 2005, we had several major developments that ultimately led us to revise our business model and shift our product strategy away from capital intensive premium console games to a focus on games for handheld systems and value products. During the latter half of the year the interactive entertainment industry experienced a sales slowdown related to the transition to the next generation of game consoles. At the same time, the prevalence of MP3 players and other devices providing digital entertainment led to increased competition for consumers' discretionary spending. As a result, we experienced weak sales across all of our product lines and subsequently

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decided to sell off our rights to and/or cancel a number of our big budget video games in development. For our fiscal year ended October 31, 2005 we recorded impairment charges related to capitalized software development costs and prepaid license fees of \$36.8 million and inventory of \$5.1 million. This contributed to an operating loss of \$70.2 million.

Subsequently, we revised our strategy and business model to focus product development efforts on quality games that are easy to “pick-up-and-play”, priced affordably and targeted for the mass market.

Throughout fiscal 2007 we continue to execute our revised business model and product strategy. Key accomplishments include:

- Reached 1.0 million units sold domestically of the Cooking Mama franchise.
- Signed digital distribution agreements with Microsoft to add Psychonauts to its Xbox Originals program that lets Xbox 360 owners download classic Xbox titles for play on the 360. This deal complements our growing digital download partnerships with GameTap, Macrovision’s Trymedia Network, Steam, and Boonty, for several of our catalog titles including: Psychonauts, BloodRayne 1&2, Advent Rising and Blowout.
- Received an industry award nomination for Cake Mania on the Nintendo DS in the category of best Casual Video Game of the Year from the British Academy of Film and Television Arts.
- Published 13 titles for the Nintendo DS, 1 title for the Nintendo Game Boy Advance, 2 titles for the Sony PlayStation Portable and 1 title for the Microsoft Xbox 360.
- Published our first 2 Wii titles: Cooking Mama and Bust-A-Move

Corporate Background

Majesco Sales Inc. was incorporated in 1986 under the laws of the State of New Jersey. On December 5, 2003, Majesco Sales Inc. completed a reverse merger with Majesco Holdings Inc. (formerly ConnectivCorp), then a publicly traded company with no active operations. Majesco Holdings Inc. was incorporated in 1998 under the laws of the State of Delaware. As a result of the merger, Majesco Sales Inc. became a wholly-owned subsidiary and the sole operating business of the public company. On April 4, 2005, Majesco Sales Inc. was merged into Majesco Holdings Inc., and, in connection with the merger, Majesco Holdings Inc. changed its name to Majesco Entertainment Company. Our principal executive offices are located at 160 Raritan Center Parkway, Edison, NJ 08837, and our telephone number is (732) 225-8910. Our web site address is www.majescoentertainment.com.

Industry Overview

The interactive entertainment industry is mainly comprised of video game hardware platforms, video game software and peripherals. Within this industry, North American combined sales of video game hardware, video game software and video game peripherals were approximately \$17.9 billion in 2007 according to the NPD Group. Of that total, video game software sales accounted for \$8.6 billion, and hardware and accessories sales accounted for \$9.3 billion.

Video Game Hardware Platforms

Video game hardware platforms are comprised of home game consoles, or consoles, and portable handheld game devices, or handhelds, as well as multi-functional devices such as PCs, Personal Digital Assistants, or PDAs, and mobile phones. The current generation of consoles includes Nintendo's Wii, Sony's PlayStation 3 and Microsoft's Xbox 360. On November 22, 2005, Microsoft launched the first of the next-generation consoles, the Xbox 360. According to the NPD Group, the installed base for the Xbox 360 as of December 2007 is approximately 9.2 million. Sony's PlayStation 3 and Nintendo's Wii, were released in North America on November 17, 2006 and November 19, 2006, respectively.

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According to the NPD Group, the installed base for the Wii and PlayStation 3 as of December, 2007 are approximately 7.4 million and 3.3 million respectively. These advanced consoles feature improved graphics capabilities, increased storage capacity and incremental online, wireless and multi-media entertainment functionality intended to attract a wider audience.

The current generation of handhelds is dominated by Nintendo's DS which launched in November 2004 and features a dual screen, wi-fi capability, higher capacity storage media than the Game Boy Advance, and is backward compatible with GBA cartridges. According to the NPD Group, the North American Nintendo DS installed base is 17.7 million as of December 2007. In March 2005, Sony launched the Sony PlayStation Portable system. According to the NPD Group, the North American PSP installed base is approximately 10.5 million as of December 2007.

The ability of multi-functional devices, such as PCs, PDAs and mobile phones to serve as video game platforms has also been greatly enhanced. This is due to periodic advances in microprocessors, graphics chips, storage capacity, operating systems and media and digital rights management. These advances have enabled developers to introduce video games for multi-functional devices with enhanced game play technology and high resolution graphics.

Video Game Software

Video game software is created by the console and handheld manufacturers, and by independent publishers and developers. Console and handheld manufacturers license publishers to develop video games for their platforms and retain a significant degree of control over the content, quality and manufacturing of these products. Most manufacturers also receive a royalty for every software title manufactured for their platform. The publishers, subject to the approval of the platform manufacturers, determine the types of games they will create. Publishers either utilize their own in-house development teams or outsource game development to third-party developers. Following development, publishers then market and sell these products to retailers, either directly or through resellers.

Premium games are often based on licensed popular content or original content with strong characters and storylines. Premium games for consoles generally receive extensive development and marketing investments. Premium games are also higher priced than value titles.

Value titles are generally priced at or below a suggested retail price of \$20.00. Success in the value category is largely based on the ability to cost-effectively bring value titles to market quickly, capitalize on current trends, and place these titles with major retailers.

Traditionally, video games and video content have been delivered using CDs, DVDs or cartridges. More recently, full games and other supplemental content including additional levels, weapons, vehicles and more can now be delivered via the Internet through game portals such as Xbox Live, and various Internet sites, such as Yahoo!. The popularity of this emerging download category is expected to increase, especially within the large-scale multiplayer game segment, and among the user bases of the next generation consoles, PDAs and mobile phones.

Peripherals

Most video game hardware platforms have a variety of peripherals that are designed to enhance the functionality of the device and the experience of the user. For instance, DS users can purchase headphone peripherals that enable private listening. New peripherals have also been developed that enable users to play video games on their televisions without the need for dedicated home game consoles.

Strategy

Our objective is to be an innovative provider of video games for the mass market with a focus on developing and publishing a wide range of casual and family oriented video games. Specifically, we will strive to:

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Focus product development efforts on quality games that are easy to “pick-up-and-play”, priced affordably and targeted for the mass market.

Video game development for handheld systems is generally less expensive and simpler than development for the current and next-generation home consoles. As such, we are focusing our game development efforts in this area with an emphasis on products for the Nintendo DS system that has been experiencing solid growth. We also believe that Nintendo’s Wii console, with its appealing price point and unique play mechanic, will continue to resonate with the mainstream gamer. The Wii’s mass market appeal, combined with its relatively affordable development costs, fits well within our strategy. As such, we now have eight games in development for this system including; titles based on the well-known and critically acclaimed franchise, Cooking Mama; and new intellectual property including Our House. In general, from a game play/content perspective, we are focusing on publishing games that are relatively easy to play and whose subject matter will appeal to as wide an audience as possible.

Leverage our long-term success in the value category.

Publishing software for the value category (suggested price point at or below \$20), which requires a relatively low investment in development and marketing, has historically been one of our strengths. We have published a strong portfolio of value titles for the GBA platform that includes products based on well-known licensed properties, such as Frogger, Cartoon Network, Strawberry Shortcake as well as popular mass market interests/trends (Monster Trucks, Quad Desert Fury, Texas Hold ‘Em Poker, The New York Times Crosswords). We are one of the first publishers to develop a line of high-quality value titles for the Nintendo DS handheld system and to date have launched 23 such titles priced at or below \$20.00. We have also opportunistically published console titles that offer a quality game play experience at value price points such as Kengo: Legend of the 9, Phantom Dust, Guilty Gear, Worms 4: Mayhem. Going forward, we will capitalize on our ability to quickly create or obtain high-quality products to sell at value prices and expand our value product line to other platforms, genres and distribution outlets.

Strategically pursue alternative distribution channels for existing and new products.

