MULTIMEDIA GAMES INC
Form 10-Q
August 05, 2010

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

Form 10-Q

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

For the quarterly period ended June 30, 2010
OR
¨ TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934

For the transition period from ______ to ______

Commission File Number: 000-28318

Multimedia Games, Inc.
(Exact name of Registrant as specified in its charter)

Texas (State or other jurisdiction of incorporation or organization)	74-2611034 (IRS Employer Identification No.)
206 Wild Basin Road South, Building B, Fourth Floor Austin, Texas (Address of principal executive offices)	78746 (Zip Code)

(512) 334-7500
(Registrant's telephone number, including area code)

Registrant's website: www.multimediagames.com

None
(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 ý No ¨

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

Indicate by check mark whether the Registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, or a smaller reporting company. See the definitions of “large accelerated filer” “accelerated filer” and “smaller reporting company” in Rule 12b-2 of the Exchange Act:

Large Accelerated Filer ¨	Accelerated Filer ý
Non-Accelerated Filer ¨	Smaller Reporting Company ¨

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

As of August 4, 2010, there were 27,572,407 shares of the Registrant’s common stock, par value $0.01 per share, outstanding.

FORM 10-Q

INDEX

PART I. FINANCIAL INFORMATION

Item 1.	Condensed Financial Statements (Unaudited)	
	Consolidated Balance Sheets (As of June 30, 2010 and September 30, 2009)	3
	Consolidated Statements of Operations (For the three months ended June 30, 2010 and 2009)	5
	Consolidated Statements of Operations (For the nine months ended June 30, 2010 and 2009)	6
	Consolidated Statements of Cash Flows (For the nine months ended June 30, 2010 and 2009)	7
	Notes to Consolidated Financial Statements	8
Item 2.	Management's Discussion and Analysis of Financial Condition and Results of Operations	22
Item 3.	Quantitative and Qualitative Disclosures about Market Risk	35
Item 4.	Controls and Procedures	35

PART II. OTHER INFORMATION

Item 1.	Legal Proceedings	36
Item 1A.	Risk Factors	36
Item 6.	Exhibits	50
Signatures		51
Exhibit Index		

PART I

FINANCIAL INFORMATION

Item 1. Condensed Financial Statements

MULTIMEDIA GAMES, INC.
CONDENSED CONSOLIDATED BALANCE SHEETS
As of June 30, 2010 and September 30, 2009
(In thousands, except shares)
(Unaudited)

ASSETS	June 30, 2010	September 30, 2009
CURRENT ASSETS:		
Cash and cash equivalents	$30,814	$12,455
Accounts receivable, net of allowance for doubtful accounts of $2,945 and $3,676, respectively	11,099	13,424
Inventory	4,967	5,742
Deferred contract costs, net	—	1,826
Prepaid expenses and other	2,311	2,806
Current portion of notes receivable, net	13,419	15,780
Federal and state income tax receivable	5,930	6,246
Deferred income taxes	—	1,138
Total current assets	68,540	59,417
Restricted cash and long-term investments	737	804
Property and equipment and leased gaming equipment, net	55,505	69,050
Long-term portion of notes receivable, net	27,617	40,124
Intangible assets, net	30,943	33,361
Value added tax receivable	6,997	7,516
Other assets	2,285	2,379
Deferred income taxes	—	2,969
Total assets	$192,624	$215,620
LIABILITIES AND STOCKHOLDERS' EQUITY		
CURRENT LIABILITIES:		
Current portion of long-term debt	$750	$750
Accounts payable and accrued expenses	26,025	27,626
Deferred revenue	2,619	2,341
Total current liabilities	29,394	30,717
Revolving line of credit	15,000	15,000
Long-term debt, less current portion	44,063	59,250
Other long-term liabilities	737	789
Deferred revenue, less current portion	2,272	2,409
Total liabilities	91,466	108,165
Commitments and contingencies		
Stockholders' equity:		
Preferred stock:		
Series A, $0.01 par value, 1,800,000 shares authorized, no shares issued and outstanding	—	—
Series B, $0.01 par value, 200,000 shares authorized, no shares issued and outstanding	—	—

Common stock, $0.01 par value, 75,000,000 shares authorized, 33,348,687 and 33,121,337 shares issued, and 27,445,270 and 27,217,920 shares outstanding, respectively	334	331

3

MULTIMEDIA GAMES, INC.
CONDENSED CONSOLIDATED BALANCE SHEETS – (Continued)
As of June 30, 2010 and September 30, 2009
(In thousands, except shares)
(Unaudited)

	June 30, 2010	September 30, 2009
Additional paid-in capital	88,766	86,317
Treasury stock, 5,903,417 common shares at cost	(50,128)	(50,128)
Retained earnings	63,437	72,803
Accumulated other comprehensive loss, net	(1,251)	(1,868)
Total stockholders' equity	101,158	107,455
Total liabilities and stockholders' equity	$ 192,624	$ 215,620

The accompanying notes are an integral part of the condensed consolidated financial statements.

MULTIMEDIA GAMES, INC.

CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS
For the Three Months Ended June 30, 2010 and 2009
(In thousands, except per share data)
(Unaudited)

	Three Months Ended June 30,	
	2010	2009
REVENUES:		
Gaming operations	$23,810	$27,407
Gaming equipment and system sales	4,935	3,786
Other	331	936
Total revenues	29,076	32,129
OPERATING COSTS AND EXPENSES:		
Cost of revenues (1)	3,302	2,137
Selling, general and administrative expenses	14,703	15,326
Write-off, reserve, impairment & settlement charges	381	299
Amortization and depreciation	12,760	15,581
Total operating costs and expenses	31,146	33,343
Operating loss	(2,070)	(1,214)
OTHER INCOME (EXPENSE):		
Interest income	830	1,156
Interest expense	(1,012)	(1,390)
Loss before income taxes	(2,252)	(1,448)
Income tax benefit	2,612	288
Net income (loss)	$360	$(1,160)
Basic earnings (loss) per common share	$0.01	$(0.04)
Diluted earnings (loss) per common share	$0.01	$(0.04)
Shares used in earnings (loss) per common share:		
Basic	27,437	26,693
Diluted	27,962	26,693

(1) Cost of revenues exclude depreciation and amortization of gaming equipment, content license rights and other depreciable assets, which are included separately in the amortization and depreciation line item

The accompanying notes are an integral part of the condensed consolidated financial statements.

5

MULTIMEDIA GAMES, INC.
CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS
For the Nine Months Ended June 30, 2010 and 2009
(In thousands, except per share data)
(Unaudited)

	Nine Months Ended June 30,	
	2010	2009
REVENUES:		
Gaming operations	$69,648	$82,636
Gaming equipment and system sales	16,354	9,907
Other	1,477	2,032
Total revenues	87,479	94,575
OPERATING COSTS AND EXPENSES:		
Cost of revenues (1)	9,139	6,311
Selling, general and administrative expenses	43,493	46,091
Write-off, reserve, impairment & settlement charges	3,896	10,271
Amortization and depreciation	39,984	46,085
Total operating costs and expenses	96,512	108,758
Operating loss	(9,033)	(14,183)
OTHER INCOME (EXPENSE):		
Interest income	2,798	3,692
Interest expense	(3,462)	(5,416)
Other income	-	74
Loss before income taxes	(9,697)	(15,833)
Income tax benefit	331	5,355
Net loss	$(9,366)	$(10,478)
Basic and diluted loss per common share	$(0.34)	$(0.39)
Shares used in loss per common share:		
Basic and diluted	27,340	26,653

(1) Cost of revenues exclude depreciation and amortization of gaming equipment, content license rights and other depreciable assets, which are included separately in the amortization and depreciation line item

The accompanying notes are an integral part of the condensed consolidated financial statements.

MULTIMEDIA GAMES, INC.
CONSOLIDATED STATEMENTS OF CASH FLOWS
For the Nine Months Ended June 30, 2010 and 2009
(In thousands)
(Unaudited)

	Nine Months Ended June 30,	
CASH FLOWS FROM OPERATING ACTIVITIES:	2010	2009
Net loss	$(9,366)	$(10,478)
Adjustments to reconcile net loss to cash provided by operating activities:		
Amortization	2,555	3,763
Depreciation	37,429	42,322
Accretion of contract rights	5,053	4,500
Adjustments to long-lived assets	704	1,316
Deferred income taxes	4,107	(1,879)
Share-based compensation	1,452	1,487
Provision for doubtful accounts	2,914	920
Interest income from imputed interest	(2,528)	(3,313)
Changes in operating assets and liabilities:		
Accounts receivable	2,124	(1,151)
Inventory	1,028	(555)
Deferred contract costs	1,826	(1,144)
Prepaid expenses and other	329	(385)
Federal and state income tax receivable	316	(1,900)
Notes receivable	1,679	1,176
Accounts payable and accrued expenses	(571)	2,547
Other long-term liabilities	15	(210)
Deferred revenue	141	(860)
NET CASH PROVIDED BY OPERATING ACTIVITIES	49,207	36,156
CASH FLOWS USED IN INVESTING ACTIVITIES:		
Acquisition of property and equipment and leased gaming equipment	(28,521)	(37,118)
Transfer of leased gaming equipment to inventory	4,573	846
Acquisition of intangible assets	(2,612)	(2,266)
Advances under development agreements	(3,040)	(7,000)
Repayments under development agreements	13,233	15,766
NET CASH USED IN INVESTING ACTIVITIES	(16,367)	(29,772)
CASH FLOWS USED IN FINANCING ACTIVITIES:		
Proceeds from exercise of stock options, warrants, and related tax benefit	1,000	378
Principal payments of long-term debt	(15,187)	(925)
Proceeds from revolving lines of credit	15,000	10,000
Payments on revolving lines of credit	(15,000)	(13,000)
NET CASH USED IN FINANCING ACTIVITIES	(14,187)	(3,547)
EFFECT OF EXCHANGE RATES ON CASH	(294)	312
Net increase in cash and cash equivalents	18,359	3,149
Cash and cash equivalents, beginning of period	12,455	6,289
Cash and cash equivalents, end of period	$30,814	$9,438
SUPPLEMENTAL CASH FLOW DATA:		

Interest paid	$2,889	$4,879
Income tax refunded, net	$(5,405)	$(2,124)
NON-CASH TRANSACTIONS:		
Change in contract rights resulting from imputed interest on development agreement notes receivable	$(229)	$(342)

The accompanying notes are an integral part of the condensed consolidated financial statements.

7

1. SIGNIFICANT ACCOUNTING POLICIES

The accompanying condensed consolidated financial statements should be read in conjunction with Multimedia Games, Inc. (the "Company," "we," "us," or "our") consolidated financial statements and footnotes contained within the Company's Annual Report on Form 10-K for the year ended September 30, 2009.

The unaudited condensed consolidated financial statements included herein as of June 30, 2010, and for each of the three and nine month periods ended June 30, 2010 and 2009, have been prepared by the Company pursuant to accounting principles generally accepted in the United States (U.S. GAAP), and the rules and regulations of the Securities and Exchange Commission, or SEC. They do not include all of the information and footnotes required by accounting principles generally accepted in the United States for complete financial statements. The information presented reflects all adjustments consisting solely of normal recurring adjustments which are, in the opinion of management, considered necessary to present fairly the financial position, results of operations, and cash flows for the periods. Operating results for the period ended June 30, 2010 are not necessarily indicative of the results which will be realized for the year ending September 30, 2010. References to specific U.S. GAAP within this report cite topics within the Financial Accounting Standards Board ("FASB") Accounting Standards Codification ("ASC"). We have evaluated all subsequent events through the date that the condensed consolidated financial statements were issued. The condensed consolidated balance sheet as of September 30, 2009 was derived from the audited consolidated financial statements at that date.

Operations – The Company is a supplier of interactive systems, server-based gaming systems, interactive electronic games, player terminals, stand-alone player terminals, video lottery terminals, electronic scratch ticket systems, electronic instant lottery systems, player tracking systems, casino cash management systems, slot accounting systems, slot management systems, unified currencies and electronic and paper bingo systems for Native American tribes, racetrack casino, casino, charity and commercial bingo, sweepstakes, lottery and video lottery markets and the Company provides support and services and operations support for its customers and products. The Company designs and develops networks, software and content that provide its customers with, among other things, comprehensive gaming systems, some of which are delivered through a telecommunications network that links its player terminals with one another, both within and among gaming facilities. The Company's ongoing development and marketing efforts focus on Class II and Class III gaming systems and products for use by Native American tribes; video lottery terminals, video lottery systems, stand-alone player terminals, electronic instant scratch systems and other products for domestic and international lotteries; products for domestic and international charity and commercial bingo markets; and promotional, sweepstakes and amusement with prize systems. The Company's gaming systems are typically provided to customers under revenue-sharing arrangements, except for video lottery terminals in the Class III market in Washington State, which are typically sold for an up-front purchase price. The Company has undertaken a concerted effort to generate additional revenue through the sale of Class II and Class III gaming systems and products. The Company offers content for its gaming systems that has been designed and developed by the Company, as well as game themes the Company has licensed from others. The Company currently operates in one business segment.

Consolidation Principles – The Company's financial statements include the accounts of Multimedia Games, Inc. and its wholly-owned subsidiaries: MegaBingo, Inc., MGAM Systems, Inc., Innovative Sweepstakes Systems, Inc., MGAM Services, LLC, MGAM Systems International, Inc., MegaBingo International, LLC, Multimedia Games de Mexico 1, S. de R.L. de C.V., and Servicios de Wild Basin S. de R.L. de C.V. Intercompany balances and transactions have been eliminated in consolidation.

