

MAJESCO HOLDINGS INC

Form POS AM

February 03, 2005

As filed with the Securities and Exchange Commission on February 3, 2005

Registration No. 333-115822

SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

POST-EFFECTIVE AMENDMENT NO. 1 TO

FORM S-1

ON

FORM S-3

REGISTRATION STATEMENT

UNDER

THE SECURITIES ACT OF 1933

MAJESCO HOLDINGS INC.

(Exact Name of registrant as specified in its charter)

Delaware
(State or other jurisdiction of
incorporation or organization)

7372
(Primary Standard Industrial
Classification Code Number)

606-1529524
(IRS Employer Identification
No.)

160 Raritan Center Parkway
Edison, New Jersey 08837
(732) 225-8910

(Address, including zip code, and telephone number, including area code, of registrant's principal executive offices)

Jan E. Chason
Chief Financial Officer
Majesco Holdings Inc.
160 Raritan Center Parkway
Edison, New Jersey 08837
(732) 225-8910

(Name, address, including zip code, and telephone number, including area code, of agent for service)

With Copies to:
Faith L. Charles
Mintz Levin Cohn Ferris

Glovsky and Popeo, P.C.
Chrysler Center
666 Third Avenue
New York, NY 10017
(212) 935-3000

Approximate date of commencement of proposed sale to public: As soon as practicable after this Registration Statement becomes effective.

If the only securities being registered on this Form are being offered pursuant to dividend or interest reinvestment plans, please check the following box.

If any of the securities being registered on this Form are being offered on a delayed or continuous basis pursuant to Rule 415 under the Securities Act of 1933, other than securities offered only in connection with dividend or reinvestment plans, check the following box.

If this Form is filed to register additional securities for an offering pursuant to Rule 462(b) under the Securities Act, check the following box and list the Securities Act registration statement number of the earlier effective registration statement for the same offering.

If this Form is a post-effective amendment filed pursuant to Rule 462(c) under the Securities Act, check the following box and list the Securities Act registration statement number of the earlier registration statement for the same offering.

If delivery of the prospectus is expected to be made pursuant to Rule 434, please check the following box.

The Registrant hereby amends this Registration Statement on such date or dates as may be necessary to delay its effective date until the Registrant shall file a further amendment which specifically states that this Registration Statement shall thereafter become effective in accordance with Section 8(a) of the Securities Act of 1933, as amended, or until the Registration Statement shall become effective on such date as the Securities and Exchange Commission, acting pursuant to Section 8(a), may determine.

Explanatory Note

This Post-Effective Amendment No. 1 to Form S-1 on Form S-3 is being filed to convert the Registration Statement on Form S-1 (No. 333-115822) into a Registration Statement on Form S-3 and to remove shares of common stock sold by certain of the selling stockholders in our secondary public offering completed on January 31, 2005. The Registrant certifies that it has reasonable grounds to believe that it meets all of the requirements for filing on Form S-3.

Subject to completion, dated February 3, 2005

PROSPECTUS

MAJESCO HOLDINGS INC.
160 RARITAN CENTER PARKWAY
EDISON, NEW JERSEY 08837
(732) 225-8910

5,764,253 SHARES OF COMMON STOCK

Selling stockholders identified in this prospectus may sell up to 5,764,253 shares of common stock of Majesco Holdings Inc. This Prospectus covers the sale of such shares from time to time by the selling stockholders. We will not receive any proceeds from the sale of these shares.

Our common stock is quoted on the Nasdaq National Market System under the symbol "MJES." On February 1, 2005, the last reported sale price of the common stock was \$11.75.

INVESTING IN OUR COMMON STOCK INVOLVES A HIGH DEGREE OF RISK. YOU SHOULD PURCHASE SHARES ONLY IF YOU CAN AFFORD A COMPLETE LOSS OF YOUR INVESTMENT. SEE "RISK FACTORS" BEGINNING ON PAGE 4.

Neither the Securities and Exchange Commission nor any state securities commission has approved or disapproved of these securities or passed upon the adequacy or accuracy of this prospectus. Any representation to the contrary is a criminal offense.