Over the last year, we have continued to pursue partnerships in the digital download arena. Psychonauts was recently added to Microsoft’s Xbox Originals program which lets Xbox 360 owners download classic Xbox titles for play on the 360. We also licensed out non-exclusive digital rights for back catalog PC games, such as BloodRayne 2, Psychonauts and Advent Rising, to some of the leading players in this area including Turner’s GameTap Network, Valve’s Steam broadband gaming platform, TryMedia’s digital download network and Boonty. We view these initiatives as incremental revenue with little to no cost. We are in discussions with additional partners in order to maximize this revenue stream and further participate in the digital download and fast-growing online gaming market.

Increase our market share in Europe and Pacific Rim territories.

As the global gaming market continues to grow, we believe that international markets represent a significant growth opportunity for us. Over the last two years, we have expanded our international presence and in late fiscal year 2005 we established an office in the United Kingdom and entered into a license and distribution agreement with a leading international publisher for distribution in European and PAL territories. Under this agreement, the distributor fulfills all sales, marketing and distribution needs for our multi-format product line-up. Our first sales under this agreement were realized in early 2006. We have generated revenues of approximately \$17.3 million through the end of fiscal year 2007. We are also developing distribution relationships in Asia Pacific and Japan and are targeting new territories, such as China, for expansion.

Leverage our industry relationships and entrepreneurial environment to enter new categories and bring innovative products to market.

In the past, we have leveraged our experience, entrepreneurial environment and industry relationships with developers, manufacturers, content providers, retailers and resellers to create and

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distribute new and innovative products. We will continue to capitalize on current market trends and pursue new product opportunities in categories related to our core business.

Products

We offer our customers a wide selection of interactive entertainment products for a variety of platforms.

Our most successful franchise to date has been Cooking Mama that through January 29, 2008 has sold approximately 1.5 million units across three SKU's. In North America Cooking Mama for the DS was first introduced in September 2006 at a \$19.99 value price and has sold more than 1.0 million units. The Wii version, Cooking Mama: Cook Off, launched in March 2007 and the latest release in the franchise is Cooking Mama 2: Dinner with Friends for the DS that was released in November 2007 at a \$29.99 price point

Games

As of November, 2007, our active catalog included more than 40 SKUs, which we categorize as either value or premium titles.

Value Titles

We believe we are a leading publisher of value titles and will continue to expand our value product line to other platforms, genres and distribution outlets. Value titles are typically sold at suggested retail prices at or below \$20. Examples of products in this category include:

- Titles based on emerging consumer fads or trends where we rapidly develop a quality title to capitalize on such interest, such as our two Brain Boost titles, ATV Quad Frenzy and Texas Hold 'Em;
- Titles based on well-known downloadable games such as Cake Mania and Fish Tycoon; and
- Titles that were once our premium titles but over time have become part of our value line including: The New York Times Crosswords, Holly Hobbie & Friends and Age of Empires for DS.

Selected value titles, their compatible platforms and launch or anticipated launch dates include:

Titles	Platform	Launch Date	Selected
Monster Trucks	GBA	October 2004	Texas Hold 'Em Poker
Ultra Bust-A-Move	Xbox	October 2004	Quad: Desert Fury 2
Worms 4: Mayhem	Xbox, PC	October 2005	Looney Toons Double Pack
Monster Trucks	DS	November 2005	ATV Quad Frenzy
Texas Hold 'Em Poker	DS	November 2005	Golden Nugget Casino
Bust-A-Move DS	DS	December 2005	Kong: King of Atlantis
3-1 Rec Room	GBA	December 2005	Super Black Bass Fishing
3-1 Sports Pack	GBA	March 2006	Bust-A-Move Deluxe

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		Selected
Titles	Platform	Launch Date
Dino Master	DS	May 2006
Strawberry Shortcake Sweet Dreams	GBA	September 2006
Cooking Mama	DS	September 2006
Monster Bomber	DS	November 2006
Brain Boost: Beta & Gamma	DS	November 2006
F-24 Stealth Fighter	GBA	November 2006
F-24 Stealth Fighter	DS	February 2007
Cake Mania	DS	April 2007
Toon-Doku	DS	April 2007
Operation Vietnam	DS	August 2007
Turn It Around	DS	August 2007
The Wild West	DS	August 2007
Fish Tycoon	DS	October 2007
Left Brain Right Brain	DS	November 2007
Furu Furu Park	Wii	January 2008
Mega Brain Boost	DS	January 2008
Pet Pals: Animal Doctor	DS	January 2008
Blokus Portable: Steambot Championship	PSP	February 2008
Toy Shop	DS	April 2008
Cake Mania 2	DS	June 2008
Nancy Drew 2	DS	July 2008
Premium Titles		

Our most successful proprietary premium title has been BloodRayne, which since its launch, in October 2002, has generated significant consumer interest and worldwide retail sales of more than 753,000 units. As a result of this success, we developed a sequel, BloodRayne 2, which was released in October 2004, and entered into a number of licensing agreements including a strategy guide, a comic book series, apparel, resin statues, WallSkinz, a feature film that was released in January 2006 and a sequel film that was released in September 2007. In addition to intellectual properties that we own, we also license the rights to content from developers or media entertainment companies as in the cases of Age of Empires, Cake Mania, Cooking Mama, Nacho Libre, Teen Titans and the classic action-suspense film Jaws.

Selected premium titles, their compatible platforms and launch or anticipated launch dates include:

		Selected
Titles	Platform	Launch Date
BloodRayne	Xbox, PS2, GC, PC	October 2002
BloodRayne 2	Xbox, PS2, PC	October 2004
Advent Rising	Xbox, PC	May 2005
Psychonauts	Xbox, PS2, PC	April, July 2005
Teen Titans	GBA	October 2005
Infected	PSP	November 2005
Aeon Flux	Xbox, PS2	November 2005
Teen Titans	GBA	February 2006
Age of Empires: The Age of Kings	DS	February 2006
Guilty Gear Dust Strikers	DS	April 2006
JAWS 'Unleashed'	Xbox, PS2, PC	May 2006
MechAssault: Phantom War	DS	September 2006
Guilty Gear Judgment	PSP	September 2006

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	Selected
Titles Platform Launch Date	Teen Titans 2 GBA October 2006 Nacho Libre DS October 2006 Cooking Mama: Cook Off Wii March 2007 Bust-A-Move Bash! Wii April 2007 The New York Times Crosswords DS May 2007 Nancy Drew DS September 2007 Holly Hobbie & Friends DS October 2007 Zoo Hospital DS October 2007 Kengo: Legend of the 9 Xbox 360 September 2007 Cooking Mama 2: Dinner with Friends DS November 2007 Nanostray 2 DS February 2008 Eco-Creatures: Save the Forest DS March 2008 Wild Earth: African Safari Wii April 2008 BlastWorks: Build, Trade, Destroy Wii May 2008 Wonderworld Amusement Park Wii June 2008 Cooking Mama Cook Off 2 Wii June 2008 Major Minor's Majestic March Wii Holiday 2008 Our House Wii Holiday 2008 Cake Mania Wii Holiday 2008
Peripheral Products	

Our peripheral products consist principally of our back catalog TV Arcade plug-and-play products. These products are stand-alone games that connect directly into television sets with standard RCA cables. These are battery operated and require no additional hardware or software. In 2006, we acted as a developer and manufacturer of Konami's Strawberry Shortcake™, Dance Dance Revolution®, and Dance Dance Revolution® Disney Mix for Konami. These Plug 'N Play products combine the high-energy dance gameplay of Konami's hit Dance Dance Revolution® (DDR) video game franchise with characters and music from each property.

Product Development

Prior to initiating the development of a video game title, we perform market research, studio due diligence and financial analyses. A title must then be approved by our "green light" committee comprised of members from our executive, product development, finance, sales and marketing and legal/business affairs teams before being accepted for publication. Once accepted, the title is evaluated at regular milestones to ensure it is progressing on time, according to specifications and on budget. In accordance with our current strategy, we will concentrate on procuring handheld products, value products, and opportunistically pursuing console titles.

