MAJESCO ENTERTAINMENT CO
Form 10-Q
September 13, 2007

UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
WASHINGTON, D.C. 20549

FORM 10-Q

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

For the quarterly period ended July 31, 2007

Commission File No. 000-51128

Majesco Entertainment Company

(Exact name of registrant as specified in its charter)

| | |
|---|---|
| DELAWARE | 606-1529524 |
| (State or Other Jurisdiction of Incorporation or Organization) | (I.R.S. Employer Identification No.) |

160 Raritan Center Parkway, Edison, NJ 08837

(Address of principal executive offices)

REGISTRANT'S TELEPHONE NUMBER, INCLUDING AREA CODE: (732) 225-8910

(Former Name, Former Address and Former Fiscal Year, if Changed Since Last Report)

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

Indicate by check mark whether the registrant 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):

Large accelerated filer Accelerated filer Non-accelerated filer

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

As of September 13, 2007, there were 28,675,962 shares of the Registrant's common stock outstanding.

MAJESCO ENTERTAINMENT COMPANY AND SUBSIDIARY
QUARTERLY REPORT ON FORM 10-Q

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MAJESCO ENTERTAINMENT COMPANY AND SUBSIDIARY
CONDENSED CONSOLIDATED BALANCE SHEET
(in thousands, except share amounts)

| | July 31, 2007 | October 31, 2006 |
|---|---|---|

| | (unaudited) | |
|---|---|---|
| ASSETS | | |
| Current assets | | |
| Cash | $ 3,834 | $ 3,794 |
| Due from factor | — | 1,189 |
| Accounts and other receivables | 515 | 3,103 |
| Inventory – principally finished goods | 1,467 | 2,438 |
| Capitalized software development costs and prepaid license fees | 1,661 | 1,489 |
| Prepaid expenses | 1,131 | 2,226 |
| Total current assets | 8,608 | 14,239 |
| Property and equipment – net | 603 | 701 |
| Other assets | 69 | 71 |
| Total assets | $ 9,280 | $ 15,011 |
| LIABILITIES AND STOCKHOLDERS' EQUITY (DEFICIENCY) | | |
| Current liabilities | | |
| Accounts payable and accrued expenses | $ 6,338 | $ 10,911 |
| Due to factor | 282 | — |
| Inventory financing payable | 9 | 1,390 |
| Accrued litigation settlement | 2,500 | — |
| Advances from customers | 829 | 961 |
| Total current liabilities | 9,958 | 13,262 |
| Stockholders' equity: | | |
| Common stock – $.001 par value; 250,000,000 shares authorized; 23,863,196 and 23,427,462 issued and outstanding at July 31, 2007 and October 31, 2006, respectively | 24 | 23 |
| Additional paid in capital | 95,955 | 94,529 |
| Accumulated deficit | (96,564) | (92,754) |
| Accumulated other comprehensive loss | (93) | (49) |
| Total stockholders' equity (deficiency) | (678) | 1,749 |
| Total liabilities and stockholders' equity (deficiency) | $ 9,280 | $ 15,011 |

See accompanying notes

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MAJESCO ENTERTAINMENT COMPANY AND SUBSIDIARY
CONDENSED CONSOLIDATED STATEMENT OF OPERATIONS
(in thousands, except share amounts)

| | Three Months Ended July 31, | | Nine Months Ended July 31, | |
|---|---|---|---|---|
| | 2007 | 2006 | 2007 | 2006 |
| | (Unaudited) | | (Unaudited) | |
| Net revenues | $ 10,010 | $ 12,363 | $ 39,121 | $ 45,186 |
| Cost of sales | | | | |

| | | | | |
|---|---|---|---|---|
| Product costs | 5,421 | 5,461 | 19,813 | 20,550 |
| Software development costs and license fees | 1,632 | 2,784 | 5,685 | 9,056 |
| | 7,053 | 8,245 | 25,498 | 29,606 |
| Gross profit | 2,957 | 4,118 | 13,623 | 15,580 |
| Operating expenses | | | | |
| Research and development | 536 | 556 | 1,687 | 1,953 |
| Selling and marketing | 2,039 | 2,159 | 5,725 | 8,484 |
| General and administrative | 1,664 | 3,061 | 6,103 | 8,021 |
| Gain on settlement of liabilities and other gains | (75) | (1,410) | (314) | (4,507) |
| Settlement of litigation and related charges, net | — | — | 2,500 | — |
| Loss on impairment of software development costs | — | — | 35 | 2,375 |
| Depreciation and amortization | 75 | 84 | 220 | 347 |
| | 4,239 | 4,450 | 15,956 | 16,673 |
| Operating loss | (1,282) | (332) | (2,333) | (1,093) |
| Other costs and expenses | | | | |
| Interest expense and financing costs, net | 266 | 392 | 1,477 | 1,378 |
| Loss before income taxes | (1,548) | (724) | (3,810) | (2,471) |
| Provision for income taxes | — | — | — | — |
| Net loss | $ (1,548) | $ (724) | $ (3,810) | $ (2,471) |
| Net loss per share: | | | | |
| Basic and diluted | $ (0.06) | $ (0.03) | $ (0.16) | $ (0.11) |
| Weighted average shares outstanding | | | | |
| Basic and diluted | 23,862,617 | 22,408,410 | 23,716,363 | 22,345,021 |

See accompanying notes

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MAJESCO ENTERTAINMENT COMPANY AND SUBSIDIARY
CONDENSED CONSOLIDATED STATEMENT OF CASH FLOWS
(dollars in thousands)

| | Nine Months Ended July 31, | |
|---|---|---|
| | 2007 | 2006 |
| | (unaudited) | |
| CASH FLOWS FROM OPERATING ACTIVITIES | | |
| Net loss | $ (3,810) | $ (2,471) |
| Adjustments to reconcile net loss to net cash provided by operating activities | | |
| Depreciation and amortization | 220 | 347 |
| Impairment of software development costs | 35 | 2,375 |
| Non-cash compensation expense | 1,013 | 1,020 |