The date of this prospectus is February 3, 2005

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You should rely only on the information contained in this prospectus. We have not authorized anyone to provide you with information different from that contained in this prospectus. This document may only be used where it is legal to sell these securities. The information contained in this prospectus is accurate only as of the date of this prospectus, regardless of the time of delivery of this prospectus or of any sale of common stock.

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PROSPECTUS SUMMARY

This summary highlights the most important features of this offering and the information contained elsewhere in this prospectus. You should read the entire prospectus carefully, especially the risks of investing in our common stock discussed under "Risk Factors".

MAJESCO HOLDINGS INC.

Our Business

We are an innovative provider of diversified offerings for digital entertainment platforms. Our offerings include video game titles, video content titles and digital media peripherals and applications. Our diverse products provide us with multiple opportunities to capitalize on the large and growing installed base of digital entertainment platforms and an increasing number of digital entertainment enthusiasts. We sell our products directly and through resellers primarily to U.S. retail chains, including Best Buy, Electronics Boutique, GameStop, Kmart, Target, Toys "R" Us and Wal-Mart. We have developed our retail and distribution network relationships over our 18-year history.

Our Market and Offerings

The digital entertainment product industry is comprised of video game hardware platforms, video game software, video content and digital media peripherals and applications. Within this industry, worldwide sales of video game hardware and video game software were approximately \$23 billion in 2003 and are expected to grow to over \$31 billion in 2009, according to DFC Intelligence.

We provide offerings for all major current-generation interactive digital entertainment hardware platforms, including Nintendo's Game Boy Advance, or GBA, and GameCube, Sony's PlayStation 2, or PS2, Microsoft's Xbox and the personal computer, or PC. We are also developing offerings for next-generation home game consoles, including Sony's PlayStation 3, Microsoft's Xbox 2 and next-generation portable handheld game devices, including Nintendo's DS and Sony's PSP.

Our video game titles are targeted at various demographics at a range of price points, from lower-priced "value" titles to premium-priced "frontline" titles. Our value titles include proprietary properties, such as Quad: Desert Fury and Texas Hold 'Em, and well-known licensed properties, such as Frogger's Adventure and Pac-Man Collection. We expect to continue to release new value titles on a regular basis. Our frontline titles include BloodRayne, which has sold more than 600,000 units worldwide, and its sequel, BloodRayne 2, which was released in October 2004. We collaborate and enter into agreements with leading content providers and video game development studios for the development of our frontline titles. We expect to expand our frontline titles by releasing several new titles in 2005, including, Advent Rising, which is anticipated to be the first in a trilogy of epic science fiction games developed in collaboration with award-winning science fiction author Orson Scott Card, Jaws, which is based on the well-known classic film and Psychonauts, which is being developed by Double Fine Productions, a studio founded and managed by award-winning game designer Tim Schafer.

Our GBA Video content titles, which utilize our proprietary video compression technology, allow GBA users to view up to 45 minutes of video content on each of our GBA Video cartridges. Nintendo's GBA North American installed base was approximately 29 million units as of September 2004, according to Nintendo. Since the retail launch of our GBA Video titles in May 2004, we have released more than 20 of these titles and sold more than three million units. Our GBA Video cartridges were the first such products sold, and we are currently the only third party to have obtained approval from Nintendo to sell GBA Video products. We offer a variety of GBA Video titles today that are primarily targeted at the youth market and are based on popular Cartoon Network, Disney, FUNimation and Nickelodeon characters, such as Code Name: Kids Next Door, Dragon Ball GT, Fairly OddParents, Kim Possible, Lilo & Stitch and SpongeBob SquarePants. We intend to actively pursue licenses for new, top-quality video content, introduce new GBA video cartridges that contain up to 90 minutes of video and expand our product line to include titles appealing to a broader demographic market.