We primarily use third party development studios to create our video game products. We carefully select third parties to develop video games based on their capabilities, suitability, availability and cost. We usually have broad rights to commercially utilize products created by the third party developers we work with. Development contracts are structured to provide developers with incentives to provide timely and satisfactory performance by associating payments with the achievement of substantive development milestones, and by providing for the payment of royalties to them based on sales of the developed product, only after we recoup development costs. We have worked, and continue to work, with independent third party developers, such as:

- Interactive;
 - Budcat Creations;
- Productions;
 - Double Fine
 - Gorilla Systems
- Inc.;

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Multimedia;

- Shin 'En

Corporation.

- Torus Games; and
- Taito

On November 7, 2007, we announced the creation of an internal development facility to be based in Los Angeles. The studio will add technical and design skills to the company's overall operation and specifically focus on products and properties for the casual gamer. We estimate that this studio will develop a small number of our titles annually.

The development process for video games involves working with platform manufacturers from the initial game concept phase through approval of the final product. During this process, we work closely with manufacturers to ensure that the title undergoes careful quality assurance testing. Each platform manufacturer requires that the software and a prototype of each title, together with all related artwork and documentation, be submitted for its pre-publication approval. This approval is generally discretionary.

Intellectual Property

Platform Licenses

Hardware platform manufacturers require that publishers obtain a license from them to publish titles for their platforms. We currently have non-exclusive licenses from Nintendo for DS, GBA, GameCube and Wii, from Sony for PS2 and PSP and from Microsoft for Xbox and Xbox 360. Each license generally extends for a term of between two to four years and is terminable under a variety of events. Each license allows us to create one or more products for the applicable system, and requires us to pay a per-unit license fee and/or royalty payment from the title produced and may include other compensation or payment terms. Publishers are not required to obtain licenses for publishing video game software for PCs. All of the hardware manufacturers approve each of the titles we submit for approval on a title-by-title basis, at their discretion.

Licenses From Third Parties

While we develop original titles, most of our titles are based on rights, licenses and properties, including copyrights and trademarks, owned by other third parties. Even our original titles usually include some rights or properties from third parties. License agreements with third parties generally extend for a term of between two to three years, are limited to specific territories or platforms, and are terminable under a variety of events. Several of our licenses are exclusive within particular territories or platforms. The licensors often have strict approval and quality control rights. Typically, we are obligated to make minimum guaranteed royalty payments over the term of these licenses and advance payments against these guarantees, but other compensation or payment terms such as milestone payments, are also common. From time to time, we may also license other technologies from third-party developers for use in our products, which also are subject to royalties and other types of payment.

Licenses To Third Parties

As we create original titles we may decide to license rights to third parties, sometimes on an exclusive basis, in order to generate publicity or market demand for our titles, to generate additional revenue related to complementary products or a combination of these factors. For example, in regards to our BloodRayne franchise, we have sold the movie rights, entered into a strategy guide deal and licensed a comic book series, resin statues and an apparel line.

Manufacturing

Sony, Nintendo and Microsoft control the manufacturing of our products that are compatible with their respective video game consoles, as well as the manuals and packaging for these products, and ship the finished products to us for distribution. Video games for Microsoft, Nintendo and Sony game

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consoles consist of proprietary format CD-ROMs or DVD-ROMs and are typically delivered to us within the relatively short lead time, of approximately two to three weeks. Sony PSP products adhere to a similar production time frame, but use a proprietary media format called a Universal Media Disc, or UMD.

With respect to GBA and DS products, which use a cartridge format, Nintendo typically delivers these products to us within 45 to 60 days after receipt of a purchase order. For our peripheral offerings we use third party manufacturers who typically deliver these products to us within three to five weeks from the time production commences.

Initial production quantities of individual titles are based upon estimated retail orders and consumer demand. At the time a product is approved for manufacturing, we must generally provide the platform manufacturer with a purchase order for that product, and an irrevocable letter of credit for the entire purchase price, or cash in advance. To date, we have not experienced any material difficulties or delays in the manufacture and assembly of our products. However, manufacturers' difficulties, which are beyond our control, could impair our ability to bring products to the marketplace in a timely manner.

Sales and Marketing

North America

Historically, our marketing programs principally supported our premium game titles. While we support most of our titles in some manner, those with the most potential will have long lead-time, multi-faceted marketing programs designed to generate enthusiasm and demand. Specific consumer marketing strategies we may employ include: TV, radio and print advertising; web site and online marketing; demo distribution; promotions and cross-promotions with third parties; and point-of-purchase advertising. Our shift in strategic focus away from a reliance on big budget console titles has resulted in less reliance on marketing and significantly lower marketing expenditures.

Additionally, we customize public relations programs that are designed to create awareness with all relevant audiences, including core gamers and mass entertainment consumers. To date, our public relations efforts have resulted in significant coverage for our company and individual titles in computer and video game publications, such as Electronic Gaming Monthly, Game Informer, GamePro, Nintendo Power, PlayStation Magazine and Official Xbox Magazine, as well as major newspapers, magazines and broadcast outlets, such as CNN, USA Today, Wired, Maxim, Newsweek, The New York Times and TV Guide, among others. We also host media events throughout the year at which print, broadcast and online journalists can preview, review and evaluate our products prior to their release.

In addition to regular face-to-face meetings and communications with our sales force, we employ extensive trade marketing efforts including: direct marketing to buyers and store managers; trade shows; various store manager shows; and distribution and sales incentive programs.

We sell our products primarily to large retail chains, specialty retail stores, video game rental outlets and distributors. Our sales team has strong relationships with major retailers and communicates with them frequently. To supplement our sales team, we currently utilize six sales representative organizations located throughout the United States. The firms we use were chosen based on their performance and retailer relationships. On average, two sales representatives per organization are assigned to our accounts. It is customary for the sales representatives and resellers of our games who are assigned specific customers to also distribute games produced by other manufacturers. Distribution channels are dominated by a select group of companies, and a publisher's access to retail shelf space is a significant competitive factor.

International

As the global gaming market continues to grow, we believe that international markets represent a significant growth opportunity for our business. Over the last two years, we have expanded our

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international presence and in late fiscal year 2005 we established a new office in the United Kingdom and entered into a license and distribution agreement with a leading international publisher for distribution in Europe and the PAL territories. Under this agreement the publisher fulfills all sales, marketing and distribution needs for our multi-format product line-up. Our first sales under this agreement were realized in early 2006 and have generated revenues of \$17.3 million through October 31, 2007. We are also looking to develop similar distribution relationships in Asia Pacific and Japan.

Customers

Our customers are comprised of national and regional retailers, specialty retailers and video game rental outlets. We believe we have developed close relationships with a number of retailers including Best Buy, Circuit City, GameStop, Target, Toys ‘‘R’’ Us and Wal-Mart. We also have strong relationships with Cokem, Jack of All Games, a subsidiary of Take-Two Interactive Software, Inc., Ingram and SVG, who act as resellers of our products to smaller retail outlets. For the fiscal year ended 2007, our most significant customers were GameStop, Wal-Mart and Best Buy, which accounted for approximately 21%, 14% and 10% of our net revenue, respectively.

Competition

In general, our products compete with other forms of entertainment for the leisure time and discretionary spending of consumers. These forms include motion pictures, television and music. More specifically, the market for interactive entertainment products is highly competitive and relatively few products achieve significant market acceptance. We continue to face significant competition with respect to our products, which may also result in price reductions, reduced gross margins and loss of market share. Many of our competitors have significantly greater financial, marketing and product development resources than we do.

With respect to our video game products, we compete with many other third party publishers in both the handheld, console and value segments. We expect that competition may increase in the future.

Current and future competitors may be able to:

- respond more quickly to new or emerging technologies or changes in customer preferences;
- carry larger inventories;
- gain access to wider distribution channels;
- undertake more extensive marketing campaigns;
- adopt more aggressive pricing policies;
- devote greater resources to securing the rights to valuable licenses and relationships with leading software developers;
- maintain better relationships with licensors and secure more valuable licenses;
- make higher royalty payments; and
- secure more and

better shelf space.

Competitive factors such as the foregoing may have a material adverse effect on our business.

Seasonality

The interactive entertainment business is highly seasonal with sales typically higher during the peak holiday selling season during the calendar year's fourth quarter. Traditionally, the majority of our sales for this key selling period ship in our fiscal fourth and first quarters, which end on October 31st and January 31st, respectively. Significant working capital is required to finance the manufacturing of inventory of products that ship during these quarters.