| | | |
|---|---|---|
| Gain on settlement of liabilities and other gains | (314) | (4,507) |
| Amortization of software development costs and prepaid license fees | 2,464 | 9,056 |
| Changes in operating assets and liabilities | | |
| Decrease (increase) in due from factor – net | 1,471 | (6,961) |
| Decrease (increase) in other receivables | 2,588 | (642) |
| Decrease in inventory | 971 | 4,369 |
| (Increase) decrease in capitalized software development costs and prepaid license fees | (2,671) | 1,791 |
| Decrease in income tax receivable | — | 275 |
| Decrease (increase) in prepaid expenses and other | 1,097 | (41) |
| Decrease in accounts payable and accrued expenses | (1,394) | (3,321) |
| Decrease in advances from customers | (132) | (177) |
| Net cash provided by operating activities | 1,538 | 1,113 |
| CASH FLOWS FROM INVESTING ACTIVITIES | | |
| Purchases of property and equipment | (122) | (182) |
| Net cash used in investing activities | (122) | (182) |
| CASH FLOWS FROM FINANCING ACTIVITIES | | |
| Proceeds from exercise of stock options | 49 | — |
| Inventory financing | (1,381) | 208 |
| Net cash (used in) provided by financing activities | (1,332) | 208 |
| Effect of exchange rates on cash and cash equivalents | (44) | 66 |
| Net increase in cash | 40 | 1,205 |
| Cash – beginning of period | 3,794 | 2,407 |
| Cash – end of period | $ 3,834 | $ 3,612 |
| SUPPLEMENTAL SCHEDULE OF NON CASH INVESTING AND FINANCING ACTIVITIES | | |
| Accounts payable settled through the issuance of common stock, classified as a liability | $ 365 | $ 125 |
| Cash paid for interest | $ 1,477 | $ 1,378 |

See accompanying notes



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## 1. PRINCIPAL BUSINESS ACTIVITY AND BASIS OF PRESENTATION

Majesco Entertainment Company, together with its wholly owned UK subsidiary (‘‘Majesco’’ or ‘‘Company’’), is a provider of interactive entertainment products. The Company’s offerings include video game software and other digital entertainment products.

Majesco’s products provide it with opportunities to capitalize on the large and growing installed base of interactive entertainment platforms and an increasing number of interactive entertainment enthusiasts. The Company sells its products directly and through resellers primarily to U.S. retail chains, including Best Buy, GameStop/Electronics Boutique, Circuit City, Target, Toys ‘‘R’’ Us and Wal-Mart. Majesco also sells products internationally through partnerships with international publishers. The Company has developed retail and distribution network relationships over its more than 20-year history.

Majesco provides offerings 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.

The Company's offerings include video game software and other digital entertainment products. The Company's operations involve similar products and customers worldwide. The products are developed and sold domestically and internationally. The Company is centrally managed and the chief operating decision makers, the chief executive and other officers, use consolidated financial information supplemented by sales information by product category, major product title and platform to make operational decisions and assess financial performance. Accordingly, the Company operates in a single segment. Sales for the Company in the United States were $7.1 million or 71% and $33.9 million or 87% for the three and nine month periods ended July 31, 2007, respectively. Sales in Europe were $2.9 million or 29% and $5.2 million or 13% for the three and nine month periods ended July 31, 2007, respectively. Sales for the Company in the United States were $11.1 million or 90% and $38.6 million or 85% for the three and nine month periods ended July 31, 2006, respectively. Sales in Europe were $1.2 million or 10% and $6.6 million or 15% for the three and nine month periods ended July 31, 2006, respectively.

The accompanying financial statements have been prepared assuming that the Company will continue as a going concern. The Company has suffered recurring operating losses and has a shareholders' deficiency and a working capital deficiency that raise substantial doubt about its ability to continue as a going concern. The financial statements do not include any adjustments that might result from the outcome of this uncertainty.

During September 2007 the Company raised approximately $5.9 million in net proceeds from the sale of equity securities (see note 10). As of July 31, 2007, management believes that there will be sufficient capital resources from operations and existing financing arrangements to meet the Company's requirements for the development, production, marketing, purchases of equipment, and the acquisition of intellectual property rights for future products for the next twelve months. However, in the event that the Company is unable to generate the level of operating revenues in its business plan, the Company will be required to reduce operating expenditures or obtain additional sources of financing to continue operations. However, there can be no assurance that additional sources of financing will be available on acceptable terms, if at all. If no additional sources of financing are available, it could create a material adverse effect on future operating prospects of the Company.

The accompanying interim consolidated financial statements of the Company are unaudited, but in the opinion of management, reflect all adjustments, consisting of normal recurring accruals, necessary for a fair presentation of the results for the interim period. Accordingly, they do not include all information and notes required by generally accepted accounting principles for complete financial statements. The results of operations for interim periods are not necessarily indicative of results to be expected for the entire fiscal year or any other period. The balance sheet at October 31, 2006 has been derived from the audited financial statements at that date but does not include all of the information and footnotes required by accounting principles generally accepted in the United States of



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America for complete financial statements. These interim consolidated financial statements should be read in conjunction with the Company's consolidated financial statements and notes for the year ended October 31, 2006 filed on Form 10-K on January 29, 2007.

The statements contained in this Report on Form 10-Q, that are not purely historical, are forward-looking information and statements within the meaning of Section 27A of the Securities Act of 1933 and Section 21E of the Securities Exchange Act of 1934. These include statements regarding our expectations, intentions, or strategies regarding future matters. All forward-looking statements included in this document are based on information available to us on the date hereof. It is important to note that our actual results could differ materially from those projected in such forward-looking statements contained in this Form 10-Q. The forward-looking statements contained herein are based on current expectations that involve numerous risks and uncertainties. Assumptions relating to the foregoing involve judgments regarding among other things, our ability to secure financing or investment for capital expenditures, future economic and competitive market conditions, and future business decisions. All these matters are difficult or impossible to predict accurately, many of which may be beyond our control. Although we believe that the assumptions underlying our forward-looking statements are reasonable, any of the assumptions could be inaccurate and, therefore, there can be no assurance that the forward-looking statements included in this Form 10-Q will prove to be accurate.

## 2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Stock Based Compensation. In December 2004, the Financial Accounting Standards Board (''FASB'') issued Statement of Financial Accounting Standards No. 123 (R) (revised 2004), ''Share-Based Payment'' which revised Statement of Financial Accounting Standards No. 123, ''Accounting for Stock-Based Compensation''. This statement supersedes Opinion No. 25, ''Accounting for Stock Issued to Employees.'' The revised statement addresses the accounting for share-based payment transactions with employees and other third parties, eliminates the ability to account for share-based compensation transactions using APB 25 and requires that the compensation costs relating to such transactions be recognized in the statement of operations. The revised statement has been implemented by the Company effective November 1, 2005.