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We design, manufacture and market a line of innovative digital media peripherals and applications, which we also refer to as "gadgets," including GBA wrap-around style headphones, GBA "wireless link" and "wireless messenger" applications and stand-alone TV Arcade "plug-and-play" video game systems. We are the only third party that Nintendo has approved to sell GBA headphones and we believe we are currently the only seller of wireless applications for the Nintendo GBA. Our GBA headphones were launched in May 2004 and our GBA wireless applications and stand-alone TV Arcade "plug-and-play" video game systems were launched during the 2004 holiday season. Since their launch, we have sold more than 800,000 TV Arcade "plug-and-play" products.

Our Strengths

Our key strengths include:

- Diversified range of offerings across platforms, target markets and price points;
- Established relationships with platform manufacturers, content providers and third-party developers;
- Access to shelf space and broad exposure for our products through well-developed retailer network;
- Ability to innovate and rapidly commercialize products; and
- Seasoned management team and strong Board of Directors.

Our Strategy

Our objective is to be an innovative and leading provider of diversified offerings for digital entertainment platforms. Our strategy to achieve this objective is to:

- Leverage our industry relationships and entrepreneurial environment to continue to bring innovative products to market;
- Capitalize on our first-to-market position in GBA Video;
- Introduce frontline titles with high-margin, franchise potential;
- Maintain focus on diversification and managing risk; and
- Grow through international expansion, new strategic partnerships and acquisitions.

Corporate Information

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 ConnectivCorp, then a publicly traded company with no active operations. ConnectivCorp 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 13, 2004, the public company changed its name from "ConnectivCorp" to "Majesco Holdings Inc." to better reflect its current operating business. 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.majescogames.com. The information contained on our web site is not incorporated by reference in this prospectus.

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The Offering

Selling stockholders identified in this prospectus may sell up to 5,764,253 shares of our common stock, par value \$0.001 per share. The selling stockholders may sell their shares according to the plan of distribution described on page 18 below. We will not receive any proceeds from the sale of these shares. We will bear the expenses related to the registration of the common stock.

The 5,764,253 shares of common stock being sold by the selling stockholders include:

- 285,714 shares of common stock issued upon conversion of an outstanding convertible note dated as of November 25, 2003;
- 3,596,847 shares of common stock issued upon the conversion of 7% convertible preferred stock that was issued in our private placement completed on February 26, 2004, which shares are subject to restrictions on transfer pursuant to a lock-up agreement;
- 892,840 shares of common stock issuable upon the exercise of warrants having an exercise price of \$7.00 per share that were issued in our private placement completed on February 26, 2004, which shares are subject to restrictions on transfer pursuant to a lock-up agreement;
- 142,856 shares of common stock issued upon (i) the conversion of 7% convertible preferred stock (71,428 shares) and (ii) warrants having an exercise price of \$7.00 per share (71,428 shares), that were issued to Jesse Sutton in exchange for previously outstanding indebtedness;
- 142,856 shares of common stock issued upon (i) the conversion of 7% convertible preferred stock (71,428 shares) and (ii) warrants having an exercise price of \$7.00 per share (71,428 shares), that were issued to Joseph Sutton in exchange for previously outstanding indebtedness;

- 360,000 shares of common stock issuable upon (i) the conversion of 7% convertible preferred stock (180,000 shares) and (ii) warrants having an exercise price of \$7.00 per share (180,000 shares), as the securities underlying the placement agent warrant to purchase units that was issued to JMP Securities;
- 262,856 shares of common stock issuable upon (i) the conversion of 7% convertible preferred stock (131,428 shares) and (ii) warrants having an exercise price of \$7.00 per share (131,428 shares), as the securities underlying the placement agent warrant to purchase units that was issued to Atlantis Equities, Inc. as a portion of the placement agent fee issued in connection with a private placement completed on February 26, 2004, which shares are subject to restrictions on transfer pursuant to a lock-up agreement;
- 43,142 shares of common stock issued to CEOcast, Inc. pursuant to a consulting agreement, dated as of November 8, 2003;
- 22,857 shares of common stock issued to Hayden Communications, Inc. pursuant to a consulting agreement, dated as of November 26, 2003; and
- 14,285 shares of common stock issued to Mintz, Levin, Cohn, Ferris, Glovsky and Popeo, P.C. pursuant to a settlement agreement, dated as of December 5, 2003.