Accounting Estimates – The preparation of consolidated financial statements in conformity with U.S. GAAP requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities, the disclosure of contingent assets and liabilities at the date of the financial statements, and the reported amounts of revenues and expenses during the reporting period. Examples include share-based compensation, provisions for

doubtful accounts, recoverability of notes and value added tax receivables, contract losses, estimated useful lives of property and equipment and intangible assets, impairment of property and equipment and intangible assets, valuation of deferred income taxes, and the provision for and disclosure of litigation and loss contingencies. Actual results may differ materially from these estimates in the future.

Reclassification – Reclassifications were made to the prior-period financial statements to conform to the current period presentation. Specifically, the presentation of revenue was changed to more closely reflect the manner in which Company management analyzes the performance of the business and charges for write-offs, reserves, impairments and settlements are separately presented on the condensed consolidated statement of operations. In addition, value added tax receivable from the Mexican government was reclassed from other assets (non-current) to a separate line item on the face of the balance sheet. These reclassifications did not have an impact on the Company's previously reported results of operations or earnings (loss) per share amounts. Additionally, these reclassifications did not impact compliance with any applicable debt covenants in the Company's credit agreement.

Revenue Recognition – In accordance with the provision of ASC Topic 605, "Revenue Recognition", the Company recognizes revenue when all of the following have been satisfied:

§ Persuasive evidence of an arrangement exists;
§ Delivery has occurred;
§ Price to the buyer is fixed or determinable; and
§ Collectibility is probable.

Revenue – The Company derives revenue from the following sources:

§ Gaming Operations	–	Participation revenue generated from the Company's games placed under the Oklahoma Compact, Native American Class II products, charity bingo and other bingo products, lottery systems and Class III back office systems
§ Gaming equipment and systems sales	–	Direct sales of player terminals, licenses, back office systems and other related equipment
§ Other	–	Maintenance and service arrangements and other

The majority of the Company's gaming revenue is generated under lease participation arrangements when the Company provides its customers with player terminals, player terminal-content licenses and back-office equipment, collectively referred to as gaming equipment. Under these arrangements, the Company retains ownership of the gaming equipment installed at customer facilities, and the Company receives revenue based on a percentage of the net win per day generated by the gaming equipment. Revenue from lease participation arrangements are considered both realizable and earned at the end of each gaming day.

Gaming revenue generated by player terminals deployed at sites under development agreements is reduced by the accretion of contract rights from those development agreements. Contract rights are amounts allocated to intangible assets for dedicated floor space resulting from development agreements, described under "Development Agreements." The related amortization expense, or accretion of contract rights, is netted against its respective revenue category in the condensed consolidated statements of operations.

The Company also generates gaming revenues from back-office fees with certain customers. Back-office fees cover the service and maintenance costs for back-office servers installed in each gaming facility to run its gaming equipment, as well as the cost of related software updates. Back-office fees are considered both realizable and earned at the end of each gaming day.

Gaming Equipment and System Sales – The Company sells gaming equipment and gaming systems under independent sales contracts through normal credit terms or may grant extended credit terms under contracts secured by the related equipment, with interest recognized at market rates.

For sales arrangements with multiple deliverables, the Company applies the guidance from ASC Topic 985, "Software" and ASC Topic 605, "Revenue Recognition." Deliverables are divided into separate units of accounting if: (i) each item has value to the customer on a stand-alone basis; (ii) there is objective and reliable evidence of the fair value of the undelivered items; and (iii) delivery of the undelivered item is considered probable and substantially in the Company's control.

The majority of the Company's multiple element sales contracts are for some combination of gaming equipment, player terminals, content, system software, license fees and maintenance. For multiple element contracts considered a single unit of accounting, the Company recognizes revenues based on the method appropriate for the last delivered item.

The Company allocates revenue to each accounting unit based upon its fair value as determined by Vendor Specific Objective Evidence, or VSOE. VSOE of fair value for all elements of an arrangement is based upon the normal pricing and discounting practices for those products and services when sold individually. The Company recognizes revenue when the product is physically delivered to a customer controlled location or over the period in which the service is performed and defers revenue for any undelivered elements.

§ In those situations where each element is not essential to the function of the other, the “multiple deliverables” are bifurcated into accounting units based on their relative fair market value against the total contract value and revenue recognition on those deliverables is recorded when all requirements of revenue recognition have been met.

§ If any element is determined to be essential to the function of the other, revenues are generally recognized over the term of the services that are rendered.

In those situations where VSOE does not exist for any undelivered elements of a multiple element arrangement, the aggregate value of the arrangement, including the value of products and services delivered or performed, is initially deferred until all hardware and software is delivered, and then the entire amount of the arrangement is recognized ratably over the period of the last deliverable, generally the service period of the contract. Depending upon the elements and the terms of the arrangement, the Company recognizes certain revenues under the residual method. Under the residual method, revenue is recognized when VSOE of fair value exists for all of the undelivered elements in the arrangement, but does not exist for one or more of the delivered elements in the arrangement. Under the residual method, the Company defers the fair value of undelivered elements, and the remainder of the arrangement fee is then allocated to the delivered elements and is recognized as revenue, assuming the other revenue recognition criteria are met.

Costs and Billings on Uncompleted Contract – During fiscal 2008, the Company entered into a fixed-price contract with a customer, pursuant to which it will deliver an electronic bingo system. Revenues from this fixed-price contract are being recognized on the completed-contract method in accordance with ASC Subtopic 605-35, “Construction-Type and Production-Type Contracts.” During the three month period ended June 30, 2010, the Company determined substantial completion of the contract occurred for revenue recognition purposes as all deliverables under the contract were provided to the customer, with the exception of a one year warranty, and the customer had approved the deliverables or the specified time allotted for testing had expired. Therefore, the Company began recognizing revenue ratably over the one year warranty period and thus recognized revenue and costs of $795,000 and $762,000, respectively, under the contract for the periods ended June 30, 2010.

Contract costs include all direct material and labor costs, and those indirect costs related to contract performance, such as indirect labor, supplies and tools. General and administrative costs are charged to expense as incurred.

Costs in excess of amounts billed were classified as current assets under “Deferred contract costs, net.”

At September 30, 2009, the following amounts were recorded in the Company’s condensed consolidated balance sheet:

	September 30, 2009 (in thousands)
Costs incurred on uncompleted contracts	$ 3,697
Billings on uncompleted contracts	(1,871)
Deferred contract costs, net	$ 1,826

Cash and Cash Equivalents – The Company considers all highly liquid investments (i.e., investments which, when purchased, have original maturities of three months or less) to be cash equivalents.

Restricted Cash and Long-Term Investments – Restricted cash and long-term investments at June 30, 2010 and September 30, 2009, amounted to $737,000 and $804,000, respectively, representing the fair value of investments held by the Company’s prize fulfillment firm related to outstanding MegaBingo® jackpot prizes.

Allowance for Doubtful Accounts – The Company maintains an allowance for doubtful accounts related to its accounts receivable and notes receivable that have been deemed to have a high risk of uncollectibility. Management reviews its accounts receivable and notes receivable on a quarterly basis to determine if any receivables will potentially be uncollectible. Management analyzes historical collection trends and changes in its customer payment patterns, customer concentration, and creditworthiness when evaluating the adequacy of its allowance for doubtful accounts. In its overall allowance for doubtful accounts, the Company includes any receivable balances where uncertainty exists as to whether the account balance has become uncollectible. Based on the information available, management believes the allowance for doubtful accounts is adequate; however, actual write-offs might exceed the recorded allowance.

Inventory – The Company's inventory consists primarily of completed player terminals, related component parts and back-office computer equipment expected to be sold over the next twelve months. Inventories are stated at average costs, which approximate the lower of cost (first in, first out) or market.

Property and Equipment and Leased Gaming Equipment – Property and equipment and leased gaming equipment are stated at cost. The cost of property and equipment and leased gaming equipment is depreciated over their estimated useful lives, generally using the straight-line method for financial reporting, and regulatory acceptable methods for income tax reporting purposes. Player terminals and related components and equipment are included in the Company's rental pool. The rental pool can be further delineated as "rental pool – deployed", which consists of assets deployed at customer sites under participation agreements, and "rental pool – undeployed", which consists of assets with the Company that are available for customer use. Rental pool – undeployed consists of both new units awaiting deployment to a customer site and previously deployed units currently back with the Company to be refurbished awaiting re-deployment. Routine maintenance of property and equipment and leased gaming equipment is expensed in the period incurred, while major component upgrades are capitalized and depreciated over the estimated remaining useful life of the component. Sales and retirements of depreciable property are recorded by removing the related cost and accumulated depreciation from the accounts. Gains or losses on sales and retirements of property are reflected in the Company's results of operations.

Management reviews long-lived asset classes for impairment whenever events or changes in circumstances indicate that the carrying amount of an asset may not be recoverable. Recoverability of assets to be held and used is measured by a comparison of the carrying amount of an asset to its fair value, which considers the future undiscounted cash flows expected to be generated by the asset. If such assets are considered to be impaired, the impairment recognized is measured by the amount by which the carrying amount of the assets exceeds their fair value. Assets to be disposed of are reported at the lower of the carrying amount or the fair value less costs of disposal.

Deferred Revenue – Deferred revenue represents amounts from the sale of gaming equipment and systems that have been billed, or for which notes receivable have been executed, but which transaction has not met the Company's revenue recognition criteria. The cost of the related gaming equipment and systems has been offset against deferred revenue. Amounts are classified between current and long-term liabilities, based upon the expected period in which the revenue will be recognized.

Other Long-Term Liabilities – Other long-term liabilities include investments held at fair value by the Company's prize-fulfillment firm related to outstanding MegaBingo jackpot-prize-winner annuities. These annuities were $737,000 and $800,000 as of June 30, 2010 and September 30, 2009, respectively.

Fair Value of Financial Instruments – The carrying value of financial instruments reported in the accompanying condensed consolidated balance sheets for cash, accounts receivable, current portion of notes receivable, accounts payable, and accrued expenses payable and other liabilities, approximate fair value due to the immediate or short-term nature or maturity of these financial instruments. The carrying amount for our credit facility approximates fair value due to the fact that the underlying instrument includes provisions to adjust interest rates to approximate fair value.

Segment and Related Information – Although the Company has a number of operating divisions the Company reports as one segment, as these divisions meet the criteria for aggregation as permitted by ASC Topic 280, "Segment Reporting." ASC 280-10-50-11, "Aggregation Criteria", allows for the aggregation of operating segments if the segments have similar economic characteristics and if the segments are similar in each of the following areas:

1. The nature of the products and services
2. The nature of the production processes
3. The type or class of customer for their products and services
4. The methods used to distribute their products or provide their services
5. The nature of the regulatory environment, if applicable.

The Company is engaged in the business of designing, manufacturing and distributing gaming machines, video lottery terminals and associated systems and equipment, as well as the maintenance of these machines and equipment. Our production process is essentially the same for the entire Company and is performed via outsourced manufacturing partners, as well as in house manufacturing performed primarily at our warehouse and assembly facility in Austin, Texas. Our customers consist of entities in the business of operating gaming, bingo or lottery facilities, and include Native American Tribes, charity bingo operators and commercial entities licensed to conduct such business in their jurisdictions. The distribution of our products is consistent across the entire Company and is performed via an internal fleet of vehicles, as well as third party transportation companies. The regulatory environment is similar in every jurisdiction in that gaming is regulated and our games must meet the regulatory requirements established. In addition, the economic characteristics of each customer arrangement are similar in that we obtain revenue via a revenue share arrangement or direct sale of product or service, depending on the customer's need. These sources of revenue are consistent with respect to both product line and geographic area.

In addition, discrete financial information, such as costs and expenses, operating income, net income and EBITDA (Earnings before interest expense, income taxes, depreciation, amortization and accretion of contract rights), are not captured or analyzed by product line or geographic area. Our "Chief Operating Decision Maker" analyzes our product performance based on average daily play on a game level basis, which is consistent across all product lines and geographic areas. This average daily performance data along with customer needs are the key drivers for assessing how the Company allocates resources and assesses operating performance of the Company.

Costs of Computer Software – Software development costs have been accounted for in accordance with ASC Topic 985, "Software." Under ASC Topic 985, capitalization of software development costs begins upon the establishment of technological feasibility and prior to the availability of the product for general release to customers. The Company capitalized software development costs of approximately $820,000 and $677,000 during the three month periods ended June 30, 2010 and 2009, respectively, and $2.5 million and $1.8 million for the nine month periods ended June 30, 2010 and 2009, respectively. Software development costs primarily consist of personnel costs. The Company began to amortize capitalized costs when a product is available for general release to customers. Amortization expense is determined on a product-by-product basis at a rate not less than straight-line basis over the product's remaining estimated economic life, not to exceed five years. Amortization of software development costs is included in amortization and depreciation in the accompanying condensed consolidated statements of operations.

Income Taxes – The Company accounts for income taxes using the asset and liability method and applies the provisions of ASC Topic 740, "Income Taxes". Under ASC Topic 740, deferred tax liabilities or assets arise from differences between the tax basis of liabilities or assets and their bases for financial reporting, and are subject to tests of recoverability in the case of deferred tax assets. Deferred tax assets and liabilities are measured using enacted tax rates expected to apply to taxable income in the years in which those temporary differences are expected to be recovered or settled. The effect on deferred tax assets and liabilities of a change in tax rates is recognized in income in the period that includes the enactment date. A valuation allowance is provided for deferred tax assets to the extent realization is not judged to be more likely than not. Additionally, in accordance with ASC Topic 740, we are required to determine whether it is more likely than not (a likelihood of more than 50 percent) that a tax position will be sustained upon examination, including resolution of any related appeals or litigation processes, based on the technical merits of the position in order to record any financial statement benefit. If that step is satisfied, then we must measure the tax position to determine the amount of benefit to recognize in the financial statements. The tax position is measured at the largest amount of benefit that is greater than 50 percent likely of being realized upon ultimate settlement.