Operating expenses include stock based compensation charges of $238,000 and $1,013,000 for the three and nine month periods ended July 31, 2007, and $520,000 and $1,020,000 for the three and nine month periods ended July 31, 2006, respectively.

Estimates. The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities or the disclosure of gain or loss contingencies at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Among the more significant estimates included in these financial statements are the estimated customer allowances, the valuation of inventory and the recoverability of advance payments for software development costs and intellectual property licenses. Actual results could differ from those estimates.

Loss per share. Basic loss per common share is computed by dividing the net loss by the weighted-average number of shares of common stock outstanding for the period. Diluted and basic loss per common share for the three and nine month periods ended July 31, 2007 and 2006, are the same because the impact of the conversion or exercise, as applicable, of the warrants (676,377 and 2,070,687 at July 31, 2007 and 2006) and stock options (1,123,347 and 1,450,294 at July 31, 2007 and 2006, respectively) would be antidilutive.



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## 3. DUE (TO) FROM FACTOR

Due (to) from factor consists of the following:

| | July 31, 2007 (in thousands) | October 31, 2006 (in thousands) |
|---|---|---|
| Outstanding accounts receivable sold to factor | $ 5,395 | $ 14,384 |
| Less: Allowance | (3,169) | (4,047) |
| Advances from factor | (2,508) | (9,148) |
| | $ (282) | $ 1,189 |

The following table sets forth the adjustments to the price protection and other customer sales incentive allowances included as a reduction of the amounts due from factor:

| | Nine Months Ended July 31, | |
|---|---|---|
| | 2007 (in thousands) | 2006 (in thousands) |
| Balance – beginning of period | $ (4,047) | $ (9,551) |
| Add: provision | (1,930) | (2,231) |
| Less: amounts charged against allowance | 2,808 | 9,066 |
| Balance – end of period | $ (3,169) | $ (2,716) |

4. PREPAID EXPENSES

The following table presents the major components of prepaid expenses:

| | July 31, 2007 (in thousands) | October 31, 2006 (in thousands) |
|---|---|---|
| Advance payments for inventory | $ 1,002 | $ 1,934 |
| Other (less than 5% of total assets) | 129 | 292 |
| | $ 1,131 | $ 2,226 |

5. ACCOUNTS AND OTHER RECEIVABLES

The following table presents the major components of accounts and other receivables:

| | July 31, 2007 (in thousands) | October 31, 2006 (in thousands) |
|---|---|---|
| Accounts receivable | $ 173 | $ 2,370 |

| | | |
|---|---|---|
| Legal fee reimbursements due from insurance carriers | 342 | 733 |
| | $ 515 | $ 3,103 |



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6. ACCOUNTS PAYABLE AND ACCRUED EXPENSES

Accounts payable and accrued expenses consist of the following:

| | July 31, 2007 (in thousands) | October 31, 2006 (in thousands) |
|---|---|---|
| Accounts payable – trade | $ 1,887 | $ 3,809 |
| Accrued expenses: | | |
| Royalties – including accrued minimum guarantees | 2,312 | 3,233 |
| Salaries and other compensation | 618 | 499 |
| Sales commissions | 93 | 406 |
| Legal fees, shareholder litigations | 897 | 1,183 |
| Other accruals | 531 | 1,781 |
| | $ 6,338 | $ 10,911 |

Legal fees, shareholder litigations represents unpaid legal fees that have been invoiced directly to the Company regarding the lawsuits or under indemnification agreements with parties named in the lawsuits. The Company included $342 and $733 in other receivables (see note 5) at July 31, 2007 and October 31, 2006, respectively, representing the portion of the unpaid fees that are covered under the Company's insurance policies.

7. ACCRUED LITIGATION SETTLEMENT

As discussed in note 8, accrued litigation settlement consists of a $2.5 million liability representing the fair value of common stock which is expected to be issued to settle a shareholder class action lawsuit.

8. CONTINGENCIES AND COMMITMENTS

Commitments

At July 31, 2007, the Company had open letters of credit aggregating $0.5 million under the Company's purchase order assignment arrangements for inventory to be delivered during the subsequent quarter.

At July 31, 2007, the Company was committed under agreements with certain developers for future milestone and license fee payments aggregating $3.1 million, $1.7 million of which are payable through October 31, 2007. Milestone payments represent scheduled installments due to the Company's developers based upon the developers providing the Company certain deliverables, as predetermined in the Company's contracts. The milestone payments generally represent advances against royalties to the developers. These payments will be used to reduce future royalties due to the developers from sales of the Company's video games.

Effective January 1, 2007, upon his resignation, the Company entered into a transition agreement with Morris Sutton, its former Chairman Emeritus, under which he will provide services as a consultant for a two year period. The agreement provides for a monthly retainer of $29,175 and a commission equal to 2% of sales to certain specified accounts.

The Company has entered into ‘‘at will’’ employment agreements with certain key executives. These employment agreements include provisions for, among other things, annual compensation, bonus arrangements and equity incentives. These agreements also contain provisions related to severance terms and change of control provisions.

Contingencies

In July 2005, four purported class action complaints were filed against the Company and several current and former directors and officers of the Company in the United States District Court for the



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District of New Jersey. On September 12, 2005, a fifth purported class action complaint was filed in the same court on behalf of a class of individuals who purchased shares of the Company common stock in the Company’s January 26, 2005 offering of six million shares of common stock (the ‘‘Offering’’). The complaint named as defendants the Company, current and former officers of the Company, and certain financial institutions who served as underwriters with respect to the Offering.

On October 11, 2005, the Court consolidated the five cases and appointed a Lead Plaintiff. On December 14, 2005, the Lead Plaintiff filed an Amended Consolidated Complaint, which is now the operative Complaint. The Complaint names the following as defendants: the Company, Carl Yankowski, Jan E. Chason, Jesse Sutton, Joseph Sutton, Morris Sutton, Laurence Aronson, F. Peter Cuneo, James Halpin, Louis Lipschitz, Marc Weisman, RBC Capital Markets Corporation, JMP Securities LLC, Harris Nesbitt & Corp., Wedbush Morgan Securities Inc., and Goldstein Golub Kessler LLP.