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Employees

We had 64 full-time employees in the United States and 6 full-time employees in the United Kingdom as of January 26, 2008. We have not experienced any work stoppages and consider our relations with our employees to be good.

Item 1A. Risk Factors.

Our business and operations are subject to a number of risks and uncertainties as described below. However, the risks and uncertainties described below are not the only ones we face. Additional risks and uncertainties that we are unaware of, or that we may currently deem immaterial, may become important factors that harm our business, financial condition or results of operations. If any of the following risks actually occur, our business, financial condition or results of operations could suffer.

We have experienced recent net losses and we may incur future net losses which may cause a decrease in our stock price.

We incurred net losses of \$4.8 million, \$5.4 million, and \$70.9 million in fiscal years 2007, 2006 and 2005, respectively. For fiscal year 2005, the net loss was due to weak sales across all of our product lines, which resulted in significant reserves relating to capitalized costs, increased provisions in price protection and other allowances. In 2007 and 2006, the loss is primarily the result of revenues and resulting gross margins that were not sufficient to meet operating expenses. The 2006 loss was also the result of impairment charges and higher than normal legal expenses. Going forward, we may not be able to generate revenues sufficient to offset our costs, and may sustain further net losses in future periods. In addition, if we do become profitable, we may not be able to sustain or increase our profitability. Continued losses, or an inability to sustain profitability, may have an adverse effect on our future operating prospects and stock price.

We have experienced volatility in the price of our stock.

The price of our common stock has experienced significant volatility over the last three years, and such prices may be higher or lower than the price paid for our shares, depending on many factors, some of which are beyond our control and may not be directly related to our operating performance. These factors include, but are not limited to, the following:

- price and volume fluctuations in the overall stock market from time to time;
- actual or anticipated changes in our earnings or fluctuations in our operating results or changes in the expectations of securities analysts;
- our, or a competitor's, announcement of new products, services or technological innovations;
- departures of key personnel;
- general economic, political and market conditions and trends;
- risks associated with possible disruption in our operations due to terrorism; or
- other risks and uncertainties as may be detailed from time to time in our public announcements and Securities and Exchange

Commission filings.

For example, the market price of our stock has fluctuated widely over the last fiscal year. Between November 1, 2006, and October 31, 2007, the closing sale price of our common stock ranged between a high of \$2.36 and a low of \$1.25, experiencing greater volatility over that time than most of the market did. The historic market price of our common stock may not be indicative of future market prices. We may not be able to sustain or increase the value of our common stock. Further declines in the market price of our stock could adversely affect our ability to retain personnel with stock incentives, to acquire businesses or assets in exchange for stock and/or to conduct future financing activities with or involving our common stock.

In addition, purchases or sales of large quantities of our stock could have an unusual effect on our stock price.

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If we fail to maintain an effective system of internal controls, we may not be able to accurately report our financial results. As a result, current and potential stockholders could lose confidence in our financial reporting, which could have a negative market reaction.

Section 404 of the Sarbanes-Oxley Act of 2002 requires our management to report on, and may require our independent registered public accounting firm to attest to, the effectiveness of our internal control over financial reporting. The initial deadline for us to become compliant with Section 404 was October 31, 2005. As of such date, we were compliant and have implemented an ongoing program to perform the system and process evaluation and testing necessary to continue to comply with these requirements. Accordingly, we continue to incur expenses and will devote management resources to Section 404 compliance as necessary. Further, effective internal controls and procedures are necessary for us to provide reliable financial reports. If our internal controls and procedures become ineffective, we may not be able to provide reliable financial reports, our business and operating results could be harmed and current and potential stockholders may not have confidence in our financial reporting.

Our business activities may require additional financing that might not be obtainable on acceptable terms, if at all, which could have a material adverse effect on our financial condition, liquidity and our ability to operate going forward.

Although there can be no assurance, our management believes that based on our current plan there are sufficient capital resources from operations, including our factoring and purchase order financing arrangements, to finance our operational requirements through at least the next twelve months. If we continue to incur operating losses, or if unforeseen events occur that would require additional funding, we may need to raise additional capital or incur debt to fund our operations. We would expect to seek such capital through sales of additional equity or debt securities and/or loans from financial institutions, but there can be no assurance that funds will be available to us on acceptable terms, if at all, and any sales of additional securities will be dilutive to investors.

Failure to obtain financing or obtaining financing on unfavorable terms could result in a decrease in our stock price and could have a material adverse effect on future operating prospects, or require us to significantly reduce operations.

We are the subject of litigation, including a securities class action and other shareholder lawsuits.

The Company and certain of its current and former officers and directors are defendants in a securities class action and other shareholder lawsuits. While we intend to vigorously defend ourselves in these actions, we cannot predict the outcome of such lawsuits. We may also in the future be subject to additional class action suits, other litigation or regulatory proceedings. Any expenses incurred in connection with existing or additional potential litigation or proceedings or any adverse resolution of current and potential litigation or proceedings could have a material adverse effect on our business, results of operations, cash flows and financial condition. Further, any litigation proceeding or action may be time consuming, and it may distract our management from the conduct of our business.

We may be unable to complete the settlement of our class action and other shareholder litigation.

In October 2007, we reached agreements to settle certain litigations pending in the United States District Court, District of New Jersey: (i) a securities class action brought on behalf of a purported class of purchasers of the Company's securities, (ii) a private securities action filed by Trinad Capital Master Fund, Ltd., and (iii) a second action filed by Trinad purportedly on behalf of the Company. These settlements require notice to the shareholder class and/or court approval to become effective. We have no assurance that the court will approve these settlements, and if it does not, we may be forced to revert back to disputing the class claims, which may cause us to incur significant costs.

In addition, stockholders may decide to opt-out of the class action settlement and bring separate actions against the Company, which actions could have a material adverse effect on our business, results of operations, cash flows and financial condition.

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The issuance of stock in connection with our class action settlement will result in dilution to existing stockholders and may cause our stock price to decline.

Under the terms of the settlement agreement in the securities class action, we are required to contribute shares of our common stock with a market value of \$2.5 million. The shares being contributed to the settlement will be distributed to the settlement class if and when the court grants final approval to the settlement and the settlement becomes effective. At this time, we cannot estimate the timing of the issuance or the exact number of shares that will be contributed to the settlement, however, it will not be less than 1.8 million shares. Further, if the average closing bid price of our common stock for the 20 days prior to the settlement becoming effective is less than \$1.37, we will have to issue additional shares to fulfill our obligation under the settlement, or could, under certain circumstances, determine not to conclude the settlement and revert back to disputing the class claims. The issuance of these shares will be dilutive to investors and may hurt our stock price.

We may not be able to maintain our listing on the Nasdaq Capital Market.

Our common stock currently trades on the Nasdaq Capital Market. This market has continued listing requirements that we must maintain to avoid delisting. The standards include, among others, minimum bid price requirements and any of (i) a minimum stockholders' equity or (ii) minimum market value of our stock or minimum net income. Our results of operations and our fluctuating stock price directly impact our ability to satisfy these listing standards. In the event we are unable to maintain these listing standards, we may be subject to delisting.

A delisting from Nasdaq would result in our common stock being eligible for listing on the Over-The-Counter Bulletin Board (the "OTCBB"). The OTCBB is generally considered to be a less efficient system than markets such as Nasdaq or other national exchanges because of lower trading volumes, transaction delays and reduced security analyst and news media coverage. These factors could contribute to lower prices and larger spreads in the bid and ask prices for our common stock. Additionally, trading of our common stock on the OTCBB may make us less desirable to institutional investors and may, therefore, limit our future equity funding options and could negatively affect the liquidity of their investment by our stockholders.

Customer accommodations could materially and adversely affect our business, results of operations, financial condition, and liquidity.

When demand for our offerings falls below expectations, we may negotiate accommodations to retailers or distributors in order to maintain our relationships with our customers and access to our sales channels. These accommodations include negotiation of price discounts and credits against future orders commonly referred to as price protection. At the time of product shipment, we establish reserves for price protection and other similar allowances. These reserves are established according to our estimates of the potential for markdown allowances based upon historical rates, expected sales, retailer inventories of products and other factors. We cannot predict with certainty whether existing reserves will be sufficient to offset any accommodations we will provide, nor can we predict the amount or nature of accommodations that we will provide in the future. If actual accommodations exceed our reserves, our earnings would be reduced, possibly materially. Any such reduction may have an adverse effect on our business, financial condition or results of operations. The granting of price protection and other allowances reduces our ability to collect receivables and impacts our availability for advances from our factoring arrangement. The continued granting of substantial price protection and other allowances may require additional funding sources to fund operations, but there can be no assurance that such funds will be available to us on acceptable terms, if at all.