Treasury Stock – The Company utilizes the cost method for accounting for its treasury stock acquisitions and dispositions.

Share-Based Compensation – The Company accounts for share-based compensation under the provisions of ASC Topic 718, "Compensation – Stock Compensation." Among other items, ASC Topic 718 requires the Company to recognize in the financial statements, the cost of employee services received in exchange for awards of equity instruments, based on the grant date fair value of those awards. To measure the fair value of stock options granted to employees, the Company currently utilizes the Black-Scholes-Merton option-pricing model. The Company applied the "modified prospective" method, under which compensation cost is recognized in the financial statements beginning with the adoption date for all share-based payments granted after that date, and for all unvested awards granted prior to the adoption date. Expense is recognized over the required service period, which is generally the vesting period of the options.

The Black-Scholes-Merton model incorporates various assumptions, including expected volatility, expected life, and risk-free interest rates. The expected volatility is based on the historical volatility of the Company's common stock over the most recent period commensurate with the estimated expected life of the Company's stock options, adjusted

for the impact of unusual fluctuations not reasonably expected to recur. The expected life of an award is based on historical experience and on the terms and conditions of the stock awards granted to employees.

There were 7,600 option grants issued to employees during the three months ended June 30, 2010 at an average fair value per share price of $4.50. Total pretax share-based compensation for the three and nine month periods ended June 30, 2010 were $230,000 and $1.5 million, respectively; and $363,000 and $1.5 million, respectively, for the three and nine month periods ended June 30, 2009. The Company did not recognize an income tax benefit for stock-based compensation arrangements in the three or nine month periods ended June 30, 2010. The total income tax benefit recognized in the statement of operations for share-based compensation arrangements was $89,000 and $384,000 for the three and nine month periods ended June 30, 2009. As of June 30, 2010, $4.9 million of unamortized stock compensation expense, including estimated forfeitures, remained, which will be recognized over the vesting periods of the various option grants.

Foreign Currency Translation. The Company accounts for currency translation in accordance with ASC Topic 830. “Foreign Currency Matters.” Balance sheet accounts are translated at the exchange rate in effect at each balance sheet date. Income statement accounts are translated at the average rate of exchange prevailing during the period. Translation adjustments resulting from this process are charged or credited to other comprehensive income (loss) a component of shareholder equity, in accordance with ASC Topic 220, “Comprehensive Income.” Transactional currency gains and losses arising from transactions in currencies other than the Company’s local functional currency are included in the condensed consolidated statement of operations in accordance with ASC Topic 830.

Comprehensive Income (Loss). Comprehensive income (loss) consists of the following:

	Three months ended June 30,		Nine months ended June 30,	
	2010	2009	2010	2009
	(in thousands)		(in thousands)	
Net income (loss)	$360	$(1,160)	$(9,366)	$(10,478)
Foreign currency translation adjustment	(448)	846	617	(1,443)
Comprehensive loss	$(88)	$(314)	$(8,749)	$(11,921)

Recent Accounting Pronouncements Issued. In June 2009, the Financial Accounting Standards Board(“FASB”), issued Statement of Financial Accounting Standards No. 168, “The FASB Accounting Standards Codification and Hierarchy of Generally Accepted Accounting Principles.” FASB Accounting Standards Codification (ASC) has become the source of authoritative generally accepted accounting principles GAAP recognized by the FASB to be applied by nongovernmental entities. Rules and interpretive releases of the SEC under authority of federal securities laws are also sources of authoritative GAAP for SEC registrants. On the effective date of this statement, the codification will supersede all then-existing non-SEC accounting and reporting standards; and all non-grandfathered, non-SEC accounting literature not included in the codification will be superseded and deemed non-authoritative. The new codification standards have been adopted by the Company in its annual report on Form 10-K as of September 30, 2009. Reference to the new ASC topic, subtopic, or section has been provided in place of historical accounting literature. The adoption of codification standards did not impact our consolidated financial position, results of operation or cash flows.

In October 2009, FASB issued ASU No. 2009-13, “Revenue Recognition(Topic 605), Multiple-Deliverable Revenue Arrangements” and ASU No. 2009-14, “Software(Topic 985), Certain Revenue Arrangements that Include Software Elements,” both consensus of the FASB Emerging Issues Task Force. ASU No. 2009-13 establishes the accounting and reporting guidance for arrangements under which the vendor will perform multiple revenue-generating activities; specifically, how to separate deliverables and how to measure and allocate arrangement consideration to one or more units of accounting. ASU No. 2009-14 affects vendors that sell or lease tangible products in an arrangement that contains software that is more than incidental to the tangible product as a whole and clarifying what guidance should be used in allocating and measuring revenue. Upon adoption of these standards, a company can recognize revenue on delivered elements within a multiple elements arrangement based upon estimated selling prices, which is a departure from previous guidance. These standards are required to be implemented by October 1, 2010, We are currently evaluating the impact of implementation.

2. DEVELOPMENT AGREEMENTS

The Company enters into development agreements, including placement fees, to provide financing for new gaming facilities or for the expansion of existing facilities. In return, the facility dedicates a percentage of its floor space to placement of the Company’s player terminals, and the Company receives a fixed percentage of those player terminals’ win per unit over the term of the agreement. The agreements typically provide for some or all of the advances to be repaid by the customer to the Company. Amounts advanced in excess of those to be reimbursed by the customer are allocated to intangible assets and are generally amortized over the life of the contract, which is recorded as a reduction of revenue generated from the gaming facility. Certain of the agreements contain player terminal performance standards that could allow the facility to reduce a portion of the Company’s floor space. In the past and in the future, the Company may by mutual agreement and for consideration, amend these contracts to reduce its floor space at the facilities. Any proceeds received for the reduction of floor space is first applied as a recovery against the intangible asset or property and development for that particular development agreement, if any.

Management reviews intangible assets related to development agreements for impairment whenever events or changes in circumstances indicate that the carrying amount of an asset may not be recoverable. There were no events or changes in circumstances during the three and nine month periods ended June 30, 2010, which would require an impairment charge to the carrying value of intangible assets recorded in connection with development agreements. See Notes 6 “Notes Receivable” and Note 10 “Write-off, reserve, impairment and settlement charges” for further discussion of reserves recorded on notes receivable from development agreements.

During the nine month periods ended June 30, 2010, the Company advanced under development agreements $3.0 million compared to $7.0 million for the same period of 2009. The following net amounts related to advances made under development agreements and were recorded in the following balance sheet captions:

	June 30, 2010	September 30, 2009
Included in:	(In thousands)	
Notes receivable, net	$37,188	$50,288
Intangible assets – contract rights, net of accumulated amortization	$25,934	$28,175

3. INVENTORY

Inventory consisted of the following (in thousands):

	June 30, 2010	September 30, 2009
Raw materials and component parts	$2,309	$3,753
Work in progress	1,491	936
Finished goods	1,167	1,053
Total Inventory	$4,967	$5,742

Included in inventory as of June 30, 2010 and September 30, 2009, were reserves of approximately $121,000 and $931,000 for slow-moving or obsolete inventory and to reduce the carrying value of inventory to the lower of cost or market.

4. PROPERTY AND EQUIPMENT AND LEASED GAMING EQUIPMENT

The Company's property and equipment and leased gaming equipment consisted of the following (in thousands):

	June 30, 2010			September 30, 2009		
	Cost	Accum. Depr.	Net Book Value	Cost	Accum. Depr.	Net Book Value
Rental pool – deployed	$ 172,387	$ 129,783	$ 42,604	$ 192,944	$ 140,363	$ 52,581
Rental pool – undeployed (1)	78,011	67,566	10,445	85,031	72,219	12,812
Machinery and equipment	14,572	13,395	1,177	16,371	15,084	1,287
Computer software	7,789	7,237	552	7,720	6,636	1,084
Vehicles	2,472	2,139	333	3,064	2,900	164
Other	4,272	3,878	394	6,554	5,432	1,122
Total property and equipment and leased gaming equipment	$ 279,503	$ 223,998	$ 55,505	$ 311,684	$ 242,634	$ 69,050

(1)Gaming equipment and third-party gaming content licenses begin depreciating when they are available for customer use.

Property and equipment and leased gaming equipment is depreciated as follows: Rental pool – deployed and undeployed – 1.5 to 3 years; Machinery and equipment – 5 to 7 years; Computer software – 3 to 5 years; Vehicles – 3 to 10 years and Other – 3 to 7 years.

In accordance with ASC Topic 360, "Property, Plant, and Equipment," the Company (i) recognizes an impairment loss only if the carrying amount of a long-lived asset is not recoverable from its undiscounted cash flows; and (ii) measures an impairment loss as the difference between the carrying amount and fair value of the asset.

During the three and nine month periods ended June 30, 2010, in the ordinary course of business activities or upon reviewing the nature of the assets, the Company disposed, wrote off or sold $303,000 and $1.9 million, respectively of third-party gaming content licenses, Native American tribal gaming facilities and portable buildings, vehicles, deployed gaming equipment, or other equipment. In the same period ended June 30, 2009, the Company disposed, wrote off or sold $55,000 and $132,000, respectively.

The rental pool includes leased gaming equipment placed under participation arrangements that are either at customer facilities(rental pool – deployed) or warehoused by the Company for future deployment (rental pool – undeployed).

5. INTANGIBLE ASSETS

The Company's intangible assets consisted of the following:

	June 30, 2010	September 30, 2009	Estimated Useful Lives
	(In thousands)		
Contract rights	$49,131	$46,319	4-7 years
Internally-developed gaming software	30,615	28,388	1-5 years
Patents and trademarks	8,368	8,226	1-5 years
Other	961	961	3-5 years
Total intangible assets	89,075	83,894	
Less accumulated amortization – all other	(58,132)	(50,533)	
Total intangible assets, net	$30,943	$33,361	

Contract rights are amounts allocated to intangible assets for dedicated floor space resulting from development agreements or placement fees. The related amortization expense, or accretion of contract rights, is netted against its respective revenue category in the accompanying condensed consolidated statements of operations.

Internally developed gaming software is accounted for under the provisions of ASC Topic 985 "Software" and is stated at cost, which is amortized over the estimated useful life of the software, generally using the straight-line method. The Company amortizes internally-developed games over a twelve month period, gaming engines over an eighteen month period, gaming systems over a three-year period and its central management systems over a five-year period. Software development costs are capitalized once technological feasibility has been established, and are amortized when the software is placed into service. Any subsequent software maintenance costs, such as bug fixes and subsequent testing, are expensed as incurred. Discontinued software development costs are expensed when the determination to discontinue is made. For the three and nine month periods ended June 30, 2010, amortization expense related to internally-developed gaming software was $739,000 and $1.9 million, respectively; and $813,000 and $3.0 million, respectively, for the three and nine month periods ended June 30, 2009. During the three and nine month periods ended June 30, 2010, the Company wrote off $43,000 and $233,000, respectively, related to internally-developed gaming software and patents and trademarks, compared to write-offs of $372,000 and $827,000 in the same periods ended June 30, 2009.

Management reviews intangible assets for impairment whenever events or changes in circumstances indicate that the carrying amount of an asset may not be recoverable.

6. NOTES RECEIVABLE

The Company's notes receivable consisted of the following:

	June 30, 2010	September 30, 2009
	(In thousands)	
Notes receivable from development agreements	$44,413	$57,558
Less imputed interest discount reclassed to contract rights	(4,513)	(7,270)

Less allowance	(2,712)	—
Notes receivable from equipment sales and other	3,848	5,616
Notes receivable, net	41,036	55,904
Less current portion	(13,419)	(15,780)
Notes receivable – non-current	$27,617	$40,124

Notes receivable from development agreements are generated from reimbursable amounts advanced under development agreements. As of March 31, 2010, the Company reserved for a note receivable outstanding with an Alabama customer in the amount of $2.7 million. On April 27, 2010, this customer indicated to the Company that under current conditions its facility will remain closed and consequently has doubts as to their ability, in the short term, to make scheduled payments pursuant to the terms of its development agreement, which led the Company to conclude that collectability of the note receivable was no longer considered probable.

Notes receivable from equipment sales consisted of financial instruments issued by customers for the purchase of player terminals and licenses, and bore interest at 5.25% as of June 30, 2010. All of the Company's notes receivable from equipment sales are collateralized by the related equipment sold, although the value of such equipment, if repossessed, may be less than the note receivable outstanding.

7. VALUE ADDED TAX RECEIVABLE

The value added tax (VAT) receivable is a receivable from the Mexican taxing authority primarily related to a value added tax levied on product shipments originating outside of Mexico. At June 30, 2010 and September 30, 2009, the Company's VAT receivable was $7.0 million and $7.5 million, respectively. The majority of the VAT receivable relates to shipments that occurred from 2006 through 2008. A portion of the $7.0 million balance remains under audit by the Mexican taxing authority.

Preliminary audit results indicate that $2.3 million has been approved through audit for payment, $1.8 million of which was received in July 2010. The Company expects to collect the remaining $0.5 million within the next twelve months. Additionally, the Company believes it will be able to offset a portion of the current VAT receivable against a corresponding $1.3 million VAT payable recorded on our June 30, 2010 balance sheet.

The Company has received an initial ruling from the Mexican taxing authority indicating that the Mexican tax authority has challenged the registration of certain of the Company's transactions that have generated approximately $600,000 in VAT receivable. Mexican tax law permits the Company to formally contest the initial ruling, and the Company believes that it has the necessary documentation to support the portion that has been challenged. However, the final resolution of the contested balances remains uncertain and may adversely affect the carrying value of the receivable and may have an adverse affect on our foreign income tax expense.