The Complaint alleges that the Registration Statement and Prospectus filed with the SEC in connection with the Company’s Offering and certain of the Company’s press releases and other public filings contained material misstatements and omissions about the Company’s financial condition and prospects as well as its products. The lead Plaintiff asserts a claim under Section 11 of the Securities Act against all the defendants on behalf of investors who purchased in the Offering. It asserts a Section 12(a)(2) claim against the Company and the financial institutions who served as underwriters in connection with the Offering, and a Section 15 control person claim against defendants Carl Yankowski, Jan Chason, Jesse Sutton, Joseph Sutton, and Morris Sutton (the ‘‘Defendants’’). Lead Plaintiff also asserts a claim under Section 10(b) of the Exchange Act and Rule 10b-5 promulgated there under against the Company and the Defendants and a claim under Section 20(a) of the Exchange Act against the Defendants. The Complaint seeks damages in an unspecified amount. The proposed class period for the Exchange Act claims is December 8, 2004 through September 12, 2005.

On October 10, 2006, Trinad Capital Master Fund, Ltd., a shareholder of our common stock, filed a complaint against the Company and several current and former directors and officers of the Company in the United States District Court for the District of New Jersey. The current or former officers and directors named as defendants in the complaint are Morris Sutton, Jesse Sutton, Joseph Sutton and Carl Yankowski. The Complaint also named the Company’s outside auditors, Goldstein Golub Kessler LLP, as a defendant. Goldstein Golub Kessler LLP has since been voluntarily dismissed without prejudice. The allegations in the Complaint are similar to those in the Amended Consolidated Complaint filed in the in the Majesco Securities Litigation putative class action discussed above. The Complaint alleges three causes of action: (1) a claim under Section 10(b) of the Exchange Act (and Rule 10b-5 promulgated thereunder) against all the named defendants; (2) a claim under Section 20(a) of the Exchange Act against Morris Sutton, Jesse Sutton and Joseph Sutton; and (3) a common law fraud claim against Morris Sutton, Jesse Sutton, Joseph Sutton and Carl Yankowski. Trinad seeks compensatory damages of no less than $10 million. This amount is sought with respect to each claim. In connection with the fraud claim, Trinad also seeks $10 million in punitive damages.

On November 2, 2006, Trinad Capital Master Fund, Ltd., filed a complaint, purportedly on behalf of the Company, against certain current or former directors of the Company in the United States District Court for the District of New Jersey. The individuals named as defendants in the complaint are Morris Sutton, Jesse Sutton, Joseph Sutton, Louis Lipschitz and Laurence Aronson. The complaint also names the Company as a nominal defendant. The complaint alleges that, from late 2004 through the filing date, defendants breached their fiduciary duties which caused damage to the Company. The complaint does not specify the amount of damages sought.

The Company and the Individual Defendants have been in negotiations with Plaintiffs to resolve the Securities Class Action lawsuit, and have reached a tentative understanding on settlement terms. These terms include a payment in the form of common stock of the Company with a market value of approximately $2.5 million in addition to payments in cash from proceeds of the Company’s insurance carrier. Assuming a Class Action settlement is concluded, it will require court approval before it can become effective. The Company anticipates that its insurance will be adequate to pay the cash portion of such settlement and related legal costs and will also be adequate to address Trinad Capital’s



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litigation against the Company. There is no assurance that the settlement described above will be achieved, and if not achieved, there can be no assurance that the Company’s insurance will be adequate to cover the Company’s costs relating to the Class Action lawsuit or Trinad Capital’s litigation against the Company. Any expenses incurred in connection with such litigation not covered by available insurance or any adverse resolution of such litigation could have a material adverse effect on our financial condition.

On July 26, 2007, Charlie Bolton filed a complaint against the Company and several current and former directors and officers of the Company in the United States District Court for the District of New Jersey. The current or former officers and directors named as defendants in the complaint are Morris Sutton, Jesse Sutton, Joseph Sutton and Carl Yankowski. The allegations in the Complaint are similar to those in the Amended Consolidated Complaint filed in the In re: Majesco Securities Litigation putative class action and the Complaint filed in Trinad Capital’s complaint against the Company and several current and former directors and officers of the Company discussed above. The Complaint alleges four causes of action: (1) a claim under Section 10(b) of the Exchange Act (and Rule 10b-5 promulgated thereunder) against all the named defendants; (2) a claim under Section 20(a) of the Exchange Act against Morris Sutton, Jesse Sutton and Joseph Sutton; (3) a claim under Section 18(a) of the Exchange Act against all the named defendants; and (4) a common law fraud claim against Morris Sutton, Jesse Sutton, Joseph Sutton and Carl Yankowski. Bolton seeks compensatory damages of no less than $2 million and $2 million in punitive damages. No liability has been recorded in the financial statements as of July 31, 2007 for legal or settlement expenses related the complaint, as they can not be reasonably estimated at this time. Expenses incurred in connection with Bolton’s litigation or any adverse resolution thereof could have a material adverse effect on the Company’s financial condition.

The Company at times may be a party to other routine claims and suits brought by the Company and against the Company in the ordinary course of business, including disputes arising over contractual claims and collection matters. In the opinion of management, after consultation with legal counsel, the outcome of such routine claims will not have a material adverse effect on the Company's business, financial condition, and results of operations or liquidity. However, the costs and other effects of pending or future litigation, governmental investigations, legal and administrative cases and proceedings (whether civil or criminal), settlements, judgments and investigations, claims and changes in those matters (including the matters described above), and developments or assertions by or against the Company relating to intellectual property rights and intellectual property licenses, could have a material adverse effect on the Company's business, financial condition, and results of operations or liquidity.

9. RELATED PARTIES

The Company receives printing and packaging services from a business of which the brother of Morris Sutton, the Company's former Chairman Emeritus, and uncle of Jesse Sutton, the Company's interim Chief Executive Officer is a principal. During the three and nine month periods ended July 31, 2007 and 2006 the Company was charged $0.1 million and $1.0 million, and $0.2 million and $1.0 million respectively. These charges are included in product costs in the accompanying consolidated statement of operations. Such charges are, to the Company's knowledge, on terms no less favorable to what the Company could receive from providers of similar services.