Our symbol on the Nasdaq National Market System is "MJES." As of February 1, 2005, there were 22,104,141 shares of our common stock issued and outstanding.

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RISK FACTORS

An investment in our common stock involves a high degree of risk. You should carefully consider the risks described below together with all of the other information included in this prospectus before making an investment decision. 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 occurs, our business, financial condition or results of operations could suffer. In that case, the trading price of our common stock could decline, and you may lose all or part of your investment.

We expect our operating results to fluctuate on a quarterly and annual basis, which may result in volatility in our stock price.

Our quarterly net revenues and results of operations have significantly varied in the past and can be expected to significantly vary in the future. Our business experiences substantial seasonality, and typically, our net revenues are significantly higher during our fourth fiscal quarter ending October 31 than during our other quarters because of increased consumer demand during the year-end holiday season. As a result, our fourth fiscal quarter accounts for a significant portion of our revenues and profitability for the entire fiscal year, and if we are not successful in the fourth fiscal quarter, this may have a significant adverse impact on our entire fiscal year. Other factors that cause fluctuations include:

- the timing of the release of our new offerings;
- the popularity of our new offerings and offerings released in prior periods;
- changes in the mix of offerings with varying profit margins;
-

competitive factors, including the introduction of new products, product enhancements and technologies;

- the timing of new platform releases;
- product approval delays;
- shipping or manufacturing difficulties or delays; and
- fluctuations in the size and rate of growth of consumer demand for titles for different platforms.

As a result of these and other factors, we cannot assure you that our results of operations will be consistent on a quarterly or annual basis. Accordingly, you should not rely on our results of operations for a particular quarter or year as an indication of our future performance. If our results of operations in a quarter fall below our expectations and the expectations of market analysts or investors, the price of our common stock may likely decrease.

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

In fiscal years 2002, 2003 and 2004, we incurred net losses of \$751,000, \$10.8 million and \$11.2 million, respectively. In fiscal years 2002 and 2003, these net losses were principally related to our operations, and included financing costs, litigation expense and impairment reserves. For the fiscal year 2004, our net loss related principally to a non-cash charge to reflect the change in the fair value of our outstanding warrants issued in our February 2004 private placement. We expect to continue to incur increased operating expenses over the next several years in connection with the continued growth of our business, such as increased sales and marketing expenditures, development costs and costs associated with expanding our general and administrative functions. We may not generate revenues sufficient to offset these increased costs, and may sustain losses in future periods. If we do become profitable, we may not sustain or increase our profitability. Continued losses, or an inability to sustain profitability, may have an adverse effect on our stock price.

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

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. 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, or the amount or nature of accommodations that we will provide in the future. If actual accommodations exceed our reserves, our earnings would be reduced, perhaps materially. Any such reduction may have an adverse effect on our business, financial condition or results of operations.

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 and liquidity.

As our business expands, we expect to increase our expenditures in a number of efforts, including sales, marketing, licensing and product development. Although there can be no assurance, our management believes that there are

sufficient capital resources from the proceeds of our recently completed secondary offering and from operations, including our factoring and purchase order financing arrangements, to finance our operational requirements through at least the next twelve months. If we 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 in this offering. Failure to obtain financing or obtaining financing on unfavorable terms could have a material adverse effect on future operating prospects and continued growth and could result in a decrease in our stock price.

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

We utilize the services of independent software developers to develop our video games. Consequently, our success in the video game market depends on our continued ability to obtain or renew product development agreements with leading 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 leading 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 leading independent video game software developers to enter into publishing agreements with us. We may be unable to secure or maintain relationships with leading 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, sometimes without notice, if either party declares bankruptcy, becomes insolvent, ceases operations or materially breaches its agreement and fails to cure that breach within a designated time frame. In addition, many leading 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, and all of our GBA Video titles and plug-and-play video game offerings, 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, or maintain our licenses 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. For example, the development of frontline video games requires significant development and marketing expenditures. In the event we are not successful in developing new titles, peripherals 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 could be materially negatively affected.