8. ACCOUNTS PAYABLE AND ACCRUED EXPENSES

At June 30, 2010 and September 30, 2009, the Company's accounts payable and accrued expenses consisted of the following:

	June 30, 2010	September 30, 2009
	(In thousands)	
Trade accounts payable	$ 12,816	$ 12,431
Accued expenses	5,208	7,272
Accrued bonus and salaries	4,452	4,196
Other	3,549	3,727
Accounts payable and accrued expenses	$ 26,025	$ 27,626

9. CREDIT AGREEMENT, LONG-TERM DEBT AND CAPITAL LEASES

The Company's Credit Agreement, long-term debt and capital leases consisted of the following:

	June 30, 2010	September 30, 2009
	(In thousands)	
Long-term revolving lines of credit	$ 15,000	$ 15,000
Term loan facility	$ 44,813	$ 60,000
Less current portion	(750)	(750)

Long-term debt, less current portion	$	44,063	$	59,250
Total indebtedness under Credit Agreement	$	59,813	$	75,000

16

Credit Agreement. On April 27, 2007, the Company entered into a credit agreement with Comerica Bank, the Credit Agreement, to provide the Company a $150 million credit facility which replaced its previous credit facility in its entirety. On October 26, 2007, the Company amended the Credit Agreement, and transferred a portion of the revolving credit commitment to a fully funded term loan. The term loan is amortized at an annual amount of 1% per year, payable in equal quarterly installments beginning January 1, 2008, with the remaining amount due on the maturity date. The Company entered into a second amendment to the Credit Agreement on December 20, 2007. The second amendment (i) extended the hedging arrangement date related to a portion of the term loan to June 1, 2008; and (ii) modified the interest rate margin applicable to the Credit Agreement. On July 22, 2009, the Company entered into a third amendment to the Credit Agreement, which amended certain covenants, reduced the total borrowing capacity of the Credit Agreement to $125 million ($65 million under the revolving credit commitment and $60 million under the term loan) from the previous total borrowing capacity of $150 million, and agreed to a LIBOR floor of 2%.

On April 6, 2010, the Company entered into a fourth amendment to the Credit Agreement which (i) removed the requirement to maintain a minimum consolidated EBITDA (earnings before net interest expense, taxes, depreciation and amortization and accretion of contract rights); (ii) amended the consolidated total leverage ratio to a ratio of not greater than 1.50 to 1.00; (iii) reduced the total borrowing capacity of the Credit Agreement by reducing the revolving commitment of the credit facility from $65 million to $45 million and the term loan from $60 million to $45 million; and (iv) amended the definition of Consolidated EBITDA to include any extraordinary, unusual or non-cash non-recurring expenses or losses (including, whether or not otherwise includable as a separate item in the Consolidated Statement of Operations for such period, losses on sales of assets outside the ordinary course of business) of up to $10 million, commencing June 30, 2010. As a result of this amended definition of Consolidated EBITDA in the fourth amendment, commencing June 30, 2010, the Company modified its calculation of Adjusted EBITDA. Adjusted EBITDA is presented and reconciled to EBITDA and Net Income/Loss and Adjusted EBITDA continues to be the basis for which compliance with a number of covenants will be determined, including certain ratios. As of June 30, 2010, the calculation of Adjusted EBITDA is as follows:

Consolidated net income or loss
+ Interest expense
+ Depreciation and amortization expense
+ Non-cash expense related to stock compensation
+ Extraordinary, unusual or non-cash non-recurring expenses or losses (up to $10 million)
- Non-cash income items
- Extraordinary income or gains

There are no items included in the calculation of Adjusted EBITDA that were not previously agreed to as part of the amendments to the Credit Agreement.

The Company accounts for amendments or changes to its Credit Agreement in accordance with ASC 470-50-40-21, “Modifications and exchanges of line of credit or revolving debt arrangements.” Based on the requirements of ASC 470-50-40-21, the Company wrote-off $381,000 during the three month period ended June 30, 2010 related to unamortized deferred costs of the original Credit Agreement and subsequent amendments. The remaining deferred costs of approximately $1.0 million, in addition to the approximately $284,000 of costs related to the fourth amendment will be amortized over the remaining term of the Credit Agreement.

The Credit Agreement is collateralized by substantially all of the Company’s assets, and also contains financial covenants as defined in the agreement. As of June 30, 2010, the Company is in compliance with the loan covenants. The Credit Agreement requires certain mandatory prepayments be made on the term loan from the net cash proceeds of certain asset sales and condemnation proceedings (in each case to the extent not reinvested, within certain specified time periods, in the replacement or acquisition of property to be used in its businesses).

The Credit Agreement provides the Company with the ability to finance development agreements and acquisitions and working capital for general corporate purposes. Advances under the revolving credit commitment and the term loan mature on April 27, 2012, and bear interest at the Eurodollar rate plus the applicable spread, tied to various levels of interest pricing determined by total debt to EBITDA.

As of June 30, 2010, the $44.8 million on the term loan bore interest at 6.5% and the $15 million revolver bore interst at 5.25%. The Company has approximately $30 million available under the Credit Agreement, subject to covenant restrictions.

10. WRITE-OFF, RESERVE, IMPAIRMENT AND SETTLEMENT CHARGES

Write-off, reserve, impairment and settlement charges for the three and nine month periods ended June 30, 2010 and 2009 consisted of the following(in thousands):

	Three month period ended		Nine month period ended	
	June 30, 2010	June 30, 2009	June 30, 2010	June 30, 2009
Litigation and settlement costs	$-	$299	$-	$8,220
Reserve against note and accounts receivable (1)	-	-	2,912	397
Write-off of install costs and portable buildings in Alabama	-	-	332	-
Severance and related benefit costs	-	-	-	1,064
Write-off of prepaid loan fees	381	-	381	-
Write-off of property and equipment and intangibles	-	-	271	590
Total write-off, reserve, impairment and settlement charges	$381	$299	$3,896	$10,271

(1) See Note 6 of the Notes to Condensed Consolidated Financial Statements.

11. INCOME TAXES

Income tax benefit for the three and nine month periods ended June 30, 2010 were $2.6 million and $331,000, respectively. The benefit for the current period was primarily due to a change in method for calculating depreciation expense for tax purposes related to game licenses acquired from third party vendors and utilized in the Company's rental pool. The Company claimed a cumulative adjustment for the method change under Internal Revenue Service(IRS) guidelines and will prospectively utilize the new method for future game license purchases. The adjustment will be realized by the Company through a carryback to prior taxable income years. In addition, the Company recorded a benefit for a research and development credit study performed during the current period in the amount of $474,000. As of June 30, 2010, the Company has fully reserved for all of its deferred tax assets as management has determined that it is more likely than not that the Company will not be able to realize the benefit of those assets. Income tax benefits were recorded during the three and nine month periods ended June 30, 2009 of $288,000 and $5.4 million commensurate with the net loss reported in those respective periods.

12. INCOME (LOSS) PER COMMON SHARE

Income (loss) per common share is computed in accordance with ASC Topic 260, "Earnings per Share." Presented below is a reconciliation of net income (loss) available to common shareholders and the differences between weighted average common shares outstanding, which are used in computing basic earnings (loss) per share, and weighted average common and potential shares outstanding, which are used in computing diluted earnings (loss) per share. Diluted amounts are not included in the computation of diluted loss per share, as such amounts would be antidilutive.

	Three months ended June 30,		Nine months ended June 30,	
	2010	2009	2010	2009
Net income (loss) available to common shareholders (in thousands)	$ 360	$ (1,160)	$ (9,366)	$ (10,478)
Weighted average common shares outstanding	27,436,616	26,693,006	27,339,511	26,653,093
Effect of dilutive securities:				
Options	525,058	-	-	-
Weighted average common and potential shares outstanding	27,961,674	26,693,006	27,339,511	26,653,093
Basic earnings (loss) per share	$ 0.01	$ (0.04)	$ (0.34)	$ (0.39)
Diluted earnings (loss) per share	$ 0.01	$ (0.04)	$ (0.34)	$ (0.39)

The Company had the following options to purchase shares of common stock that were not included in the weighted average common and potential shares outstanding in the computation of dilutive earnings per share, due to the antidilutive effects:

	Three months ended June 30,		Nine months ended June 30,	
	2010	2009	2010	2009
Common Stock Options	3,857,108	7,071,583	6,374,719	6,989,626
Range of exercise price	$ 3.58-18.71	$ 1.00-18.71	$ 3.58-$18.71	$ 1.00-$21.53

In the three and nine month periods ended June 30, 2010, options to purchase approximately 3.9 million and 4.2 million shares of common stock, with exercise prices ranging from $3.58 to $18.71 per share respectively, were not included in the computation of dilutive loss per share, due to the antidilutive effect. In addition, for the nine month period ended June 30, 2010 approximately 2.2 million equivalent shares were not included, due to the loss generated in the period.

13. COMMITMENTS AND CONTINGENCIES

Litigation and Regulatory Proceedings

The Company is subject to the possibility of loss contingencies arising in its business and such contingencies are accounted for in accordance with ASC Topic 450, “Contingencies.” In determining loss contingencies, the Company considers the possibility of a loss as well as the ability to reasonably estimate the amount of such loss or liability. An estimated loss is recorded when it is considered probable that a liability has been incurred and when the amount of loss can be reasonably estimated.

In addition to the threat of litigation relating to the Class II or Class III status of the Company’s games and equipment, the Company is the subject of various pending and threatened claims arising out of the ordinary course of business. The Company believes that any liability resulting from these various other claims will not have a material adverse effect on its results of operations or financial condition or cash flows. During its ordinary course of business, the Company enters into obligations to defend, indemnify and/or hold harmless various customers, officers, directors, employees and other third parties. These contractual obligations could give rise additional litigation cost and involvement in court proceedings.

International Gamco. International Gamco, Inc., or Gamco, claiming certain rights in U.S. Patent No. 5,324,035, or the ‘035 Patent, brought suit against the Company on May 25, 2004 in the U.S. District Court for the Southern District of California alleging that the Company’s central determinant system, as operated by the New York State Lottery, infringes the ‘035 Patent. Gamco claims to have acquired ownership of the ‘035 Patent from Oasis Technologies, Inc., or Oasis, a previous owner of the ‘035 Patent. In February 2003, Gamco assigned the ‘035 Patent to International Game Technology, or IGT. Gamco claims to have received a license back from IGT for the New York State Lottery. The lawsuit claims that the Company infringed the ‘035 Patent after the date on which Gamco assigned the ‘035 Patent to IGT.

We have made a number of challenges to Gamco's standing to sue for infringement of the '035 Patent. On October 15, 2007, pursuant to an interlocutory appeal, the federal circuit court reversed the district court's order when it held that Gamco did not have sufficient rights in the '035 Patent to sue us without the involvement of the patent owner, IGT.

On December 4, 2007, Gamco and IGT entered into an Amended and Restated Exclusive License Agreement whereby IGT granted to Gamco exclusive rights to the '035 Patent in the state of New York and the right to sue for past infringement of the same. On January 9, 2008, Gamco filed its third amended complaint for infringement of the '035 Patent against us. On January 28, 2008, we filed an answer to the complaint denying liability. We also filed a third amended counterclaim against Oasis, Gamco and certain officers of Gamco, for fraud, promise without intent to perform, negligent misrepresentation, breach of contract, specific performance and reformation of contract with regard to the Company's rights under the Sublicense Agreement for the '035 Patent, as well as for non-infringement and invalidity of the '035 Patent. These parties filed a motion to dismiss and a motion for summary judgment as to these claims. On August 11, 2009, the Court issued an order denying the motion to dismiss and granting in part and denying in part the motion for summary judgment. The Court entered judgment against the Company on its claims for fraud, promise without intent to perform and negligent misrepresentation. However, the Court held that Gamco was not entitled to judgment as a matter of law on our claims for breach of contract, reformation and specific performance. Our affirmative motion for partial summary judgment was denied.

The court issued a claim construction ruling in this case on April 20, 2009.   On August 28, 2009, the court held a telephonic conference, issued pre-trial deadlines and set the Final Pre-Trial Conference date for September 9, 2010.

On February 23, 2010, we filed a motion for summary judgment of non-infringement of the '035 Patent and a motion for summary judgment challenging the validity of the '035 Patent under 35 U.S.C. § § 102 and 103. The Court heard oral argument on both motions on July 22, 2010, and the matters were taken under submission. A trial date will be scheduled during the Final Pre-Trial Conference on September 9, 2010.

We continue to vigorously defend this matter. Given the inherent uncertainties in this litigation, we are unable to make any prediction as to the ultimate outcome.

Alabama Litigation. The Company, along with other major manufacturers, recently was named in three lawsuits, as further described below, all pending in federal court in Alabama. The lawsuits were filed on behalf of patrons of either White Hall Gaming Center in Lowndes County, Alabama or VictoryLand in Shorter, Alabama, and include several claims related to the alleged illegality of electronic bingo in Alabama. The Company has filed motions to dismiss the complaints for, among other things, failure to state a claim upon which relief could be granted.

Ethel Adell, et al., v. Macon County Greyhound Park, Inc., et al., a civil action, was filed on February 16, 2010 in the United States District Court for the Middle District of Alabama Eastern Division, on behalf of over 800 plaintiffs against the Company, Macon County Greyhound Park, Inc. (VictoryLand), as a corporation, International Gaming Technologies, Inc., Cadillac Jack, Inc., Colossus, Inc., Rocket Gaming Systems, LLC, Nova Gaming, LLC, and Bally Gaming, Inc. The plaintiffs, who were patrons of VictoryLand, are seeking actual damages, compensatory damages, treble damages and/or punitive damages based on Ala. Code, Sec 8-1-150(A), the Alabama Deceptive Trade Practices Act, and the Racketeer Influenced and Corruption Organizations Act 18 U.S.C. sec 1961(1).