Morris Sutton resigned from the company effective January 1, 2007, becoming a consultant. The Company paid approximately $90,000 and $270,000 to Mr. Sutton under the consulting agreement during the three and nine months ended July 31, 2007, respectively.

10. SUBSEQUENT EVENTS

On August 3, 2007, the Company granted 545,872 shares of restricted stock to officers and employees of the company under the 2004 Employee, Director and Consultant Incentive Plan. The shares had an aggregate market value of approximately $1.2 million on the date of grant and vest over a three year period.

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On September 5, 2007, the Company sold 3,966,668 shares of common stock, and warrants to purchase an additional 1,586,668 shares of common stock, to a group of accredited investors for gross proceeds of $5.9 million. The warrants have an exercise price of $2.04 per share and a term of five years, which begins six months from the issue date. The Company is obligated to file a registration statement for the securities within 45 days of the closing of the transaction, and have the registration declared effective by the Securities and Exchange Commission within 120 days of the closing of the transaction. If the registration obligations are not met, the Company is subject to a cash penalty of 1% for each month the registration is delayed, subject to a maximum of 18%. Additionally, the warrants contain a cashless exercise feature if a registration statement is not effective on the date of exercise, and a provision for exercise price adjustments under certain circumstances as defined in the warrant agreement. In connection with the transaction, the Company issued to the placement agent 277,667 shares of common stock and a warrant to purchase 111,067 shares of common stock, with terms identical to those issued to the investors.

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Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations.

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 arrangements 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 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 systems. We believe this strategy will allow 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 the ''mass market'' consumer. In addition, we continue to opportunistically look for titles to publish on the PC and other home console systems.

Net Revenues. Our revenues are derived from the following types of offerings:

- Games. Our video games consist of ''premium'' titles and ''value'' titles for console and handheld video game systems. Premium titles are higher-priced video games that typically involve greater development and marketing costs. We work with third-party development studios to develop our own proprietary titles and we also license rights to well-known properties from third parties. Value titles are typically sold at suggested retail prices below $20 and typically involve comparatively lower development and marketing costs than our premium titles; and
- Other digital entertainment products. We develop, manufacture and market a variety of digital media peripherals and applications including ''plug-and-play'' video game systems. These products connect directly to a user's television and play pre-installed video games without the need for a dedicated console. We have also published GBA video titles utilizing our video compression technology, enabling users to view up to 90 minutes of color video content with

stereo audio on their GBA or DS, using a standard GBA cartridge. We entered into licensing agreements with entertainment industry leaders for GBA Video content.

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. Our gross profit is directly affected by the mix of revenues from our premium handheld versus value titles. The excess of net revenues over product costs has the potential to be substantially higher from publishing premium titles given the relatively lower manufacturing costs and higher sales prices. However, development and license fees incurred to produce premium 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 developers of our video games and other products, 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. Although there can be no assurance, legal costs incurred in connection with our pending shareholder litigation in excess of related deductibles are expected to be covered under our insurance policies. Therefore, they are not reflected in operating results.

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.

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.



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We have identified the policies below as critical to our business operations and 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.

For those agreements which provide customers with the right to multiple copies in exchange for guaranteed minimum royalty amounts, revenue is recognized at delivery of the product master or the first copy since we have no continuing obligations including requirements for duplication. Royalties on sales that exceed the guaranteed minimum are recognized as earned.

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. 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 three and nine month periods ended July 31, 2007 and 2006 we provided allowances for future price protection and other allowances of $0.3 million and $1.9 million, and $0.1 million and $2.2 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 the factor generally buys our receivables without recourse.

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 software 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



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intellectual property rights in the development of 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.

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. We recorded an expense of $2.4 million for the nine months ended July 31, 2006 related to development costs for projects which were either canceled, or for which full recoverability was not expected. In the three and nine month periods ended July 31, 2007 and 2006 we charged $1.6 and $5.7 million, and $2.8 million and $9.1 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 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 have decided to use the modified prospective transition method, which require 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.

Results of operations

Three months ended July 31, 2007 versus three months ended July 31, 2006

Net Revenues. Net revenues for the three months ended July 31, 2007 decreased to $10.0 million from $12.4 million in the comparable quarter last year. The $2.4 million decrease is primarily due a decrease in revenues generated from newly released games. Our quarterly revenues may fluctuate significantly based on the timing of releases of our premium console games. During the three months ended July 31, 2006 we generated significant revenue from the release of the frontline title ‘‘Jaws Unleashed’’, to be sold at retail during the summer selling months. During the three months ended July 31, 2007 we did not have a new release console game of similar magnitude.

Gross Profit. Gross profit for the three months ended July 31, 2007 was $3.0 million compared to a gross profit of $4.1 million in the same quarter last year. The decrease in gross profit is primarily attributable to the lower net revenues discussed above, and a higher gross profit as a percentage of net sales related to the premium console title ‘‘Jaws Unleashed’’ released in 2006. As discussed above, premium console games generally have higher gross profit potential, as well as higher risk related to the upfront development and licensing fees typically required to publish them. Gross profit as a percentage of net sales was 30% for the three months ended July 31, 2007 compared to 33% for the three months ended July 31, 2006.

Product Research and Development Expenses. Research and development costs decreased $0.1 million to $0.5 million for the three months ended July 31, 2007 from $0.6 million for the comparable period in 2006. These expenses have remained at a stable level due to the focus on games with relatively shorter development times and lower development costs.

Selling and Marketing Expenses. Total selling and marketing expenses were approximately $2.0 million for the three months ended July 31, 2007, a $ 0.2 decrease from $2.2 million for the same



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period in 2006. Selling and marketing expenses consist primarily of salaries, commissions, and internet and print media costs associated with the games that were released during the period. Selling and marketing expense as a percentage of net sales was approximately 20% for the three months ended July 31, 2007, compared to 17% for the same quarter last year.

General and Administrative Expenses. For the three month period ended July 31, 2007 general and administrative expenses were $1.7 million, a decrease of $1.4 million from $3.1 million in the comparable period in 2006. The decrease is primarily due to lower non cash compensation expense and lower legal expenses related to the class action lawsuit and other litigation. During 2006 we recorded expenses of approximately $0.8 million related to legal expenses that were below the deductible in our directors and officers liability insurance policy, or otherwise not reimbursable under the policy. We recorded $0.2 million and $0.5 million of stock compensation expense related to SFAS 123(R) for the three months ended July 31, 2007 and 2006, respectively.