Increased competition for limited shelf space and promotional support from retailers could affect the success of our business and require us to incur greater expenses to market our products.

Retailers typically have limited shelf space and promotional resources, such as circulars and in-store advertising, to support any one product among an increasing number of newly introduced entertainment offerings.

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Competition for retail support and shelf space is expected to increase, which may require us to increase our marketing expenditures or reduce prices to retailers. Competitors with more extensive lines, popular products and financial resources frequently have greater bargaining power with retailers. Accordingly, we may not be able to achieve or maintain the levels of support and shelf space that our competitors receive. As a result, sales of our products may be less than expected, which would have a material and adverse effect on our business, financial condition and results of operations.

The loss of any of our key customers could adversely affect our sales.

Our sales to Game Stop, Wal-Mart, and Best Buy accounted for approximately 21%, 14% and 10% of our net revenue for the fiscal year 2007, respectively. Although we seek to broaden our customer base, we anticipate that a small number of customers will continue to account for a large concentration of our sales given the consolidation of the retail industry. We do not have written agreements in place with several of our major customers. Consequently, our relationship with these retailers could change at any time. Our business, results of operations and financial condition could be adversely affected if:

- we lose any of our significant customers;
- any of these customers purchase fewer of our offerings; or
- we experience any other adverse change in our relationship with any of these customers.

Significant competition in our industry could continue to adversely affect our business.

We cannot be assured that we will be able to successfully compete against our current or future competitors or that competitive pressures will not have a material adverse effect on our business, results of operations or financial condition. The market for interactive entertainment products is highly competitive and relatively few products achieve significant market acceptance. We face significant competition with respect to our products, which may also result in price reductions, reduced gross margins and loss of market share. Many of our competitors have significantly greater financial, marketing and product development resources than we do. As a result, current and future competitors may be able to:

- respond more quickly to new or emerging technologies or changes in customer preferences;
- undertake more extensive marketing campaigns;
- devote greater resources to secure rights to valuable licenses and relationships with leading software developers;
- gain access to wider distribution channels; and
- have better access to prime shelf space.

With respect to our video game products, we compete with many other third party publishers in both our handheld and console market segments. In addition, console and handheld manufacturers, such as Microsoft, Nintendo and Sony, publish software for their respective platforms. Further, media companies and film studios are increasing their focus

on the video game software market and may become significant competitors. We expect competition to increase as more competitors enter the video game market.

Our business is dependent on the viability of console hardware.

Our business depends on hardware on which consumers play our games. Our business can be adversely affected by hardware as follows:

Hardware shortages. The new generation console hardware systems have experienced hardware shortages, including Nintendo's Wii console. Hardware shortages generally negatively affect the sales of video games since consumers do not have consoles on which to play the games.

Hardware pricing. The new generation console systems are priced higher than each of their predecessor platforms. The cost of the hardware could adversely affect their sales, which could negatively affect sales of our products for these platforms since consumers need a platform in order to play our games.

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Software pricing. Software prices for the new generation console games are higher than prices for games for the predecessor platforms. There is no assurance that consumers will continue to pay the higher prices of these games.

Increasing development costs. The introduction of the new generation platforms has required the development of new software to play on such consoles and new technologies to create such software. Because the new generation consoles have greater complexity and capabilities than the predecessor platforms, costs are higher to develop games for new generation consoles. Greater costs can lead to lower operating margins, negatively affecting our profitability.

Termination or modification of our agreements with hardware manufacturers, who are also competitors and frequently control the manufacturing of our titles, may adversely affect our business.

We are required to obtain a license in order to develop and distribute software for each of the manufacturers of video game hardware. We currently have licenses from Sony to develop products for PlayStation, PlayStation 2 and PSP, from Nintendo to develop products for the GBA, GameCube, the DS, Wii and Micro and from Microsoft to develop products for the Xbox and the Xbox 360. These licenses are non-exclusive, and as a result, many of our competitors also have licenses to develop and distribute video game software for these systems. These licenses must be periodically renewed, and if they are not, or if any of our licenses are terminated or adversely modified, we may not be able to publish games for such platforms or we may be required to do so on less attractive terms.

Our contracts with these manufacturers grant them approval rights over new products and often also grant them control over the manufacturing of our products. While we believe our relationships with these manufacturers are good, the potential for delay or refusal to approve or support our products exists, particularly since these manufacturers are also video game publishers and hence are also our competitors. We may suffer an adverse effect on our business if these manufacturers:

- do not approve a project for which we have expended significant resources;
- refuse or are unable to manufacture or ship our products;
- increase manufacturing lead times or delay the manufacturing of our products; or
- require us to take significant risks in prepaying and holding an inventory of products.

We may be unable to develop and publish new products if we are unable to secure or maintain relationships with third party video game software developers.

We utilize the services of independent software developers to develop the majority of our video games. Consequently, our success in the video game market depends on our continued ability to obtain or renew product development agreements with quality independent video game software developers. However, we cannot assure you that we will be able to obtain or renew these product development agreements on favorable terms, or at all, nor can we assure you that we will be able to obtain the rights to sequels of successful products which were originally developed for us by independent video game software developers.

Many of our competitors have greater financial resources and access to capital than we do, which puts us at a competitive disadvantage when bidding to attract independent video game software developers. We may be unable to secure or maintain relationships with quality independent video game software developers if our competitors can offer

them better shelf access, better marketing support, more development funding, higher royalty rates, more creative control or other advantages. Usually, our agreements with independent software developers are easily terminable if either party declares bankruptcy, becomes insolvent, ceases operations or materially breaches its agreement.

In addition, many independent video game software developers have limited financial resources. Many are small companies with a few key individuals without whom a project may be difficult or impossible to complete. Consequently, we are exposed to the risk that these developers will go out of business before completing a project, lose key personnel or simply cease work on a project for which we have hired them.

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If we are unable to maintain or acquire licenses to intellectual property, we may publish fewer titles and our revenue may decline.

Many of our video game titles are based on or incorporate intellectual property and other character or story rights acquired or licensed from third parties. We expect that many of our future products will also be based on intellectual property owned by others. The cost of acquiring these licenses is often high, and competition for these licenses is intense. Many of our competitors have greater resources to capitalize on licensing opportunities. Our licenses are generally limited in scope to specific platform and/or geographic territories and generally last for two to three years. We may not be able to obtain new licenses, renew licenses when they expire or include new offerings under existing licenses. If we are unable to obtain new licenses or maintain existing licenses that have significant commercial value, at reasonable costs, we may be unable to sustain our revenue growth in the future other than through sales or licensing of our independently created material.

If we are unable to successfully introduce new products on a timely basis, or anticipate and adapt to rapidly changing technology, including new hardware platform technology, our business may suffer.

A significant component of our strategy is to continue to bring new and innovative products to market, and we expect to incur significant development, licensing and marketing costs in connection with this strategy.

The process of introducing new products or product enhancements is extremely complex, time consuming and expensive, and will become more complex as new platforms and technologies emerge. In the event we are not successful in developing new titles and other products that gain wide acceptance in the marketplace, we may not recoup our investment costs in these new products, and our business, financial condition and results of operations may be materially adversely affected.

Furthermore, interactive entertainment platforms are characterized by rapidly changing technology. We must continually anticipate the emergence of, and adapt our products to, new interactive entertainment platforms and technologies. The introduction of new technologies, including new console and handheld technology, software media formats and delivery channels, could render our previously released products obsolete, unmarketable or unnecessary. In addition, if we incur significant expense developing products for a new system that is ultimately unpopular, sales of these products may be less than expected and we may not be able to recoup our investment. Conversely, if we choose not to publish products for a new system that becomes popular, our revenue growth, reputation and competitive position may be adversely affected. Even if we are able to accurately predict which video game platforms will be most successful, we must deliver and market offerings that are accepted in our extremely competitive marketplace.