On April 28, 2010, the Company filed a motion to dismiss the entire complaint pursuant to Rules 12(b)(2), (5) and (6) of the Federal Rules of Civil Procedure based, in part, on the grounds that the plaintiffs failed to state a claim against the Company upon which relief could be granted. All briefing on the motion has been completed. The court is expected to rule on the motion in the near future.

We continue to vigorously defend this matter. Given the inherent uncertainties in this litigation, we are unable to make any prediction as to the ultimate outcome.

Walter Bussey, et al., v. Macon County Greyhound Park, Inc., et al., a civil action, was filed on March 8, 2010 in the United States District Court for the Middle District of Alabama Eastern Division against the Company, Macon County Greyhound Park, Inc. (VictoryLand), as a corporation, International Gaming Technologies, Inc., Cadillac Jack, Inc., Colossus, Inc., Rocket Gaming Systems, LLC, Nova Gaming, LLC, and Bally Gaming, Inc. The plaintiffs, who were patrons of VictoryLand, originally sought actual damages, compensatory damages, treble damages and/or punitive damages based on both Ala. Code, Sec 8-1-150(A), and the Racketeer Influenced and Corruption Organizations Act ("RICO"), 18 U.S.C. sec 1961(1) and claim, in part, that the defendants conspired to promote gambling and/or to advance or profit from gambling activity in violation of Ala. Code Sec. 13 A-12-23 and have requested that the court certify the action as a Class Action as required under the Federal Rules of Civil Procedure.

On April 28, 2010, the Company filed a motion to dismiss the entire complaint pursuant to Rules 12(b)(2), (5) and (6) of the Federal Rules of Civil Procedure based, in part, on the grounds that the plaintiffs failed to state a claim against the Company upon which relief could be granted. After the Company filed its motion to dismiss, Plaintiffs voluntarily dismissed their RICO claim, leaving only a claim for recovery of gambling losses under Ala. Code Sec. 8-1-150(A). All briefing on the Company's motion has been completed. The court is expected to rule on the motion in the near future.

We continue to vigorously defend this matter. Given the inherent uncertainties in this litigation, we are unable to make any prediction as to the ultimate outcome.

Ozetta Hardy v. Whitehall Gaming Center, LLC, et al., a civil action, was filed against White Hall Gaming Center, LLC, Cornerstone Community Outreach, Inc., and Freedom Trail Ventures, Ltd., in the Circuit Court of Lowndes County, Alabama. On June 3, 2010, Plaintiffs filed an amended complaint adding the Company, IGT, Bally, Inc., Eclipse Gaming Systems, LLC, Video Gaming Technologies, Inc., Cadillac Jack, Inc., and AGS, LLC. The plaintiffs, who were patrons of White Hall, seek recovery of gambling losses based on Ala. Code, Sec 8-1-150(A) and have requested that the court certify the action as a Class Action as required under the Federal Rules of Civil Procedure.

On July 2, 2010, the defendants removed the case to the United States District Court for the Middle District of Alabama Northern Division. On July 9, 2010, the Company filed a motion to dismiss the complaint pursuant to Rules 12(b)(2), (5) and (6) of the Federal Rules of Civil Procedure based, in part, on the grounds that the plaintiffs failed to state a claim against the Company upon which relief could be granted. Plaintiffs have until August 13, 2010, to respond to the motion.

We continue to vigorously defend this matter. Given the inherent uncertainties in this litigation, we are unable to make any prediction as to the ultimate outcome.

Alabama Regulatory Environment. On November 13, 2009, the Supreme Court of Alabama, in a 6-3 decision, reversed and remanded a trial court’s preliminary injunction in favor of a charity operating bingo in the Town of White Hall, Lowndes County, Alabama, referred to herein as the White Hall decision. The appeal arose out of a raid conducted by the Governor’s Task Force on Illegal Gambling on March 19, 2009. The Governor’s Task Force on Illegal Gambling seized server-based bingo gaming systems, computers, servers, and cash. Included with the equipment seized were approximately 34 of the Company’s games and certain of the Company’s charity bingo equipment located in Alabama. The Governor’s Task Force on Illegal Gambling also filed a forfeiture action against all of the equipment seized at White Hall. The forfeiture action remains pending in the trial court. The Supreme Court of Alabama denied an application for rehearing filed by the charity that operates White Hall.

In the White Hall decision, the Supreme Court of Alabama established a definition of “bingo” that included a set of standards that apply to the operation of charity bingo in Alabama. We believe that our modified games comply with the standards established by the recent Supreme Court decision and have received certifications and/or formal written opinions from independent gaming laboratories verifying to us that each game, as modified, is compliant with the applicable Alabama standards.

Notwithstanding our initiatives to have our games comply with the specified standards, there can be no assurance that we will not encounter further legal, regulatory, financial, or competitive issues related to this matter as the legality of charitable bingo gaming in Alabama continues to be challenged by the state’s Governor. Legislation to put the legality question to a public referendum in Alabama failed to pass the recently concluded legislative session. As a result, many charitable bingo properties have voluntarily ceased operations pending resolution of the matter.

Three of the four facilities in Alabama which have historically placed our charitable bingo units, as well as other game manufacturers’ units, have ceased operations. We voluntarily removed our charitable bingo units from one of the facilities before it ceased operations. One of the Alabama facilities where the Company has historically placed units has been operating under the protection of a temporary restraining order. On July 30, 2010, however, the Supreme Court of Alabama issued a ruling reversing the trial court’s entry of the temporary restraining order.

As of June 30, 2010, the net book value of charitable bingo machines held by the Company in Alabama totaled $4.8 million.

14. SUBSEQUENT EVENTS

The Company has evaluated subsequent events through the date the financial statements were issued, and determined that no events, other than those disclosed within the footnotes hereto, have occurred subsequent to June 30, 2010 that warrant additional disclosure or accounting considerations.

--

ITEM 2. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

FUTURE EXPECTATIONS AND FORWARD-LOOKING STATEMENTS

This Quarterly Report and the information incorporated herein by reference contain various "forward-looking statements" within the meaning of federal and state securities laws, including those identified or predicated by the words "believes," "anticipates," "expects," "plans," "will," or similar expressions with forward-looking connotations. Such statements are subject to a number of risks and uncertainties that could cause the actual results to differ materially from those projected. Such factors include, but are not limited to, the uncertainties inherent in the outcome of any litigation of the type described in this Quarterly Report under "PART II – Item 1. Legal Proceedings," trends and other expectations described in "PART I – Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations," risk factors disclosed in our earnings and other press releases issued to the public from time to time, as well as those other factors as described under "PART II – Item 1A. Risk Factors" set forth below. Given these uncertainties, readers of this Quarterly Report are cautioned not to place undue reliance upon such statements. All forward-looking statements in this document are based on information available to us as of the date hereof, and we assume no obligations to update any such forward-looking statements.

Overview

Multimedia Games, Inc. designs, manufactures and supplies innovative standalone and networked gaming systems. Our products and systems are used by Native American tribes and commercial casino operators as well as state lottery operators in North America, and our electronic bingo and lottery systems are deployed in certain international markets. We have long been a provider of server-based gaming systems known as central determinant and downloadable systems. These systems are used by our Native American gaming operator customers in both Class II and Class III, as defined below, settings, by our commercial casino customers, by operators of charity and commercial bingo gaming facilities, and by lottery jurisdictions for operation of their video lottery systems.

As part of our networked gaming systems, we also provide customers with access to proprietary local-area and wide-area telecommunications networks that allow us to link player terminals with one another inside a single casino, inside an operator's multiple casinos and across many casinos nationwide. Our games include a mix of proprietary content that has been designed and developed internally by our own game studios as well as themes that we license from third parties. Behind our products and systems is a suite of back-office, player tracking, slot accounting, slot management and slot monitoring systems that enable our customers to track their operations and adjust the performance of their slot floor in real-time to ensure optimum financial performance.

We derive the majority of our gaming revenues from participation, or revenue share, agreements. Under our participation agreements, we place third party player terminals and systems, as well as our proprietary and other licensed game content, at a customer's facility in return for a share of the revenues that these terminals and systems generate. As of June 30, 2010, we have 13,782 gaming units in operation domestically and internationally which are installed pursuant to revenue share arrangements. The Company has undertaken a concerted effort to generate additional revenue through the sale of Class II and Class III gaming systems and products and we also generate revenues from the sale of gaming units and systems as we continue to expand into additional gaming jurisdictions and into other segments of the gaming market. We also generate revenues from our provision of the central determinant system for approximately 12,500 video lottery terminals installed at racetracks in the State of New York and operated by the New York State Division of the Lottery.

RESULTS OF OPERATIONS

Three and Nine Month Periods Ended June 30, 2010 Compared to Three and Nine Month Periods Ended June 30, 2009

Below are our revenues and costs and expenses for the periods noted above. This information should be read in conjunction with our Condensed Consolidated Financial Statements and notes thereto. (in thousands)

	Three month periods ended June 30,			Nine month periods ended June 30,		
	2010	2009	% change	2010	2009	% change
Revenue						
Gaming Operations						
Participation revenue	$ 21,784	$ 25,395	(14.2)%	$ 63,962	$ 77,167	(17.1)%
Lottery	2,026	2,012	0.7 %	5,686	5,469	3.9 %
Gaming Equipment and Systems Sales						
Player terminal and equipment sales	3,818	2,624	45.5 %	13,000	8,649	50.3 %
Systems and Licensing	1,117	1,162	3.9 %	3,354	1,258	166.6 %
Other Revenue	331	936	(64.7)%	1,477	2,032	(27.4)%
Total Revenue	29,076	32,129	(9.5)%	87,479	94,575	(7.5)%
Costs and Expenses						
Cost of revenues	3,302	2,137	54.5 %	9,139	6,311	44.8 %
Selling, general and administrative	14,703	15,326	(4.1)%	43,493	46,091	(5.6)%
Write-offs, reserves, impairment and settlement charges	381	299	27.4 %	3,896	10,271	(62.1)%
Depreciation and amortization	12,760	15,581	(18.1)%	39,984	46,085	(13.2)%
Other expense, net	(182)	(234)	22.64 %	(664)	(1,650)	59.8 %

	At June 30, 2010	2009	% change
End-of-period installed player terminal base:			
Oklahoma	7,041	7,553	(6.8)%
Mexico	5,093	5,727	(11.1)%
Alabama(1)	559	2,280	(75.5)%
Other	1,089	1,641	(33.6)%
Total participation units	13,782	17,201	(19.9)%

(1) See Note 13 of the Notes to Condensed Consolidated Financial Statements. Some of the facilities of the Company's Alabama customers are currently closed, and if the facilities of the Company's Alabama customers continue to remain closed, or if additional facilities close, the resulting decrease in our revenue and EBITDA for the 2010 fiscal year, as well as additional write-down of assets currently dedicated to the Alabama market, may adversely impact our financial position and results of operations.

Three Months Ended June 30, 2010, Compared to Three Months Ended June 30, 2009

Total revenues for the three months ended June 30, 2010, were $29.1 million, compared to $32.1 million for the three months ended June 30, 2009, a $3.0 million or 9.5% decrease.

Gaming Operations – Participation revenue

§ Oklahoma gaming revenues were $15.8 million in the three months ended June 30, 2010, compared to $17.6 million in the three months ended June 30, 2009, a decrease of $1.8 million, or 10.0%. Oklahoma's end of period unit count as of June 30, 2010 was 7,041 compared to 7,553 as of June 30, 2009, a 512 unit or 6.8% decrease. This unit reduction was primarily caused by casinos that purchased or removed 239 units from their floor. To a lessor extent the revenue decrease can also be attributed to the continuing economic slowdown in the Oklahoma market.

§ Revenues from the Mexico bingo market were $2.1 million in the three months ended June 30, 2010 and $2.4 million during the same period of 2009, a decrease of $314,000 or 13.2%. As of June 30, 2010, we had installed 5,093 player terminals at 29 bingo parlors in Mexico compared to 5,727 terminals installed at 28 bingo parlors at June 30, 2009. The reduction in the number of units relates to our strategic initiative to reduce our overall footprint in the facilities of our largest customer in Mexico and the beginning of a transition in the Mexico market from a Class II product to a Class III product. In addition, the decrease in revenue relates to a reduction in the win per unit in Mexico caused by an increase in competition into the major Mexican markets and can also be attributable to a national smoking policy change that has affected traffic into our customers' locations since the first quarter of Fiscal 2010.

§ Alabama gaming revenues decreased $1.0 million, or 46.5%, to $1.1 million for the three months ended June 30, 2010, compared to $2.1 million for the three months ended June 30, 2009. The decrease in revenue relates to the previously disclosed matter that the Company no longer has units in operation at three of the four facilities in Alabama where the Company has historically placed its charitable bingo units. The fourth facility where the Company has historically placed units has been operating under the protection of a temporary restraining order. On July 30, 2010, however, the Supreme Court of Alabama issued a ruling reversing the trial court's entry of the temporary restraining order. Accordingly, this fourth facility will no longer be operating under the protection of a temporary restraining order. See Note 13 of the Notes to Condensed Consolidated Financial Statements.

§ Other gaming operations revenue relates to participation revenue from other states, including Washington, Wisconsin, Texas, New York, Minnesota, California and Rhode Island. Gaming revenue from these states combined was $2.8 million in the three months ended June 30, 2010 compared to $2.9 million during the same period of 2009, a 2.8%, decrease. The end of period unit count for these states decreased to 1,089 as of June 30, 2010 from 1,641 as of June 30, 2009. Other gaming operations revenue includes back office fees for system installations of $1.3 million and $838,000 for the three months ended June 30, 2010 and 2009, respectively.