Gains on Settlement of Liabilities and Other Gains. Gains on settlement of liabilities for the three months ended July 31, 2006 and 2007 relates to the settlement of legal, marketing and development accounts payable for less than the invoice amount.

Operating Loss. Operating loss for the three months ended July 31, 2007 was $1.3 million, compared to operating loss of $0.3 million for the three month period ended July 31, 2006. The increase in operating loss was primarily due to the decreased revenues and operating expenses discussed above, and a decrease in gain on settlement of liabilities and other gains of $1.3 million from 2006.

Interest and Financing Costs, Net. Interest and financing costs were approximately $0.3 million for the three months ended July 31, 2007 compared to $0.4 million for the three months ended July 31, 2006. The decline is primarily due to a reduction in fees related to the factoring of accounts receivable.

Income Taxes. We did not record any income tax benefit because realization of the resulting loss carryforwards can not be assured.

Net Loss. Net loss for the three months ended July 31, 2007 was $1.5 million, an increase of $0.8 million from a net loss of $0.7 million for the comparable period in 2006, primarily due to a $1.4 million gain on settlement recorded in 2006.

Nine months ended July 31, 2007 versus nine months ended July 31, 2006

Net Revenues. Net revenues for the nine months ended July 31, 2007 decreased to $39.1 million from $45.2 million in the comparable period last year. The $6.1 million decrease is primarily due to lower revenues from the sale of GBA video movies. During the nine months ended July 31, 2006 we released two 90 minute video movies for the Nintendo GBA handheld system. During 2007 the Company changed its focus to handheld and console games with lower development, royalty and marketing expense requirements.

Gross Profit. Gross profit for the nine months ended July 31, 2007 was $13.6 million compared to a gross profit of $15.6 million in the same quarter last year. The decrease in gross profit is primarily attributable to the lower net revenues discussed above. Gross profit as a percentage of net sales was 35% for the nine months ended July 31, 2007 and 2006.

Product Research and Development Expenses. Research and development costs decreased $0.3 million to $1.7 million for the nine months ended July 31, 2007 from $2.0 million for the comparable period in 2006. The decrease is principally the result of a reduction in the number of quality assurance employees in January 2006, as we changed our focus to games with shorter development times and relatively lower development costs.

Selling and Marketing Expenses. Total selling and marketing expenses decreased to $5.7 million for the nine months ended July 31, 2007 from $8.5 million in the same nine month period in 2006. The $2.8 million decrease is primarily due to a decrease in media and other marketing costs associated with premium games that were launched in the quarter ended January 31, 2006. Selling and marketing

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expense as a percentage of net sales was approximately 15% for the nine months ended July 31, 2007, compared to 19% for the same quarter last year. The decline is the result of an overall decrease in media costs related to the premium games.

General and Administrative Expenses.    For the nine month period ended July 31, 2007 general and administrative expenses were $6.1 million, a decrease of $1.9 million from $8.0 million in the comparable period in 2006. The decrease is primarily due to lower legal costs. During 2006 we recorded legal expenses of approximately $1.2 million related to shareholder and other litigation that were below the deductibles in our insurance policies, or otherwise not reimbursable. We recorded $1.0 million of stock compensation expense related to SFAS 123(R) for the nine months ended July 31, 2007 and 2006.

Gains on Settlement of Liabilities and Other Gains.    Gains on settlement of liabilities for the nine months ended July 31, 2006 consists of $1.5 million related to negotiated reductions in royalty payments due for certain video and video game titles, $0.5 million gain on the sale of the rights to certain video game titles, and $2.5 million gain on the settlement of legal and marketing and development accounts payable for less than the invoice amount.

Settlement of litigation and related costs, net.    As discussed in note 7 to the financial statements, the Company and the Individual Defendants have been in negotiations with Plaintiffs to resolve the Securities Class Action lawsuit, and have reached a tentative understanding on settlement terms. These terms include a payment in the form of common stock of the Company with a market value of approximately $2.5 million in addition to payments in cash from proceeds of the Company’s insurance carrier. Assuming a Class Action settlement is concluded, it will require court approval before it can become effective. The Company anticipates that its insurance will be adequate to pay the cash portion of such settlement and related legal costs and will also be adequate to address Trinad Capital’s litigation against the Company. There is no assurance that the settlement described above will be achieved, and if not achieved, there can be no assurance that the Company’s insurance will be adequate to cover the Company’s costs relating to the Class Action lawsuit or its other litigation. Any expenses incurred in connection with such litigation not covered by available insurance or any adverse resolution of such litigation could have a material adverse effect on our financial condition.

Operating Loss.    Operating loss for the nine months ended July 31, 2007 was $2.3 million, compared to an operating loss $1.1 million for the nine month period ended July 31, 2006. The increase in operating loss was primarily due to a charge for the settlement of litigation in 2007 of $2.5 million and decreased gain on settlement of liabilities and other gains of $4.2 million, partially offset by lower operating expenses discussed above and a $2.3 million decrease in impairment charges.

Interest and Financing Costs, Net.    Interest and financing costs increased to $1.5 million for nine months ended July 31, 2007 from $1.4 million for the nine months ended July 31, 2006.

Income Taxes.    We did not record any income tax benefit because realization of the resulting loss carryforwards can not be assured.

Net Loss.    Net Loss for the nine months ended July 31, 2007 was $3.8 million, an increase of $1.3 million from a net loss of $2.5 million for the comparable period in 2006. The increase in net loss was primarily due to a charge for the settlement of litigation in 2007 of $2.5 million and decreased gain on settlement of liabilities and other gains of $4.2 million, partially offset by lower operating expenses discussed above and a $2.3 million decrease in impairment charges.

Liquidity and Capital Resources

Historically, we have met our capital needs through our factoring and purchase order financing arrangements, sales of our common stock, and advances from customers.

We do not have any bank debt. To satisfy our liquidity needs, we factor our receivables. We also utilize purchase order financing through the factor and through a finance company to provide funding for the manufacture of our products. In connection with these arrangements, the finance company and the factor have a security interest in substantially all of our assets.