Furthermore, digital entertainment platforms are characterized by rapidly changing technology. We must continually anticipate the emergence of, and adapt our products to, new digital 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.

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

Our sales to Wal-Mart, Toys "R" Us and Jack of All Games accounted for approximately 27%, 25% and 16% of our net revenue for the fiscal year 2004, 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.

We have grown rapidly and if we fail to manage our growth, our business may suffer.

Although we commenced operations 18 years ago, recently we have experienced, and continue to experience, significant growth in our operations. This growth has entailed hiring key personnel,

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including our Chief Executive Officer, developing and introducing to market several new product lines and forging new customer and licensing relationships. We anticipate that further expansion of our operations will be required to address our potential growth as we continue to address market opportunities. This expansion has placed, and is expected to continue to place, a substantial strain on our management, operational and financial resources. In order to manage future growth, we will be required to improve existing and implement new operating and management

systems, procedures and controls. We also need to hire, train and manage additional qualified personnel. A significant factor in our growth has been a substantial increase in consumer demand for our products. If we do not effectively manage our growth, we may not adequately satisfy this demand. In addition, the quality of our offerings or our ability to develop and bring our offerings to market on a timely or cost effective basis could suffer. This could negatively impact our reputation, revenue and results of operations.

We must continue to strengthen our financial systems and controls, and failure to do so could adversely affect our ability to provide timely and accurate financial statements.

As a closely-held company with no prior public reporting obligations prior to our merger with ConnectivCorp in December 2003, we had committed limited personnel and resources to the development of our internal financial controls and systems. In connection with our fiscal year 2003 financial statement audit and in connection with their continuing engagement, our independent auditors have and continue to provide us with comments and recommendations regarding a number of areas in our internal accounting and disclosure controls needing improvement. These areas include: segregating duties in key functions; the creation of formal accounting controls, policies and procedures; a need to hire additional management and staff experienced in financial reporting; and finalizing documentation of our accounting and disclosure internal controls and procedures. We have begun to address these issues by hiring a Chief Financial Officer who was formerly a partner in a Big Four accounting firm. We believe that as a result of our fiscal year 2004 audit, our auditors will likely issue to us a management letter setting forth their recommendations related to the above issues. There can be no assurance as to the nature of the recommendations, observations and suggestions regarding our operations, activities and efficiencies that may be contained in the management letter.

Continued improvement in our internal controls and procedures and the continued hiring and training of key accounting personnel will be required in order for us to manage future growth successfully and effectively assess our results of operations and liquidity needs. Continued improvement of our internal controls as well as compliance with the Sarbanes-Oxley Act of 2002 and related requirements will be costly and will place a significant burden on management. In addition, as of October 31, 2005, we will become subject to the heightened internal control and procedure requirements of Section 404 of the Sarbanes-Oxley Act. To date, we have taken limited actions with respect to our requirements under Section 404, and we expect to hire additional personnel and/or engage outside consultants, among other preparations, over the next twelve months to assist in our Section 404 related activities. While we have made improvements, we cannot assure you that the measures we have taken or any future measures will enable us to provide accurate and timely financial reports, particularly if we are unable to hire additional personnel in our accounting and financial department, or if we lose personnel in this area. Any failure to improve our internal controls or other problems with our financial systems or internal controls could result in delays or inaccuracies in reporting financial information, or non-compliance with SEC reporting and other regulatory requirements, any of which could adversely affect our business and stock price.

Significant competition in our industry could adversely affect our business.

We cannot assure you 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 digital entertainment products, including video game titles, video content titles and digital media peripherals and applications, 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 value and frontline market segments. In addition, console and handheld manufacturers, such as Microsoft, Nintendo and Sony, publish software for their respective platforms, and 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 in both the value and frontline areas as more competitors enter the video game market.