Gaming Operations – Lottery

§ Revenues from the New York Lottery system increased $13,000, or 1.0%, to $2.0 million in the three months ended June 30, 2010, from $2.0 million in the three months ended June 30, 2009. Currently, eight of the nine planned racetrack casinos are operating, with approximately 12,500 total terminals. The increase is attributable to increased activity within the New York Lottery system.

Gaming Equipment and System Sales –Player Terminal and Equipment Sales

§ Player terminal and equipment sales were $3.8 million for the three months ended June 30, 2010, and $2.6 million for the three months ended June 30, 2009, an increase of $1.2 million or 45.5%. Player terminal sales for the three months ended June 30, 2010 were $2.0 million on the sale of 128 new proprietary units, with no comparible sales for the three month period ended June 30, 2009. Gaming equipment sales were $1.3 for the three month period ended June 30, 2010 compared to $283,000 in the June 30, 2009 period. Generally, gaming equipment sales include ancillary equipment necessary for the full functionality of the player terminals in a casino. Player terminal and equipment sales also include $288,000 and $2.3 million related to deferred revenue recognized during the three month periods ended June 30, 2010 and 2009, respectively, due to contract amendments or final execution of deliverables.

Gaming Equipment and System Sales – Systems and Licensing

- § Systems and licensing sales revenue was $1.1 million for the three months ended June 30, 2010, and $1.2 million for the three months ended June 30, 2009. Systems and licensing revenue for the three months ended June 30, 2010 relates to $163,000 of licenses associated with the player terminal sales during the period and $880,000 of systems and game themes sold in prior periods being amortized to revenue from deferred revenue over the contract period. Systems and licensing revenue for the three months ended June 30, 2009 relates to $350,000 of licenses associated with game changes, and $812,000 of systems and game themes sold in prior periods being amortized to revenue from deferred revenue over the contract period.

Cost of Revenues

- § Total cost of revenues, which includes cost of gaming equipment and system sales and royalty fees, increased $1.2 million, or 54.5%, to $3.3 million in the three months ended June 30, 2010, from $2.1 million in the three months ended June 30, 2009. Costs of sales related to player terminal sales were $938,000 for the three months periods ended June 30, 2010, Royalty fees were $765,000 and $549,000 for the same periods. Cost of sales for the three months ended June 30, 2010 also includes $935,000 of costs of prior period shipments being amortized from deferred revenue over the contract period and $425,000 related to the sale of gaming equipment during the period. Cost of sales for the three months ended June 30, 2009 also includes $1.5 million of costs of prior period shipments being amortized from deferred revenue over the contract period, and $333,000 related to the sale of gaming equipment during the period.

Selling, General and Administrative Expenses

- § Selling, general and administrative expenses, or SG&A, decreased approximately $623,000, or 4.1%, to $14.7 million for the three months ended June 30, 2010, from $15.3 million in the same period of 2009. This decrease was primarily a result of (i) a decrease in repair and maintenance of leased gaming equipment of $422,000, (ii) decrease in bad debt of $523,000, (iii) other taxes and license fees of $328,000 offset by an increase of $684,000 to salaries and wages.

Write-off, reserve, impairment and settlement charges

- § Write-off, reserve, impairment and settlement charges for the three month period ended June 30, 2010 were $381,000 compared to $299,000 for three month period ended June 30, 2009. The charges in the current period consisted of approximately $381,000 of write offs for loan costs from the amendment of our credit facility.

- § On May 1, 2009, the Company entered into a comprehensive settlement agreement to resolve all claims arising from a November 2004 lawsuit. The Company incurred charges of $299,000 for the three month period ended June 30, 2009 related to legal fees and settlement costs, net of insurance proceeds.

Amortization and Depreciation

- § Amortization expense decreased $117,000, or 11.0%, to $948,000 for the three months ended June 30, 2010, compared to $1.1 million for the same period of 2009. Depreciation expense decreased $2.7 million, or 18.6%, to $11.8 million for the three months ended June 30, 2010 from $14.5 million for the three month period ended June 30, 2009, primarily as a result of a reduction in capital expenditures and assets becoming fully depreciated.

Other Income and Expense

§ Interest income decreased $326,000, or 28.2%, to $830,000 for the three months ended June 30, 2010, from $1.2 million in the same period of 2009. We entered into development agreements with a customer under which approximately $41.7 million has been advanced and is outstanding at June 30, 2010, and for which we impute interest on these interest-free loans. For the three months ended June 30, 2010, we recorded imputed interest of $778,000 relating to development agreements with an imputed interest rate range of 5.75% to 9.0%, compared to $1.0 million for the same period in 2009. In addition, interest income of $52,000 was accrued during the three month period ended June 30, 2010 on interest bearing notes.

§ Interest expense decreased $378,000, or 27.2%, to $1.0 million for the three months ended June 30, 2010, from $1.4 million in the same period of 2009 due to a reduction in the outstanding debt balance.

Income Taxes

§ Income tax benefit increased by $2.3 million to $2.6 million for the three months ended June 30, 2010, from an income tax benefit of $288,000 in the same period of 2009. These figures represent effective income tax rates of 116.0% and 19.9% for the three months ended June 30, 2010 and 2009, respectively. During the three month period ended June 30, 2010, we recorded benefit of $3.7 million due to a change in method for calculating depreciation expense for tax purposes related to game licenses acquired from third party vendors and utilized in our rental pool. The Company claimed a cumulative adjustment for the method change under IRS guidelines and will prospectively utilize the new method for future game license purchases. The adjustment will be realized by the Company through a carryback to prior taxable income years. In addition, we recorded a benefit for a research and development credit study performed during the current period in the amount of $474,000. These amounts were offset by a valuation allowance against our remaining deferred tax assets in the amount of $1.6 million. As of June 30, 2010, the Company has fully reserved for all of its deferred tax assets as management has determined that it is more likely than not that the Company will not be able to realize the benefit of those assets.

Nine Months Ended June 30, 2010, Compared to Nine Months Ended June 30, 2009

Total revenues for the nine months ended June 30, 2010, were $87.5 million, compared to $94.6 million for the nine months ended June 30, 2009, a $7.1 million or 7.5% decrease.

Gaming Operations – Participation revenue

§ Oklahoma gaming revenues were $45.3 million in the nine months ended June 30, 2010, compared to $52.4 million in the nine months ended June 30, 2009, a decrease of $7.1 million or 13.5%. Oklahoma's end of period unit count as of June 30, 2010 was 7,041 compared to 7,553 as of March 31, 2009, a 512 unit or 6.8% decrease. This unit reduction was primarily caused by casinos that purchased or removed 599 units from their floor. To a lessor extent the revenue decrease can also be attributed to the continuing economic slowdown in the Oklahoma market.

§ Revenues from the Mexico bingo market were $6.5 million in the nine months ended June 30, 2010 and $7.4 million during the same period of 2009, a decrease of $912,000 or 12.2%. As of June 30, 2010, we had installed 5,093 player terminals at 29 bingo parlors in Mexico compared to 5,727 terminals installed at 28 bingo parlors at June 30, 2009. The reduction in the number of units relates to our strategic initiative to reduce our overall footprint in the facilities of our largest customer and the beginning of a transition in the Mexico market from a Class II product to a Class III product. In addition, the decrease in revenue relates to a reduction in the win per unit in Mexico caused by an increased supply into the major Mexican markets and can also be attributable to a national smoking policy change that has affected traffic into our customers' locations during the period.

§ Alabama gaming revenues decreased $3.4 million, or 45.8%, to $4.0 million for the nine months ended June 30, 2010, compared to $7.3 million for the nine months ended June 30, 2009. The decrease in revenue relates to the previously disclosed fact that the Company no longer has units in operation at three of the four facilities in Alabama where the Company has historically placed its charitable bingo units. The fourth facility where the Company has historically placed units has been operating under the protection of a temporary restraining order. On July 30, 2010, however, the Supreme Court of Alabama issued a ruling reversing the trial court's entry of the temporary restraining order. Accordingly, this fourth facility will no longer be operating under the protection of a temporary restraining order. See Note 13 of the Notes to Condensed Consolidated Financial Statements.

§ Other gaming operations revenue relates to participation revenue from other states, including Washington, Wisconsin, Texas, New York, Minnesota, California and Rhode Island. Gaming revenue from these states combined was $8.2 million in the nine months ended June 30, 2010 compared to $9.9 million during the same

period of 2009 a $1.7 million, or 17.3%, decrease. The end of period unit count for these states decreased to 1,089 as of June 30, 2010 from 1,641 as of June 30, 2009. Other gaming operations revenue includes back office fees for system installations of $3.2 million and $2.4 million for the nine months ended June 30, 2010 and 2009, respectively.

Gaming Operations – Lottery

§ Revenues from the New York Lottery system increased $218,000, or 4.0%, to $5.7 million in the nine months ended June 30, 2010, from $5.5 million in the six months ended June 30, 2009. Currently, eight of the nine planned racetrack casinos are operating, with approximately 12,500 total terminals. The increase is attributable to increased activity within the New York Lottery system.

Gaming Equipment and System Sales –Player Terminal and Equipment Sales

§ Player terminal and equipment sales were $13.0 million for the nine months ended June 30, 2010, and $8.6 million for the nine months ended June 30, 2009, an increase of $4.4 million or 50.3%. Player terminal sales for the nine months ended June 30, 2010 were $8.7 million on sales of 621 new proprietary units, compared to $4.4 million on sales of third party units for the nine month period ended June 30, 2009. Gaming equipment sales were $2.9 million and $1.9 million for the nine month periods ended June 30, 2010 and 2009, respectively. Generally, gaming equipment sales include ancillary equipment necessary for the full functionality of the player terminals in a casino; however, in nine months ended June 30, 2010 and 2009 gaming equipment sales also included $344,000 and $160,000 of used equipment sales, respectively. Player terminal and equipment sales also include $1.1 million and $2.3 million related to deferred revenue recognized during the nine months period ended June 30, 2010 and 2009, respectively, due to contract amendments or final execution of deliverables.

Gaming Equipment and System Sales – Systems and Licensing

§ Systems and licensing sales revenue was $3.4 million for the nine months ended June 30, 2010, and $1.3 million for the nine months ended June 30, 2009. Systems and licensing revenue for the nine months ended June 30, 2010 relates to: (i) a system sale of $1.0 million; (ii) $724,000 of licenses associated with the player terminal sales during the period; (iii) $1.3 million of systems and game themes sold in prior periods being amortized to revenue from deferred revenue over the contract period. Systems and licensing revenue for the nine months ended June 30, 2009 relates to: (i) $812,000 of systems and game themes sold in prior periods being amortized to revenue from deferred revenue over the contract period; (ii) $250,000 from the sale of third party units; and (iii) $115,000 from game changes.

Cost of Revenues

§ Total cost of revenues, which includes cost of gaming equipment and system sales and royalty fees, increased $2.8 million, to $9.1 million in the nine months ended June 30, 2010, from $6.3 million in the nine months ended June 30, 2009. Costs of sales related to player terminal sales were $4.8 million and $2.2 million for the nine months periods ended June 30, 2010 and 2009, respectively, and royalty fees were $1.6 million and $1.6 million for the same periods. Cost of sales for the nine months ended June 30, 2010 also includes $1.4 million of costs from deferred revenue related to prior period shipments recognized during the period, and $937,000 related to the sale of gaming equipment during the period. Cost of sales for the nine months ended June 30, 2009 also includes: (i) $1.5 million of costs from deferred revenue related to prior period shipments recognized during the period; (ii) $2.2 million from the sale of third part units; and (iii) $1.1 million related to the sale of gaming equipment during the period.

Selling, General and Administrative Expenses

§ Selling, general and administrative expenses, or SG&A, decreased approximately $2.6 million, or 5.6.%, to $43.5 million for the nine months ended June 30, 2010, from $46.1 million in the same period of 2009. This decrease was primarily a result of (i) a decrease in repairs and maintenance expenses of $1.8 million, (ii) decrease in consulting and contract labor of $764,000 and (iii) decrease in accounting fees of $575,000.

Write-off, reserve, impairment and settlement charges

§ Write-off, reserve, impairment and settlement charges for the nine month period ended June 30, 2010 were $3.9 million compared to $10.3 million for nine month period ended June 30, 2009. The charges in the current period consisted of approximately $381,000 of write offs for loan costs from the amendment of our credit facility along

with charges of approximately $3.1 million of reserves and impairment charges for a note receivable and installation and other costs within the state of Alabama. In addition to the charges related to the Alabama market, during the nine month period ended June 30, 2010 as part of the Company's routine asset analysis, charges of $421,000 were incurred, including the write-off of facility install costs, components, licenses, capitalized software and reserves for bad debts.

§ On May 1, 2009, the Company entered into a comprehensive settlement agreement to resolve all claims arising from a November 2004 lawsuit. The Company incurred charges of $8.2 million nine month period ended June 30, 2009 related to legal fees and settlement costs, net of insurance proceeds. In addition, during the three and nine month period ended June 30, 2009 as part of the Company's routine asset analysis, charges of $987,000 were incurred, including the write-off of facility install costs, components, licenses, patents, capitalized software and reserves for bad debts; and $1.1 million for severance and other benefits.

Amortization and Depreciation

§ Amortization expense decreased $1.2 million, or 32.1%, to $2.6 million for the nine months ended June 30, 2010, compared to $3.8 million for the same period of 2009. Depreciation expense decreased $4.9 million, or 11.6%, to $37.4 million for the six months ended June 30, 2010 from $42.3 million for the nine month period ended June 30, 2009, primarily as a result of a reduction in capital expenditures and assets becoming fully depreciated.