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Under the terms of our factoring agreement, we assign our accounts receivable to the factor. The factor, in its sole discretion, determines whether or not it will accept a receivable based on its assessment of its credit risk. Once a receivable is accepted by the factor, the factor assumes substantially all of the credit risk associated with the receivable. The factor is required to remit payments to us for the assigned accounts receivable in accordance with the terms of the assigned invoice, regardless of whether the factor receives payment on the receivable, so long as the customer does not have a valid dispute related to the invoice. The amount remitted to us by the factor equals the invoiced amount adjusted for allowances and discounts we have provided to the customer less factor charges of 0.5% of invoiced amounts, subject to a minimum charge per invoice, for these credit and collection services.

We utilize purchase order financing arrangements in order to enable us to provide letters of credit necessary for the manufacture of our products. Manufacturers require us to present a letter of credit in order to manufacture the products required under a purchase order. Currently, we utilize letters of credit from a finance company which charges a fee of 1.5% of the purchase order amount for each transaction for 30 days, plus a maintenance fee of 0.05% per day (18% annually) for any advances outstanding under the financing arrangement for more than 30 days. Our factor also provides purchase order financing at a cost of 0.5% of the purchase order amount for each transaction for 30 days. Additional charges are incurred under both arrangements if letters of credit remain outstanding in excess of the original time period.

In addition, we may request that the factor provide us with cash advances based on our accounts receivable and inventory. The factor may either accept or reject our request for advances at its discretion. Amounts to be paid to us by the factor for any assigned receivable are offset by any amounts previously advanced by the factor. As our needs require, we may request that the factor advance 80% of the eligible receivables and advance 50% of inventory.

On September 5, 2007, we sold 3,966,668 shares of common stock, and warrants to purchase an additional 1,586,668 shares of common stock, to a group of accredited investors for gross proceeds of $5.9 million. The warrants have an exercise price of $2.04 per share and a term of five years, which begins six months from the issue date. We are obligated to file a registration statement for the securities within 45 days of the closing of the transaction, and have the registration declared effective by the Securities and Exchange Commission within 120 days of the closing of the transaction. If the registration obligations are not met, we are subject to a cash penalty of 1% for each month the registration is delayed, subject to a maximum of 18%. Additionally, the warrants contain a cashless exercise feature if a registration statement is not effective on the date of exercise, and a provision for exercise price adjustments under certain circumstances as defined in the warrant agreement. In connection with the transaction, we issued to a placement agent, 277,667 shares of common stock and a warrant to purchase 111,067 shares of common stock, with terms identical to those issued to the investors.

As of July 31, 2007, management believes that there will be sufficient capital resources from operations and existing financing arrangements, including the sale of common stock described above, to meet our requirements for development, production, marketing, purchases of equipment, and the acquisition of intellectual property rights for future products for the next twelve months. However, in the event that we are unable to generate the level of operating revenues in the business plan, we will be required to reduce operating expenditures or obtain additional sources of financing to continue operations. There can be no assurance that additional sources of financing will be available on acceptable terms, if at all. If no additional sources of financing are available, it could create a material adverse effect on future operating prospects of the Company.

As a result of recurring losses incurred by us, the report of our independent Registered Public Accounting firm on the financial statements as of October 31, 2005 and 2006 contained an explanatory paragraph indicating that we may be unable to continue as a going concern.

Advances From Customers.    On a case by case basis, distributors and other customers have in the past agreed to provide us with cash advances on their orders. These advances were then applied

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against future sales to these customers. In exchange for these advances, we offer these customers beneficial pricing or other considerations.

Commitments and Contingencies.    We do not currently have any material commitments with respect to any capital expenditures.

As of July 31, 2007 we had open letters of credit aggregating $0.5 million for inventory purchases to be delivered during the quarter ended July 31, 2007.

We are committed under agreements with certain developers and content providers for milestone and license fee payments aggregating $3.1 million, $1.7 million of which are payable through October 31, 2007.

As of July 31, 2007 we were committed under operating leases for office space and equipment for approximately $0.9 million through October 2009.

Effective January 1, 2007, upon his resignation, we entered into a transition agreement with Morris Sutton, our former Chairman Emeritus under which he will provide services as a consultant for a two year period. The agreement provides for a monthly retainer of $29,175 and a commission equal to 2% of sales to certain specified accounts.

As previously disclosed, the Company and the Individual Defendants have been in negotiations with Plaintiffs to resolve the Securities Class Action lawsuit, and have reached a tentative understanding on settlement terms. These terms include a payment in the form of common stock of the Company with a market value of approximately $2.5 million in addition to payments in cash from proceeds of the Company’s insurance carrier. Assuming a Class Action settlement is concluded, it will require court approval before it can become effective. The Company anticipates that its insurance will be adequate to pay the cash portion of such settlement and related legal costs and will also be adequate to address Trinad Capital’s litigation against the Company. There is no assurance that the settlement described above will be achieved, and if not achieved, there can be no assurance that the Company’s insurance will be adequate to cover the Company’s costs relating to the Class Action lawsuit or Trinad Capital’s litigation against the

Company. Any expenses incurred in connection with such litigation not covered by available insurance or any adverse resolution of such litigation could have a material adverse effect on our financial condition.

On July 26, 2007, Charlie Bolton filed a complaint against the Company and several current and former directors and officers of the Company in the United States District Court for the District of New Jersey. The current or former officers and directors named as defendants in the complaint are Morris Sutton, Jesse Sutton, Joseph Sutton and Carl Yankowski. The allegations in the Complaint are similar to those in the Amended Consolidated Complaint filed in the In re: Majesco Securities Litigation putative class action and the Complaint filed in Trinad Capital's complaint against the Company and several current and former directors and officers of the Company discussed above. The Complaint alleges four causes of action: (1) a claim under Section 10(b) of the Exchange Act (and Rule 10b-5 promulgated thereunder) against all the named defendants; (2) a claim under Section 20(a) of the Exchange Act against Morris Sutton, Jesse Sutton and Joseph Sutton; (3) a claim under Section 18(a) of the Exchange Act against all the named defendants; and (4) a common law fraud claim against Morris Sutton, Jesse Sutton, Joseph Sutton and Carl Yankowski. Bolton seeks compensatory damages of no less than $2 million and $2 million in punitive damages. No liability has been recorded in the financial statements as of July 31, 2007 for legal or settlement expenses related the complaint, as they can not be reasonably estimated at this time. Expenses incurred in connection with Bolton's litigation or any adverse resolution thereof could have a material adverse effect on the Company's financial condition.