While our GBA Video titles were the first video content titles to market, and to date the only third party titles that Nintendo has approved for the GBA, our competitors are developing competing titles and compression technology. Nintendo may approve these competing titles, which may utilize superior technology and prove to be more successful than our products. Nintendo itself is already using an alternative form of compression technology and producing GBA Video titles that compete with our products. We cannot assure you that competitors will not be able to also secure strong relationships with content providers on terms equal to or more favorable than we have. In addition, sales of our GBA Video products will be affected by the success of other portable video player platforms, including portable DVD players and other handheld video devices.

Our digital media peripherals and applications also face significant competition. For example, there have been a number of other recent "plug-and-play" video game systems containing different software, and offering different games, than ours. In addition, platform manufacturers may expand their product lines to include digital media peripherals and applications that may compete with our product offerings. Next-generation consoles may also render our digital media peripherals and applications obsolete. For example, Nintendo may incorporate an email or "chat" concept in future generations of its GBA, which could render our "wireless messenger" application obsolete.

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. 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.

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 and GameCube, and from Microsoft to develop products for the

Xbox. These licenses are non-exclusive, and as a

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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 face limitations on our ability to find suitable acquisition opportunities and difficulties in integrating acquired businesses.

A component of our strategy is to grow through strategic relationships and acquisitions. If we make acquisitions, they could be material in size and scope. While we will continually be searching for appropriate strategic partnerships or acquisition opportunities, there can be no assurance that we will be successful in identifying suitable candidates. As the video game and digital entertainment industry continues to consolidate, we face significant competition for strategic partnership or acquisition opportunities, which may inhibit our ability to complete suitable transactions. Additionally, our management has generally had limited experience completing acquisitions or managing the integration of acquisitions. Accordingly, in the event we are able to identify suitable acquisition candidates, we cannot guarantee that we will be able to successfully complete or integrate any business, products, technologies or personnel that we might acquire or seek to acquire in the future, and our failure to do so could harm our business. Furthermore, any future acquisitions, if completed, would subject us to many risks, including:

- difficulties in integrating the products, operations or personnel of acquired companies into our business;
- diversion of our management's attention from our ongoing operations;
- additional expenses associated with amortization of acquired assets or impairment of acquired goodwill;
- difficulties in maintaining uniform standards, controls, procedures and policies;
- potential impairment of existing relationships with employees and customers as a result of the difficulties in integration of new management personnel; and
- dilution to our stockholders in the event we issue stock to finance an acquisition or increased leverage if we incur debt to finance an acquisition.

The loss of our senior management and skilled personnel could negatively affect our business.

Our business greatly relies on the services of Morris Sutton, our Chairman Emeritus, and his relationships with hardware manufacturers, licensors of our content and several of our customers. We also greatly rely on the services of Carl Yankowski, our Chief Executive Officer, and Kevin Ray, our Chief Technology Officer. Our future success will depend to a significant degree upon the performance and contribution of these and other members of our senior management team, and upon our ability to attract, motivate and retain other highly qualified employees with technical, management, marketing, sales, product development, creative and other skills. In our industry, competition for highly skilled and creative employees is intense and costly. Our business, financial condition and results of operations could be materially and adversely affected if we lost the services of any members of our senior management team or key technical or creative employees or if we failed to attract additional highly qualified employees.

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We intend to increase our revenues from our international operations, which may subject us to economic, political, regulatory and other risks.

Historically, we have not devoted significant resources to our international operations. However, a component of our strategy is to expand our international operations in order to increase our revenues. Expanding our international operations, however, may subject us to many risks, including:

- economic and political instability;
- compliance with foreign and domestic laws and regulations;
- changes in foreign and domestic legal and regulatory requirements or policies resulting in burdensome government controls, tariffs, restrictions, embargoes or export license requirements;
- currency fluctuations;
- difficulties in staffing and managing our international operations;
- less favorable foreign intellectual property laws making it more difficult to protect our properties from appropriation by competitors;
- potentially adverse tax treatment;
- difficulties with distributors; and
- difficulties collecting our accounts receivable.

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 noncompl