Other Income and Expense

§ Interest income decreased $894,000, or 24.2%, to $2.8 million for the nine months ended June 30, 2010, from $3.7 million in the same period of 2009. We entered into development agreements with a customer under which approximately $41.7 million has been advanced without interest and is outstanding at June 30, 2010, and for which we impute interest on these interest-free loans. For the nine months ended June 30, 2010, we recorded imputed interest of $2.5 million relating to development agreements with an imputed interest rate range of 5.75% to 9.0%, compared to $3.3 million for the same period in 2009. In addition, interest income of $270,000 was accrued during the nine month period ended June 30, 2010 on interest bearing notes.

§ Interest expense decreased $1.9 million, or 36.1%, to $3.5 million for the nine months ended June 30, 2010, from $5.4 million in the same period of 2009 due to a reduction in the outstanding debt balance.

§ We had no other income for the nine months ended June 30, 2010, compared to $74,000 in the same period of 2009. Other income primarily decreased due to the last distribution from a partnership interest.

Income Taxes

§ Income tax benefit decreased by $5.0 million to $331,000 for the nine months ended June 30, 2010, from an income tax benefit of $5.4 million in the same period of 2009. These figures represent effective income tax rates of 3.4% and 33.8% for the nine months ended June 30, 2010 and 2009, respectively. During the nine month period ended June 30, 2010, we recorded a valuation allowance against our remaining deferred tax assets in the amount of $4.1 million. The full valuation allowance on our deferred tax assets is the result of changes in our forecast, based on events described above, for the remainder of the 2010 fiscal year and the determination that it is more likely than not that we will not be able to realize the benefit of those assets.

RECENT ACCOUNTING PRONOUNCEMENTS

We monitor new, generally accepted accounting principles and disclosure reporting requirements issued by the Securities and Exchange Commission, or SEC, and other standard setting agencies. Recently issued accounting standards affecting our financial results are described in Note 1 of our unaudited condensed consolidated financial statements.

CRITICAL ACCOUNTING POLICIES AND ESTIMATES

We prepare our consolidated financial statements in conformity with accounting principles generally accepted in the United States. As such, we are required to make certain estimates, judgments and assumptions that we believe are reasonable based on the information available. These estimates and assumptions affect the reported amounts of assets and liabilities at the date of the financial statements, and the reported amounts of revenues and expenses during the periods presented. There can be no assurance that actual results will not differ from those estimates. We believe the following represent our most critical accounting policies.

Management considers an accounting estimate to be critical if:

- § It requires assumptions to be made that were uncertain at the time the estimate was made (Critical Assumption #1), and

- § Changes in the estimate or different estimates that could have been selected could have a material impact on our consolidated results of operation or financial condition (Critical Assumption #2).

Revenue Recognition. As further discussed in the discussion of our Revenue Recognition policy in Note 1 of our condensed consolidated financial statements, revenue from the sale of software is accounted for under ASC Topic 985, “Software”. If Vendor-Specific Objective Evidence, or VSOE, of fair value does not exist, the revenue is deferred until such time that all elements have been delivered or services have been performed. If any element is determined to be essential to the function of the other, revenues are generally recognized over the term of the services that are rendered. In those limited situations where VSOE does not exist for any undelivered elements of a multiple element arrangement, then the aggregate value of the arrangement, including the value of products and services delivered or performed, is initially deferred until all hardware and software is delivered, and then is recognized ratably over the period of the last deliverable, generally the service period of the contract. Depending upon the elements and the terms of the arrangement, we recognize certain revenues under the residual method. Under the residual method, revenue is recognized when VSOE of fair value exists for all of the undelivered elements in the arrangement, but does not exist for one or more of the delivered elements in the arrangement. Under the residual method, we defer the fair value of undelivered elements, and the remainder of the arrangement fee is then allocated to the delivered elements and is recognized as revenue, assuming the other revenue recognition criteria are met.

Assumptions/Approach Used: The determination whether all elements of sale have VSOE is a subjective measure, where we have made determinations about our ability to price certain aspects of transactions.

Effect if Different Assumptions Used: When we have determined that VSOE does not exist for any undelivered elements of an arrangement, then the aggregate value of the arrangement, including the value of products and services delivered or performed, is initially deferred until all hardware and software is delivered, and then is recognized ratably over the period of the last deliverable, generally the service period of the contract. The deferral of revenue under arrangements where we have determined that VSOE does not exist has resulted in $4.9 million being recorded as deferred revenue at June 30, 2010. If we had made alternative assessments as to the existence of VSOE in these arrangements, some or all of these amounts could have been recognized as revenue prior to June 30, 2010.

Share-Based Compensation Expense. We recognize compensation expense for all share-based payments granted after October 1, 2005 and prior to but not yet vested as of October 1, 2005, in accordance with ASC Topic 718, “Compensation-Stock Compensation” and ASC Subtopic 505-50, “Equity-Based Payments to Non-Employees”. Under the fair value recognition provisions of ASC Topic 718 and Subtopic 505-50, we recognize share-based compensation net of an estimated forfeiture rate, and only recognize compensation cost for those shares expected to vest on a straight-line basis over the service period of the award.

Assumptions/Approach Used: Determining the appropriate fair value model and calculating the fair value of share-based payment awards requires the input of highly subjective assumptions, including the expected life of the share-based payment awards, and stock price volatility. Management determined that volatility is based on historical volatility trends. In addition, we are required to estimate the expected forfeiture rate, and only recognize expense for those shares expected to vest. If our actual forfeiture rate is materially different from our estimate, the share-based compensation expense could be significantly different from what we have recorded in the current period.

Effect if Different Assumptions Used: The assumptions used in calculating the fair value of share-based payment awards, along with the forfeiture rate estimation, represent management’s best estimates, but these estimates involve inherent uncertainties and the application of management’s judgment. As a result, if factors change and we use different assumptions, our stock-based compensation expense could be materially different in the future.

Property and Equipment and Leased Gaming Equipment. Property and equipment and leased gaming equipment is stated at cost. The cost of property and equipment and leased gaming equipment is depreciated over their estimated useful lives, generally using the straight-line method for financial reporting, and regulatory acceptable methods for tax reporting purposes. Player terminals and related components and equipment are included in the Company’s rental

pool. The rental pool can be further delineated as “rental pool – deployed”, which consists of assets deployed at customer sites under participation agreements, and “rental pool – undeployed”, which consists of assets with the Company that are available for customer use. Rental pool – undeployed consists of both new units awaiting deployment to a customer site and previously deployed units currently back with the Company to be refurbished awaiting re-deployment. Routine maintenance of property and equipment and leased gaming equipment is expensed in the period incurred, while major component upgrades are capitalized and depreciated over the estimated useful life (Critical Assumption #1) of the component. Sales and retirements of depreciable property are recorded by removing the related cost and accumulated depreciation from the accounts. Gains or losses on sales and retirements of property are reflected in our results of operations.

Management reviews long-lived asset classes for impairment at least annually or whenever events or changes in circumstances indicate that the carrying amount of an asset may not be recoverable. For impairment analysis purposes, the Company's rental pool is viewed as a fungible pool of assets; including assets in both rental pool-deployed and rental pool-undeployed. In order to determine whether these assets are impaired, the net book value of the rental pool is compared to an estimate of future net cash flows from all existing facilities. The primary assumption used in determining future cash flows is our estimate of future revenue. In addition, the Company analyzes the composition of its rental pool to determine the future use of older models and related components for those models. The impairment analysis for the fiscal year ended September 30, 2009 indicated that we had substantial cash flows to fully recover the carrying value of the entire rental pool. As of June 30, 2010 and September 30, 2009, the balance sheet consisted of $53.0 million and $65.4 million, respectively, of rental pool assets. (Critical Assumption #2)

Assumptions/Approach used for Critical Assumption #1: The carrying value of the asset is determined based upon management's assumptions as to the useful life of the asset, where the assets are depreciated over the estimated life on a straight line basis, where the useful life of items in the rental pool has been determined by management to be three years.

Effect if different assumptions used for Critical Assumption #1: While we believe that the useful lives that have been determined for our fixed assets are reasonable, different assumptions could materially affect the carrying value of the assets, as well as the depreciation expense recorded in each respective period related to those assets. During the nine month period ended June 30, 2010, a significant portion of the $40.0 million of depreciation and amortization expense related to assets in the rental pool. If the depreciable life of assets in our rental pool were changed from three years to another period of time, we could incur a materially different amount of depreciation expense during the period.

Assumptions/Approach used for Critical Assumption #2: Recoverability of assets to be held and used is measured through considerations of the future undiscounted cash flows expected to be generated by the assets as a group, as opposed to analysis by individual asset. We also reviewed the future undiscounted cash flows of assets in place at specific locations for further analysis. If such assets are considered to be impaired, the impairment recognized is measured by the amount by which the carrying amount of the assets exceeds their fair value. Assets to be disposed of are reported at the lower of the carrying amount or the fair value less costs of disposal. The carrying value of the asset is determined based upon management's assumptions as to the useful life of the asset, where the assets are depreciated over the estimated life on a straight-line basis.

Effect if different assumptions used for Critical Assumption #2: Impairment testing requires judgment, including estimations of useful lives of the assets, estimated cash flows, and determinations of fair value. While we believe our estimates of useful lives and cash flows are reasonable, different assumptions could materially affect the measurement of useful lives, recoverability and fair value. If actual cash flows fall below initial forecasts, we may need to record additional amortization and/or impairment charges. Additionally, while we believe that analysis of the recoverability of assets in our rental pool is accurately assessed from a homogenous level due to the interchangeability of player stations and parts, if these assets were to be reviewed for impairment using another approach, there could be different outcomes to any impairment analysis performed.

Development Agreements. We enter into development agreements to provide financing for new gaming facilities or for the expansion of existing facilities. In return, the facility dedicates a percentage of its floor space to exclusive placement of our player terminals, and we receive a fixed percentage of those player terminals' hold per day over the term of the agreement. Certain of the agreements contain player terminal performance standards that could allow the facility to reduce a portion of our guaranteed floor space. In addition, certain development agreements allow the facilities to buy out floor space after advances that are subject to repayment have been repaid. The agreements typically provide for a portion of the amounts retained by the gaming facility for their share of the hold to be used to repay some or all of the advances recorded as notes receivable. Amounts advanced in excess of those to be reimbursed

by the customer for real property and land improvements are allocated to intangible assets and are generally amortized over the life of the contract, using the straight-line method of amortization (Critical Assumption #1), which is recorded as a reduction of revenue generated from the gaming facility. In the past and in the future, we may by mutual agreement and for consideration, amend these contracts to reduce our floor space at the facilities. Any proceeds received for the reduction of floor space is first applied against the intangible asset for that particular development agreement, if any.

Management reviews intangible assets related to development agreements for impairment whenever events or changes in circumstances indicate that the carrying amount of an asset may not be recoverable (Critical Assumption #2). For the nine month period ended June 30, 2010, there was no impairment to the assets' carrying values.

Assumptions/Approach used for Critical Assumption #1: Amounts advanced in excess of those to be reimbursed by the customer for real property and land improvements are allocated to intangible assets and are generally amortized over the life of the contract, using the straight-line method of amortization, which is recorded as a reduction of revenue generated from the gaming facility. We use a straight-line amortization method, as a pattern of future benefits cannot be readily determined.

Effect if Different Assumptions used for Critical Assumption #1: While we believe that the use of the straight-line method of amortization is the best way to account for the costs associated with the costs of acquiring exclusive floor space rights at our customers facilities, the use of an alternative method could have a material effect on the amount recorded as a reduction to revenue in the current reporting period.

Assumptions/Approach used for Critical Assumption #2: We estimate cash flows directly associated with the used of the intangible assets to test recoverability and remaining useful lives based upon the forecasted utilization of the asset and expected product revenues. In developing estimated cash flows, we incorporate assumptions regarding future performance, including estimations of hold per day and estimated units. When the carrying amount exceeds the undiscounted cash flows expected to result from the use and eventual disposition of the asset, we then compare the carrying amount to its current fair value. We recognize an impairment loss if the carrying amount is not recoverable and exceeds its fair value.

Effect if Different Assumptions used for Critical Assumption #2: Impairment testing requires judgment, including estimations of cash flows, and determinations of fair value. While we believe our estimates of future revenues and cash flows are reasonable, different assumptions could materially affect the measurement of useful lives, recoverability and fair value. If actual cash flows fall below initial forecasts, we may need to record additional amortization and/or impairment charges.

Allowance for Doubtful Accounts. We maintain an allowance for doubtful accounts related to our accounts receivable and notes receivable that have been deemed to have a high risk of uncollectibility. Management reviews its accounts receivable and notes receivable on a monthly basis to determine if any receivables will potentially be uncollectible. Management analyzes historical collection trends and changes in its customer payment patterns, customer concentration, and creditworthiness when evaluating the adequacy of its allowance for doubtful accounts. In our overall allowance for doubtful accounts, we include any receivable balances where uncertainty exists as to whether the account balance has become uncollectible. Based on the information available, management believes the allowance for doubtful accounts is adequate; however, actual write-offs may vary from the recorded allowance.

Income Taxes. In accordance with ASC Topic 740, "Income Taxes", we have recorded deferred tax assets and liabilities to account for the expected future tax benefits and consequences of events that have been recognized in our financial statements and our tax returns. There are several items that result in deferred tax asset and liability impact to the balance sheet. If we conclude that it is more likely than not that some portion or all of the deferred tax assets will not be realized under accounting standards, it is reduced by a valuation allowance to remove the benefit of recovering those deferred tax assets from our financial statements. Additionally, in accordance with ASC Topic 740, as of June 30, 2010, we have recorded a liability of $263,000 associated with uncertain tax positions. ASC Topic 740 prescribes a recognition threshold and measurement attribute for the financial statement recognition and measurement of a tax position taken or expected to be taken in a tax return. We are required to determine whether it is more likely than not (a likelihood of more than 50 percent) that a tax position will be sustained upon examination, including resolution of any related appeals or litigation processes, based on the technical merits of the position in order to record any financial statement benefit. If that step is satisfied, then we must measure the tax position to determine the amount of benefit to recognize in the financial statements. The tax position is measured at the largest amount of benefit that is greater than 50 percent likely of being realized upon ultimate settlement.