A significant portion of our revenue in 2007 was generated from games based on one licensed franchise.

Approximately 37% of our net revenues in 2007 were generated from two games based on the Cooking Mama franchise, developed for use on the Nintendo DS and Wii. We licensed the rights to publish these games from a third party. We have secured rights to publish sequels to these games, which are scheduled for release in 2008 and 2009, however we cannot guarantee that the sequels will be as successful as the original versions. If the sequels are not successful, this may have a significant impact on our revenues. In addition, even if successful, we may be unable to secure the rights to publish further sequels to these games, which may adversely affect our business and financial performance.

Intellectual property claims may increase our product costs or require us to cease selling affected products which could adversely affect our earnings and sales.

Development of original content, including publication and distribution, sometimes results in claims of intellectual property infringement. Although we make efforts to ensure our products do not violate the intellectual property rights of others, it is possible that third parties still may allege infringement. These claims and any litigation resulting from these claims, could prevent us from selling

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the affected product, or require us to redesign the affected product to avoid infringement or obtain a license for future sales of the affected product. Any of the foregoing could have a material adverse effect on our business, financial condition, results of operations and future business prospects. Any litigation resulting from these claims could require us to incur substantial costs and divert significant resources, including the efforts of our technical and management personnel.

Our intellectual property is vulnerable to misappropriation and infringement which could adversely affect our business prospects.

Our business relies heavily on proprietary intellectual property, whether our own or licensed from third parties. Despite our efforts to protect our proprietary rights, unauthorized parties may try to copy our products, or obtain and use information that we regard as proprietary. In addition, the laws of some foreign countries may not protect our proprietary rights to as great an extent as the law of the United States. Our rights and the additional steps we have taken to protect our intellectual property may not be adequate to deter misappropriation, particularly given the difficulty of effectively policing unauthorized use of our properties. If we are unable to protect our rights in intellectual property, our business, financial condition or results of operations could be materially adversely affected.

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

The products that we publish and distribute are complex and may contain undetected errors when first introduced or when new versions are released. Despite extensive testing prior to release, we cannot be certain that errors will not be found in new products or releases after shipment, which could result in loss of or delay in market acceptance. This loss or delay could significantly harm our business and financial results.

Rating systems for digital entertainment software, potential legislation and consumer opposition could inhibit sales of our products.

Trade organizations within the video game industry require digital entertainment software publishers to provide consumers with information relating to graphic violence, profanity or sexually explicit material contained in software titles, and impose penalties for noncompliance. Certain countries have also established similar rating systems as prerequisites for sales of digital entertainment software in their countries. In some instances, we may be required to modify our products to comply with the requirements of these rating systems, which could delay the release of those products in these countries. We believe that we comply with such rating systems and properly display the ratings and content descriptions received for our titles. Several proposals have been made for legislation to regulate the digital entertainment software, broadcasting and recording industries, including a proposal to adopt a common rating system for digital entertainment software, television and music containing violence or sexually explicit material, and the Federal Trade Commission has issued reports with respect to the marketing of such material to minors. Consumer advocacy groups have also opposed sales of digital entertainment software containing graphic violence or sexually explicit material by pressing for legislation in these areas, including legislation prohibiting the sale of certain “M” rated video games to minors, and by engaging in public demonstrations and media campaigns. Retailers may decline to sell digital entertainment software containing graphic violence or sexually explicit material, which may limit the potential market for our “M” rated products, and adversely affect our operating results. If any groups, whether governmental entities, hardware manufacturers or advocacy groups, were to target our “M” rated titles, we might be required to significantly change or discontinue a particular title, which could adversely affect our business.

Our business is subject to risks generally associated with the entertainment industry, and we may fail to properly assess consumer tastes and preferences, causing product sales to fall short of expectations.

Our business is subject to all of the risks generally associated with the entertainment industry and, accordingly, our future operating results will depend on numerous factors beyond our control, including the popularity, price and timing of new hardware platforms being released; economic,

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political and military 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 be predicted. A decline in the popularity of certain game genres or particular platforms could cause sales of our titles to decline dramatically. The period of time necessary to develop new game titles, obtain approvals of platform licensors and produce finished products is unpredictable. During this period, consumer appeal for a particular title may decrease, causing product sales to fall short of expectations.

We have developed international operations, which may subject us to economic, political, regulatory and other risks.

Continuing our international operations may subject us to many risks, including:

- in maintaining or finding a suitable distribution partner;
 - political instability;
 - foreign and domestic laws and regulations;
 - and domestic legal and regulatory requirements or policies resulting in burdensome government controls, tariffs, restrictions, embargoes or export license requirements;
 - fluctuations;
 - staffing and managing our international operations;
 - foreign intellectual property laws making it more difficult to protect our properties from appropriation by competitors;
 - potentially adverse tax treatment;
 - distributors;
 - collecting our accounts receivable; and
 - business relationships.
- difficulty
 - economic and
 - compliance with
 - changes in foreign
 - currency
 - difficulties in
 - less favorable
 -
 - difficulties with
 - difficulties
 - relying on limited
- Our failure to manage or address any of these could adversely affect our business.

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 “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 us 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 we anticipate, which could cause our product sales to fall below our expectations. If our competitors develop more successful products or offer competitive products at lower price, or if we do not continue to develop consistently high-quality and well received products, our revenue,

margins, and profitability will decline.

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

The market for technical, creative, marketing and other personnel essential to the development and marketing of our products and management of our businesses is extremely competitive. We are frequently competing for this talent with other companies with greater resources. Our ability to operate within this highly competitive interactive entertainment industry is dependent upon our ability to attract and retain our employees. If we cannot successfully recruit and retain the employees we need, or replace key employees following their departure, our ability to develop and manage our businesses will be impaired.

Our failure to manage or adequately address any one or more of these rights could result in our business suffering a material adverse effect.

Item 1B. Unresolved Staff Comments.

Not applicable.

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Item 2. Properties.

We lease 21,250 square feet of office, development and storage space located at 160 Raritan Center Parkway, Edison, NJ 08837. The lease, which costs approximately \$28,510 per month, plus taxes, insurance and operating costs, expires on October 31, 2009.

We lease 900 square feet of office space in Europe, located at City Point, Temple Gate, BS16PL, Bristol, UK. This lease which costs approximately \$7,200 per month and is renewable on a six month basis.

As of January 4, 2008, we lease 5,974 square feet of office space at 2121 Cloverfield Blvd., Santa Monica, CA 90404 for our development studio. The lease, which costs approximately \$13,740 per month, plus taxes, insurance and operating costs, expires on December 31, 2010.

Item 3. Legal Proceedings.

As previously disclosed, during the quarter ended October 31, 2007, we entered into agreements to settle certain litigations pending in the United States District Court, District of New Jersey: a securities class action brought on behalf of a purported class of purchasers of the Company's securities, a private securities action filed by Trinad Capital Master Fund, Ltd., and a second action filed by Trinad purportedly on behalf of the Company.

Under the terms of the settlement agreement in the securities class action, which is subject to notice to the shareholder class and court approval, our insurance carrier will make a cash payment and the we will contribute shares of our common stock with a market value of approximately \$2.5 million. Plaintiffs have not yet filed a motion seeking preliminary approval of the settlement and notice to all class members setting a date for a hearing on the fairness of the settlement. We cannot predict when Plaintiffs will file the motion or when the Court will set the date for a hearing with respect thereto. The shares being contributed to the settlement will be distributed to the settlement class if and when the court grants final approval to the settlement and the settlement becomes effective. Plaintiffs' attorney fees will be paid from the settlement amount.

The settlement of the private securities claim in the action brought by Trinad on its own behalf provides that the Company's insurance carrier will make a cash payment to Trinad, subject to final approval of the class action settlement by the Court.

The settlement agreement in the action filed by Trinad, purportedly on behalf of the Company, will not result in a payment to the Company. Plaintiff's attorneys will not receive any fees in connection with the settlement. As a result of the filing of the lawsuit, the Company has taken actions which it and Trinad believe will benefit our shareholders and address the issues raised in the lawsuit. This settlement is also subject to notice to the Company's shareholders and to court approval.

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

Not applicable.

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Item 6. Selected Financial Data.