Cash Flows

Cash was $3.8 million at July 31, 2007 and October 31, 2006.

Operating Cash Flows. Cash provided by operating activities during the nine months ended July 31, 2007 was $1.5 million compared $1.1 million during the same period in the prior year. The



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$0.4 million increase in cash provided by operations in 2007 was due primarily to a reduction in our net operating assets, partially offset by an increased net loss. We expect continued volatility in the use and availability of cash due to the seasonality of our business, timing of receivables collections and working capital needs necessary to finance our business and growth objectives.

Investing Cash Flows. Cash used in investing activities for the nine months ended July 31, 2007 and 2006 consists primarily of purchases of computer equipment and leasehold improvements necessary to accommodate our infrastructure needs.

Financing Cash Flows. Cash used in financing activities in the nine months ended July 31, 2007 was $1.3 million relating to a reduction in outstanding inventory financing. During the nine month period ended July 31, 2006 we generated $0.2 million due to an increase in the inventory financing balance.

Item 3. Quantitative and Qualitative Disclosures about Market Risk

We are exposed to various market risks, including the changes in foreign currency exchange rates and interest rates. Market risk is the potential loss arising from changes in market rates and prices. Foreign exchange contracts used to hedge foreign currency exposure are subject to market risk. We do not enter into derivatives or other financial instruments for trading or speculative purposes. At July 31, 2007 we did not have any foreign exchange contracts.

Item 4. Controls and Procedures

Our management, with the participation of our Interim Chief Executive Officer and Chief Financial Officer, has evaluated the effectiveness of our disclosure controls and procedures, as defined in Exchange Act Rule 13a-15(e) and 15d-15(e), as of the end of the period covered by this report.

In designing and evaluating our disclosure controls and procedures, management recognized that any controls and procedures, no matter how well designed and operated, can provide only reasonable assurance of achieving the desired control objectives.

While we believe our disclosure controls and procedures and our internal control over financial reporting have improved, no system of controls can prevent errors and fraud. A control system, no matter how well designed and operated, can provide only reasonable, not absolute, assurance that the control system's objectives will be met. Further, the design of a control system must reflect the fact that there are resource constraints, and the benefits of controls must be considered relative to their costs. Because of the inherent limitations in all control systems, no evaluation of controls can provide absolute assurance that all control issues and instances of fraud, if any, within our company have been detected. These inherent limitations include the realities that judgments in decision-making can be faulty, and that breakdowns can occur. Controls can also be circumvented by individual acts of some people, by collusion of two or more people, or by management override of the controls. The design of any system of controls is based in part upon certain assumptions about the likelihood of future events, and there can be no assurance that any design will succeed in achieving its stated goals under all potential future conditions. Over time, controls may become inadequate because of changes in conditions or deterioration in the degree of compliance with its policies or procedures. Because of the inherent limitations in a cost-effective control system, misstatements due to error or fraud may occur and not be detected.

Subject to the limitations above, management believes that the consolidated financial statements and other financial information contained in this report, fairly present in all material respects our financial condition, results of operations, and cash flows for the periods presented.

Based on the evaluation of the effectiveness of our disclosure controls and procedures, our Interim Chief Executive Officer and Chief Financial Officer concluded that our disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) were effective at a reasonable assurance level. There were no changes in our internal control over financial reporting that occurred during our most recent fiscal quarter that materially affected, or that are reasonably likely to materially affect, our internal control over financial reporting.



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PART II. OTHER INFORMATION

Item 1. Legal Proceedings

On July 26, 2007, Charlie Bolton filed a complaint against the Company and several current and former directors and officers of the Company in the United States District Court for the District of New Jersey. The current or former officers and directors named as defendants in the complaint are Morris Sutton, Jesse Sutton, Joseph Sutton and Carl Yankowski. The allegations in the Complaint are similar to those in the Amended Consolidated Complaint filed in the In re: Majesco Securities Litigation putative class action and the Complaint filed in Trinad Capital's complaint against the Company and several current and former directors and officers of the Company. The Complaint alleges four causes of action: (1) a claim under Section 10(b) of the Exchange Act (and Rule 10b-5 promulgated thereunder) against all the named defendants; (2) a claim under Section 20(a) of the Exchange Act against Morris Sutton, Jesse Sutton and Joseph Sutton; (3) a claim under Section 18(a) of the Exchange Act against all the named defendants; and (4) a common law fraud claim against Morris Sutton, Jesse Sutton, Joseph Sutton and Carl Yankowski. Bolton seeks compensatory damages of no less than $2 million and $2 million in punitive damages. No liability has been recorded in the financial statements as of July 31, 2007. Expenses incurred in connection with Bolton's litigation or any adverse resolution thereof could have a material adverse effect on the Company's financial condition.

Item 1A. Risk Factors

A description of the risks associated with our business, financial condition, and results of operations is set forth in Part I, Item 1A, of our Annual Report on Form 10-K for the fiscal year ended October 31, 2006. These factors continue to be meaningful for your evaluation of the Company and we urge you to review and consider the risk factors presented in the Form 10-K. There have been no material changes to these risks during the quarter ended July 31, 2007.

Item 2. Unregistered Sales of Equity Securities and Use of Proceeds

None

Item 3. Defaults Upon Senior Securities

None

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

None

Item 5. Other Information

None

Item 6. Exhibits

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| 31.1 | Certification of Principal Executive Officer pursuant to Section 302 of the Sarbanes-Oxley Act of 2002. |
| 31.2 | Certification of Principal Financial Officer pursuant to Section 302 of the Sarbanes-Oxley Act of 2002. |
| 32 | Certification of pursuant to Section 906 of the Sarbanes-Oxley Act of 2002. |



SIGNATURE

Pursuant to the requirements of the Securities Exchange Act of 1934, the registrant has duly caused this report to be signed on its behalf by the undersigned thereunto duly authorized.

MAJESCO ENTERTAINMENT COMPANY
/s/ Jesse Sutton
Jesse Sutton
Interim Chief Executive Officer

Date: September 13, 2007