Assumptions/Approach Used: Numerous judgments and assumptions are inherent in the determination of future taxable income and tax return filing positions that we take, including factors such as future operating conditions. As of September 30, 2009, management evaluated its ability to utilize the full extent of its deferred tax assets and noted that as of September 30, 2008, the Company had historically reflected a strong earnings history, and had reported cumulative book income for the three years ending September 30, 2008. However, as of September 30, 2009, the Company's earnings had deteriorated, and given the large loss experienced, the Company had reported three years of

cumulative book losses. Furthermore, management's 2010 financial forecast indicated that the Company expected to be near breakeven, and due to uncertainties in the overall economy and the gaming industry specifically, felt that we would not be able to rely, with a sufficient level of certainty, on projections beyond the coming fiscal year.

Effect if Different Assumptions Used: Management, along with consultation from an independent public accounting firm used in tax consultation, continually evaluate complicated tax law requirements and their effect on our current and future tax liability and our tax filing positions. Despite our attempt to make an accurate estimate, the ultimate utilization of our gross deferred tax assets of $28.2 million, primarily associated with the tax basis of our leased gaming equipment and property and equipment is largely dependent upon our ability to generate taxable income in the future or carryback losses to prior years with taxable income. Our liability for uncertain tax positions is dependent upon our judgment on the amount of financial statement benefit that an uncertain tax position will realize upon ultimate settlement and on the probabilities of the outcomes that could be realized upon ultimate settlement of an uncertain tax position using the facts, circumstances and information available at the reporting date to establish the appropriate amount of financial statement benefit. To the extent that a valuation allowance or liability for uncertain tax position is established or increased or decreased during a period, we may be required to include an expense or benefit within income tax expense in the income statement. As of September 30, 2009, management determined that it was not more likely than not that the Company would realize the full benefits associated with its gross deferred tax assets. Therefore, a valuation allowance has been recorded on our deferred tax assets to the full extent that those balances as of June 30, 2010. This reserve was determined due to the uncertainty as to our ability to realize the full extent of these tax differences in future periods.

LIQUIDITY AND CAPITAL RESOURCES

As of June 30, 2010, we had $30.8 million in unrestricted cash and cash equivalents, compared to $12.5 million as of September 30, 2009. Our working capital as of June 30, 2010, was $39.1 million, compared to a working capital of $28.7 million at September 30, 2009. The increase in working capital was primarily the result an increase in cash collections from notes receivable and a slight decrease in accounts payable and accrued expenses. During the nine month period ended June 30, 2010, we used $23.9 million for capital expenditures of property and equipment compared to $36.3 million for the nine month period ended June 30, 2009. We collected $13.2 million and $15.8 million on development agreements during the nine month periods ended June 30, 2010 and 2009, respectively. In addition, we have $59.8 million outstanding and $30 million available for future borrowings under our Credit Agreement, as amended, subject to covenant restrictions (see the discussion of our Credit Agreement in Note 9 and below).

As of June 30, 2010, our total contractual cash obligations were as follows (in thousands):

	Payments Due by period				
	Less than 1 year	1-3 years	3-5 years	More than 5 years	Total
Revolving Credit Facility(1)	$—	$15,000	$—	$—	$15,000
Credit Facility Term Loan(2)	750	44,063	—	—	44,813
Operating leases(3)	1,505	1,989	2,150	393	6,037
Purchase commitments	6,674	—	—	—	6,674
Total	$8,929	$61,052	$2,150	$393	$72,524

(1) Relating to the revolving credit commitment under the Credit Agreement, bearing interest at the Eurodollar rate plus the applicable spread (5.25% as of June 30, 2010).
(2) Consists of amounts borrowed under the term loan to our Credit Agreement at the Eurodollar rate plus the applicable spread (6.5% as of June 30, 2010).
(3) Consists of operating leases for our facilities and office equipment.

32

During the nine month period ended June 30, 2010, we generated $49.2 million in cash from our operations, compared to $36.2 million during the same period of 2009. This $13.0 million increase in cash generated from operations over the prior period was primarily due to collections on accounts receivable, reductions in inventories and prepaids; offset by a decrease in accounts payable.

Cash used in investing activities decreased $13.4 million to $16.4 million in the nine month period ended June 30, 2010, from $29.8 million in the three month period ended June 30, 2009. The decrease was primarily the result of an decrease in net capital expenditures (acquisition of property and equipment and leased gaming equipment less transfer of leased gaming equipment to inventory) of $12.4 million, offset by a decrease in repayments under development agreements of $2.6 million and an increase in advances under development agreements of $4.0 million. Net additions to property and equipment and leased gaming equipment consisted of the following:

	Nine month periods ended June 30,	
	2010	2009
	(In thousands)	
Gaming equipment	$23,368	$30,351
Third-party gaming content licenses	4,763	6,723
Other	390	44
Acquistion of property and equipment and leased gaming equipment	28,521	37,118
Transfer of leased gaming equipment to inventory	(4,573)	(846)
Total	$23,948	$36,272

Cash from financing activities increased by $10.7 million to a $14.2 million usage in the nine month period ended June 30, 2010, from $3.5 million used in financing activities in the same period of 2009. The increase was primarily the result of the paydown of the Credit Agreement by $15.2 million during the current period in comparison to the $3.9 million, net of repayments, borrowed during the same period in 2009.

Our capital expenditures for the next 12 months will depend upon the number of new player terminals that we are able to place into service at new or existing facilities and the actual number of repairs and equipment upgrades to the player terminals that are currently in the field. We will continue to offer games developed by us, as well as games from third parties in an attempt to optimize the balance between Oklahoma compact games (Class III) and our Class II product.

Credit Agreement

See discussion of the Credit Agreement and our credit facility in Note 9 – Credit Agreement, Long-Term Debt and Capital Leases.

The Credit Agreement provides us with the ability to finance development agreements and acquisitions and working capital for general corporate purposes. Advances under the revolving credit commitment and the term loan mature on April 27, 2012, and bear interest at the Eurodollar rate plus the applicable spread, tied to various levels of interest pricing determined by total debt to Adjusted EBITDA.

We are currently in compliance with the covenants in our Credit Agreement, as recently amended; however, we cannot be certain that we will be able to achieve our operating objectives for fiscal 2010 and that we will continue to meet our covenants in the Credit Agreement.

If we fail to remain in compliance with the covenants of our Credit Agreement, we will be required to seek modification or waiver of the provisions of that agreement and potentially secure additional sources of capital. We cannot be certain that, if required, we will be able to successfully negotiate additional changes to or waivers of the Credit Agreement. Alternatively, we may incur significant costs related to obtaining requisite waivers or renegotiation of the Credit Agreement that could have a material and adverse effect on our operating results.

Our performance and financial results are, to a certain extent, subject to (i) general conditions in or affecting the Native American gaming industry, and (ii) general economic, political, financial, competitive and regulatory factors beyond our control. If our business does not continue to generate cash flow at appropriate levels or if we receive a material judgment against us in a lawsuit (See “Risk Factors – “Litigation may adversely affect our business, financial condition and results of operations,” and “Part I – Item 1. Condensed Consolidated Financial Statements – Note 13 – Commitments and Contingencies”), we may need to raise additional financing. Sources of additional financing might include additional bank debt or the public or private sale of equity or debt securities. However, sufficient funds may not be available, on terms acceptable to us or at all, from these sources, or any others, to enable us to make necessary capital expenditures and to make discretionary investments in the future. See Item 1A.Risk Factors – “Our Credit Agreement contains covenants that limit our ability to finance future operations or capital needs and to engage in other business activities.”

Stock-Based Compensation

At June 30, 2010, we had approximately 5.5 million options outstanding, with exercise prices ranging from $1.61 to $18.71 per share. At June 30, 2010, approximately 3.7 million of the outstanding options were exercisable.

During the three months ended June 30, 2010, options to purchase 7,600 shares of common stock were granted at a weighted average exercise price of $4.50 per share, and we issued 15,925 shares of common stock as a result of stock option exercises with a weighted average exercise price of $2.91.

At June 30, 2009, we had approximately 6.8 million options outstanding, with exercise prices ranging from $1.00 to $18.71 per share. At June 30, 2009, approximately 3.8 million of the outstanding options were exercisable.

During the three months ended June 30, 2009, options to purchase 41,400 shares of common stock were granted at a weighted average exercise price of $3.49 per share, and we issued 217,062 shares of common stock as a result of stock option exercises with a weighted average exercise price of $1.41.

SEASONALITY

We believe our operations are not materially affected by seasonal factors, although we have experienced fluctuations in our revenues from period to period.

CONTINGENCIES

For information regarding contingencies, see “Item 1. Condensed Financial Statements – Note 13 - Commitments and Contingencies” and “PART II – Item 1. Legal Proceedings.”

INFLATION AND OTHER COST FACTORS

Our operations have not been nor are they expected to be materially affected by inflation. However, our domestic and international operational expansion is affected by the cost of hardware components, which are not considered to be inflation sensitive, but rather, sensitive to changes in technology and competition in the hardware markets. In addition, we expect to continue to incur increased legal and other similar costs associated with regulatory compliance requirements and the uncertainties present in the operating environment in which we conduct our business.

ITEM 3. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

We are subject to market risks in the ordinary course of business, primarily associated with interest rate fluctuations.

Our Credit Agreement provides us with additional liquidity to meet our short-term financing needs, as further described under “Item 1. Condensed Financial Statements - Note 9 – Credit Agreement, Long-Term Debt and Capital Leases.” Pursuant to the Credit Agreement, as amended, we may currently borrow up to a total of $90 million, of which $59.8 is outstanding and $30 million is available for future borrowings, subject to covenant restrictions.

Pursuant to the development agreements we enter into with many of our customers, we are required to advance funds for the construction and development of gaming facilities, some of which are required to be repaid. As a result of our adjustable-interest-rate notes payable and fixed-interest-rate-notes receivable described in “Item 1. Condensed Financial Statements – Note 6 – Notes Receivable and Note 9 – Credit Agreement, Long-Term Debt and Capital Leases,” we are subject to market risk with respect to interest rate fluctuations. Any material increase in prevailing interest rates could cause us to incur significantly higher interest expense.

The Credit Agreement also requires that we enter into hedging arrangements covering at least $50.0 million of the term loan for a three-year period. On May 29, 2008, we purchased, for $390,000, an interest rate cap (5% cap rate) covering $50.0 million of the term loan. To the extent that LIBOR rates do not exceed the 5% cap rate, we estimate that a hypothetical increase of 100 basis points in interest rates would increase our annual interest expense by approximately $599,000, based on our variable debt outstanding of $59.8 million as of June 30, 2010.

We account for currency translation from our Mexico operations in accordance with ASC Topic 830, “Foreign Currency Matters.” Balance sheet accounts are translated at the exchange rate in effect at each balance sheet date. Income statement accounts are translated at the average rate of exchange prevailing during the period. Translation adjustments resulting from this process are charged or credited to other comprehensive income. We do not currently manage this exposure with derivative financial instruments.

ITEM 4. CONTROLS AND PROCEDURES

Evaluation of Disclosure Control and Procedures. As of the end of the period covered by this report, an evaluation was carried out under the supervision and with the participation of our management, including our Chief Executive Officer and our Chief Financial Officer, of the effectiveness of the design and operation of management’s disclosure controls and procedures (as defined in rules 13a-15(e) and 15d-15(e) under the Securities Exchange Act of 1934) to ensure information required to be disclosed in our filings under the Securities Exchange Act of 1934, is (i) recorded, processed, summarized and reported within the time periods specified in the SEC rules and forms; and (ii) accumulated and communicated to our management, including our Chief Executive Officer and our Chief Financial Officer, as appropriate, to allow timely decisions regarding required disclosure. Management recognizes that any controls and procedures, no matter how well designed and operated, can only provide reasonable assurance of achieving desired control objectives, and management is necessarily required to apply its judgment when evaluating the cost-benefit relationship of potential controls and procedures. Based upon the evaluation, the Chief Executive Officer and our Chief Financial Officer concluded that the design and operation of these disclosure controls and procedures were effective as of June 30, 2010.

There were no significant changes in our internal controls or in other factors that could significantly affect these controls subsequent to the date of their evaluation, including any corrective actions with regard to significant deficiencies and material weaknesses.

Changes in Internal Control over Financial Reporting. There were no changes in our internal control over financial reporting identified in management's evaluation during the third quarter of fiscal 2010 that have materially affected, or are reasonably likely to materially affect, our internal control over financial reporting.

PART II
OTHER INFORMATION

ITEM 1. LEGAL PROCEEDINGS

The Company is a party to various material legal proceedings, which are described in Note 13 – Commitments and Contingencies, and incorporated by reference into this item and in the Company's Annual Report on Form 10-K filed for the year ended September 30, 2009 under the caption "Item 3. Legal Proceedings." We are subject to litigation from time to time in the ordinary course of our business, as well as litigation to which we are not a party that may establish laws that affect our business. Except as discussed in Note 13 of the Notes to Consolidated Condensed Financial Statements included herein, which is incorporated by reference into this item, during the three month period covered by this Quarterly Report on Form 10-Q, the Company has not been named in any new material legal proceeding, and there have been no material developments in the previously reported legal proceedings.