The following tables summarize certain selected consolidated financial data, which should be read in conjunction with our audited consolidated financial statements and the notes thereto and with management's discussion and analysis of financial condition and results of operations included elsewhere in this report. All financial information presented reflects as appropriate the 1-for-7 reverse stock split of our common stock, which occurred on December 31, 2004.

		Year Ended October 31					(in thousands, except share data)				
		2007	2006	2005	2004	2003					
Consolidated Statement Of Operations Data:							Net revenues	\$ 50,967	\$ 66,683	\$	
59,716	\$ 120,984	\$ 46,608	Cost of sales (1)	33,682	46,858	61,101	86,242	30,803	Gross		
(loss) profit	17,285	19,825	(1,385)	34,742	15,805	Operating expenses (2)	21,114	22,820			
68,805	22,630	24,545	Operating (loss) income	(3,829)	(2,995)	(70,190)	12,112	(8,740)			
Interest and financing costs, net	1,552	2,371	1,869	2,806	2,077	Other non-operating (income)					
expense (3)	(611)	—	48	19,068	24	Loss before income taxes	(4,770)	(5,366)	(72,107)		
(9,762)	(10,841)	(Benefit) provision for income taxes	—	—	(1,207)	1,424	—	Net (loss)	\$ (4,770)		
\$ (5,366)	\$ (70,900)	\$ (11,186)	\$ (10,841)	Net (loss) attributable to common							
stockholders (4)	\$ (4,770)	\$ (5,366)	\$ (72,000)	\$ (15,388)	\$ (10,841)	Net (loss) attributable to					
common						stockholders per share:					
(0.24)	\$ (3.48)	\$ (1.84)	\$ (4.95)	Weighted average shares outstanding:			Basic and Diluted	\$ (0.20)	\$		
Diluted	23,891,860	22,616,419	20,686,863	8,385,657	2,189,285						

		October 31					In thousands Consolidated Balance Sheet Data:				
		2007	2006	2005	2004	2003					
Cash and cash equivalents		\$ 7,277	\$ 3,794	\$ 2,407	\$ 4,170	\$ 314	Working capital (deficit)				
2,834	977	3,757	8,915	(10,927)	Total assets	16,313	15,011	30,703	43,952	17,611	
Non-current liabilities	1,460	—	—	—	Dividend payable in common stock	—	—	—	1,261	—	
Stockholders' equity (deficiency)	2,591	1,749	4,761	13,785	(15,730)						

(1) Cost of sales, in 2005, includes: (i) charges of \$10.5 million to recognize impairments to the carrying value of products released in 2005; and (ii) \$5.1 million for reserves for slow moving inventory. Cost of sales in 2004 includes charges of \$500,000 to recognize impairments to the carrying value of products released in 2004. (2) Operating expenses include: (i) for 2007, a settlement of litigation and related charges, net of \$2.8 million, a gain from settlement of liabilities of \$0.3 million and a provision for software development costs of \$0.1 million; (ii) for 2006, a gain from settlement of liabilities and other of

Table of Contents \$4.8 million, and a loss in impairment of software development costs of \$2.4 million, (iii) for 2005, a charge for an accounts receivable write-off of \$0.3 million, \$26.3 million to write-off capitalized costs related to video games for which development was stopped or impaired, a provision for severance of \$1.4 million, and a loss of \$1.4 million related to a legal settlement; (iv) for 2004, charges for an accounts receivable write-off of \$0.6 million, non-cash compensation of \$0.3 million, and a gain of \$1.2 million related to the renegotiation of our 2003 litigation settlement; and (v) for 2003, provisions for loss on impairment of software development costs of \$3.7 million for which development was stopped and litigation and settlement costs of \$4.9 million. (3) Other non-operating expense includes: (i) for 2007, a gain from a change in fair value of warrants of \$0.6 million; (ii) for 2005, a realized loss on foreign exchange of \$48,000; (iii) for 2004, expenses related to the merger of \$0.3 million, an unrealized loss on a foreign exchange contract of \$0.3 million and a non-cash charge of \$18.5 million related to the change in fair value of warrants issued in connection with the private placement; and (iv) for 2003, an unrealized loss on a foreign exchange contract of \$24,000. (4) Net (loss) attributable to common stockholders includes: (i) for 2005, a \$1.1 million non-cash charge related to warrants exercised at a discount; and (ii) for 2004, a non-cash charge of \$0.8 million related to a deemed dividend, a preferred stock dividend requirement of \$1.3 million payable in common stock and a \$2.2 million non-cash charge related to the fair value of warrants issued in connection with lock-up agreements by certain stockholders.

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

You should read the following discussion and analysis of our financial condition and results of operations together with "Selected Consolidated Financial Data" and our consolidated financial statements and related notes appearing elsewhere in this annual report on Form 10-K. This discussion and analysis contains forward-looking statements that involve risks, uncertainties and assumptions. The actual results may differ materially from those anticipated in these forward-looking statements as a result of certain factors, including, but not limited to, those set forth under "Risk Factors" and elsewhere in this annual report on Form 10-K.

Overview

We are a provider of interactive entertainment products. We sell our products primarily to large retail chains, specialty retail stores, video game rental outlets and distributors. We also sell our products internationally through distribution agreements with other publishers. We have developed our retail and distribution network over our 20-year history.

We publish video game software for most major interactive entertainment hardware platforms, including Nintendo's Wii, Game Boy Advance, or GBA, DS, Micro and GameCube, Sony's PlayStation 2, or PS2, and PlayStation Portable, or PSP™, Microsoft's Xbox, Xbox 360 and the personal computer, or PC.

Our video game titles are targeted at various demographics at a range of price points, from lower-priced "value" titles to more expensive "premium" titles. In some instances, these titles are based on licenses of well-known properties, and in other cases based on original properties. We collaborate and enter into agreements with content providers and video game development studios for the creation of the majority of our video games.

Majesco Sales Inc. was incorporated in 1986 under the laws of the State of New Jersey. On December 5, 2003, Majesco Sales Inc. completed a reverse merger with Majesco Holdings Inc. (formerly, ConnectivCorp) then a publicly traded company with no active operations. Majesco Holdings Inc. was incorporated in 1998 under the laws of the State of Delaware. As a result of the merger, Majesco Sales Inc. became a wholly-owned subsidiary and the sole operating business of the public company. On April 4, 2005, Majesco Sales Inc. was merged into Majesco Holdings Inc., and Majesco Holdings Inc. changed its name to Majesco Entertainment Company.

During 2006, we revised our business model and shifted our product strategy away from capital intensive premium console games to a focus on lower-cost games for both console and handheld

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systems targeting “mass market” consumers. We believe this strategy allows us to capitalize on our strengths and expertise while reducing some of the cost and risk associated with publishing a large number of premium console titles. We continue to publish titles for popular handheld systems such as the GBA, DS and PSP. We also publish software for Nintendo’s Wii console (released in late 2006) as we believe this platform allows us to develop games within our cost parameters, while enabling us to reach “mass market” consumers. In addition, we continue to opportunistically look for titles to publish on the PC and other home console systems.

Net Revenues. Our revenues are principally derived from sales of our video game titles. We primarily provide video games for the mass market and casual game player. We work with third-party development studios to develop our own proprietary titles and we also license rights to properties from third parties. In 2007, we announced the opening of our own development studio. However, we expect to continue to use third party studios for the significant majority of our development. We have also developed, manufactured and marketed a variety of digital media peripherals and applications including “plug-and-play” video game systems.

Our revenues are recognized net of reserves for price protection and other allowances.

Cost of Sales. Cost of sales consists of product costs and amortization of software development costs and license fees. A significant component of our cost of sales is product costs. These are comprised primarily of manufacturing and packaging costs of the disc or cartridge media, royalties to the platform manufacturer and manufacturing and packaging costs of peripherals. Commencing upon the related product’s release, capitalized software development and intellectual property license costs are amortized to cost of sales.

Gross Profit. Gross Profit is the excess of net revenues over product costs and amortization of software development and license fees. Development and license fees incurred to produce video games are generally incurred up front and amortized to cost of sales. The recovery of these costs and total gross profit is dependent upon achieving a certain sales volume, which varies by title. Our value titles are generally characterized as having lower gross profit margin potential than premium titles as a result of their lower sales price, and carry lower financial risk associated with the recovery of upfront development and license fees as compared with premium game titles.

Product Research and Development Expenses. Product research and development expenses relate principally to our cost of supervision of third-party video game developers, testing new products and conducting quality assurance evaluations during the development cycle. Costs incurred are employee-related, may include equipment and are not allocated to cost of sales.

Selling and Marketing Expenses. Selling and marketing expenses consist of marketing and promotion expenses, the cost of shipping products to customers and related employee costs. A large component of these expenses relate to marketing and promotion expenses, which includes certain customer marketing allowances.

General and Administrative Expenses. General and administrative expenses primarily represent employee related costs, including corporate executive and support staff, general office expenses, professional fees and various other overhead charges. Professional fees, including legal and accounting expenses, typically represent the second largest component of our general and administrative expenses. These fees are partially attributable to our required activities as a publicly traded company, such as SEC filings.

Interest and Financing Costs. Interest and financing costs are directly attributable to our factoring and our purchase-order financing arrangements.

(Benefit) Provision for Income Taxes. Utilization of our net operating loss carryforwards may be subject to a substantial annual limitation due to the “change in ownership” provisions of the Internal Revenue Code. The annual limitation may result in the expiration of net operating loss carryforwards before utilization. Since the Company has a history of losses, a full valuation allowance has been established under the provisions of SFAS No. 109 and the company intends to maintain a valuation allowance for its net operating loss carryforwards until sufficient positive evidence exists to support its reversal.

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Critical Accounting Policies

Our discussion and analysis of the financial condition and results of operations is based upon our consolidated financial statements, which have been prepared in accordance with accounting principles generally accepted in the United States.

The preparation of these consolidated financial statements requires us to make estimates and judgments that affect the reported amounts of assets, liabilities, revenues and expenses, and related disclosure of contingent assets and liabilities. We base our estimates on historical experience and on various other assumptions that are believed to be reasonable under the circumstances, the results of which form the basis for making judgments about the carrying values of assets and liabilities that are not readily apparent from other sources. Actual results could differ materially from these estimates under different assumptions or conditions.

We have identified the policies below as critical to our business operations and to the understanding of our financial results. 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.

Revenue Recognition. We recognize revenue upon the shipment of our product when title and risk of loss are transferred and persuasive evidence of an arrangement exists. In order to recognize revenue, we must not have any continuing obligations and it must also be probable that we will collect the accounts receivable. Revenues, including sales to resellers and distributors, are recognized when these conditions are met.

Reserves for Price Protection and Other Allowances. We generally sell our products on a no-return basis, although in certain instances, we may provide price protection or other allowances on certain unsold products in accordance with industry practices. Price protection, when granted and applicable, allows customers a partial credit with respect to merchandise unsold by them. Revenue is recognized net of estimates of these allowances. 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 advertisement, are generally reflected as selling and marketing expenses. We estimate potential future product price protection and other discounts related to current period product revenue. Generally our price protection for premium-priced titles is higher than that needed for our value titles.

Our reserves for price protection and other allowances fluctuate over periods as a result of a number of factors including analysis of historical experience, current sell-through of retailer inventory of our products, current trends in the interactive entertainment market, the overall economy, changes in customer demand and acceptance of our products and other related factors. 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. However, actual allowances granted could materially exceed our estimates as unsold products in the distribution channels are exposed to rapid changes in consumer preferences, market conditions, technological obsolescence due to new platforms, product updates or competing products. For example, the risk of requests for allowances may increase as consoles pass the midpoint of their lifecycle and an increasing number of competitive products heighten pricing and competitive pressures. While management believes it can make reliable estimates regarding these matters, these estimates are inherently subjective. Accordingly, if our estimates change, this will result in a change in our reserves, which would impact the net revenues and/or selling and marketing expenses we report. For the twelve month periods ended October 31, 2007, 2006, and 2005, we provided allowances for future price protection and other allowances of \$2.0 million, \$3.8 million, and \$15.1 million, respectively. The fluctuations in the provisions reflected our estimates of future price protection based on the factors discussed above. We do not have significant exposure to credit risk as we

factor our receivables to a third party that generally buys our receivables without recourse.

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Inventory. Inventory, which consists principally of finished goods, is stated at the lower of cost as determined by the first-in, first-out method, or market. We estimate the net realizable value of slow-moving inventory on a title-by-title basis and charge the excess of cost over net realizable value to cost of sales.

Software development costs and prepaid license fees. Software development costs include development fees, most often in the form of milestone payments made to independent video game developers for development services. Software development costs are capitalized once technological feasibility of a product is established and it is determined that such costs should be recoverable against future revenues. For products where proven game engine technology exists, this may occur early in the development cycle. Technological feasibility is evaluated on a product-by-product basis. Amounts related to software development that are not capitalized are charged immediately to product research and development costs. Prepaid license fees represent license fees to holders for the use of their intellectual property rights in association with our products. Minimum guaranteed royalty payments for intellectual property licenses are initially recorded as an asset (prepaid license fees) and a current liability (accrued royalties payable) at the contractual amount upon execution of the contract when no significant performance remains with the licensor. Capitalized software development costs classified as non-current relate to titles for which we estimate the release date to be more than one year from the balance sheet date.

Commencing upon a related product's release, capitalized software development costs and prepaid license fees are amortized to cost of sales based upon the higher of (i) the ratio of current revenue to total projected revenue or (ii) the straight-line method. The amortization period is usually no longer than one year from the initial release of the product. The recoverability of capitalized software development costs and prepaid license fees is evaluated based on the expected performance of the specific products to which the costs relate. The following criteria are used to evaluate expected product performance: historical performance of comparable products using comparable technology; orders for the product prior to its release; and estimated performance of a sequel product based on the performance of the product on which the sequel is based. 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 to complete and publish the product. If revised forecasted or actual product sales are less than, and/or revised forecasted or actual costs are greater 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. We recorded an expense of \$0.2 million, \$2.4 million and \$26.3 million for the twelve months ended October 31, 2007, 2006 and 2005, respectively, related to development costs for projects which were either canceled, or for which full recoverability was not expected. In the twelve month periods ended October 31, 2007, 2006 and 2005, we charged \$7.7 million, \$14.6 million, and \$22.7 million, respectively, to cost of sales for amortization of software development costs, prepaid license fees and royalties on products which were sold.

Accounting for Stock-Based Compensation. In December 2004, the Financial Accounting Standards Board "FASB" issued SFAS No. 123 (revised 2004), "Share Based Payment" ("SFAS 123(R)"). SFAS 123(R) requires all share-based payments to employees, including grants of employee stock options, to be recognized in the financial statements based on their fair values. We adopted SFAS 123(R) on November 1, 2005. SFAS 123(R) permits public companies to adopt its requirements using either the modified prospective or modified retrospective transition method. We use the modified prospective transition method, which requires that compensation cost is recognized for all awards granted, modified or settled after the effective date as well as for all awards granted to employees prior to the effective date that remain unvested as of the effective date.

Commitments and Contingencies. The Company accounts for commitments and contingencies in accordance with financial accounting standards board Statement No. 5, Accounting for Contingencies. The company records a liability

for commitments and contingencies when the amount is both probable and reasonably estimable.

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Results of Operations

The following table sets forth our results of operations expressed as a percentage of total revenues:

Year Ended October 31,	2007	2006	2005	Net revenues	100.0 %	100.0 %	100.0 %	Cost of sales			
Product costs	50.9	48.4	64.3	Software development costs and license fees	15.2	21.9	38.0				
Gross (loss) profit	33.9	29.7	(2.3)	Operating expenses				Product research and development			
4.5	3.9	5.7	Selling and marketing	14.6	16.4	40.5	General and administrative	16.4	16.9		
18.3	Depreciation and amortization	0.6	0.6	1.5	Settlements, loss on impairments and other expenses						
(income)	5.3	(3.6)	49.2	Operating loss	(7.5)	(4.5)	(117.5)	Interest and financing costs and			
other non-operating expenses	1.8	3.6	3.2	Loss before income taxes	(9.4)	(8.0)	(120.7)	Benefit			
from income taxes	—	—	(2.0)	Net loss	(9.4)%	(8.0)%	(118.7)%				

The following table sets forth the components of Settlements, loss on impairments and other expenses (gains) for the years ended October 31, 2007, 2006 and 2005.