

Entertainment Gaming Asia Inc.  
Form 10-Q  
November 14, 2013

**FORM 10-Q**

**SECURITIES AND EXCHANGE COMMISSION  
Washington, D.C. 20549**

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

**For the Quarterly Period Ended September 30, 2013**

**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: 001-32161**

**Entertainment Gaming Asia Inc.**  
(Exact name of registrant as specified in its charter)

**Nevada**  
(State or other jurisdiction of  
incorporation or organization)

**91-1696010**  
(I.R.S. Employer  
Identification no.)

**Unit C1, Ground Floor, Koon Wah Building  
No. 2 Yuen Shun Circuit  
Yuen Chau Kok, Shatin  
New Territories, Hong Kong SAR**  
(Address of principal executive offices, including zip code)

**+ 852-3147-6600**  
(Registrant's telephone number, including area code)

**Not Applicable**  
(Former name, former address and former fiscal year, if changed since last report)

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

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

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Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer or a smaller reporting company (as defined in Rule 12b-2 of the Act):

Large accelerated filer ☐

Accelerated filer ☐

Non-accelerated filer ☐

Smaller reporting company ☒

(Do not check if a smaller reporting company)

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

As of November 1, 2013, 30,024,662 shares of common stock of Entertainment Gaming Asia Inc. were outstanding.

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**PART I FINANCIAL INFORMATION****Item 1. Financial Statements****ENTERTAINMENT GAMING ASIA INC. AND SUBSIDIARIES****Consolidated Balance Sheets**  
**(amounts in thousands, except per share data)**

	September 30, 2013	December 31, 2012
	(unaudited)	
ASSETS		
Current assets:		
Cash and cash equivalents	\$ 4,640	\$ 10,365
Accounts receivable, net	1,390	1,841
Other receivables	461	112
Inventories	1,443	2,047
Prepaid expenses and other current assets	310	387
Total current assets	8,244	14,752
Gaming equipment, net	9,275	9,724
Casino contracts	6,068	7,982
Property and equipment, net	9,170	6,170
Goodwill	362	380
Intangible assets, net	990	1,253
Contract amendment fees	261	342
Deferred tax assets		201
Prepays, deposits and other assets	2,646	2,914
Total assets	\$ 37,016	\$ 43,718
LIABILITIES AND STOCKHOLDERS' EQUITY		
Current liabilities:		
Accounts payable	\$ 557	\$ 3,636
Amounts due to a related party	20	
Accrued expenses	1,749	2,619
Income tax payable	(26)	
Customer deposits and other current liabilities	853	656
Total current liabilities	3,153	6,911
Other liabilities	750	1,078
Deferred tax liability	137	137
Total liabilities	4,040	8,126
Stockholders' equity:		
Common stock, \$.001 par value, 75,000,000 shares authorized; 30,024,662 and 29,974,662 shares issued and outstanding	30	30
Additional paid-in-capital	32,922	32,224
Accumulated other comprehensive income	717	929
(Accumulated losses)/ retained earnings	(694)	2,408
Total EGT stockholders' equity	32,975	35,591

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Non-controlling interest	1	1
Total stockholders' equity	32,976	35,592
Total liabilities and stockholders' equity	\$ 37,016	\$ 43,718

The notes to consolidated financial statements are an integral part of these consolidated statements.

**ENTERTAINMENT GAMING ASIA INC. AND SUBSIDIARIES**

**Consolidated Statements of Comprehensive Income**  
**(amounts in thousands, except per share data)**  
**(Unaudited)**

	Three-Month Periods Ended September 30,		Nine-Month Periods Ended September 30,	
	2013	2012	2013	2012
Revenues:				
Gaming operations, gross	\$ 4,546	\$ 4,480	\$ 15,505	\$ 14,634
Less: promotional allowances				
Gaming operations, net	4,546	4,480	15,505	14,634
Gaming products	1,106	1,718	2,695	3,228
Total revenues	5,652	6,198	18,200	17,862
Operating costs and expenses:				
Cost of gaming operations				
Gaming and property equipment depreciation	1,175	1,228	3,580	3,516
Casino contract amortization	613	617	1,851	1,847
Other gaming related intangibles amortization	63	63	189	189
Other operating costs	1,182	1,051	4,672	2,526
Cost of gaming products	1,131	1,526	3,172	2,756
Selling, general and administrative expenses	1,558	1,491	4,614	4,712
Stock-based compensation expenses	109	123	554	675
Gain on dispositions		(2)		(31)
Impairment of assets		42		114
Product development expenses	51	87	206	273
Depreciation and amortization	51	77	128	168
Total operating costs and expenses	5,933	6,303	18,966	16,745
(Loss)/income from continuing operations	(281)	(105)	(766)	1,117
Other (expense)/income:				
Interest expense and finance fees	(1)	(20)	(5)	(109)
Interest income		4	4	32
Foreign currency (losses)/gains	(39)	55	(228)	269
Other	1	(3)	11	22
Total other (expense)/income	(39)	36	(218)	214
(Loss)/income from continuing operations before income tax expense	(320)	(69)	(984)	1,331
Income tax benefit/(expense)	11	(34)	(38)	(124)

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Net (loss)/income from continuing operations	(309)	(103)	(1,022)	1,207
Net income/(loss) from discontinued operations, net of tax		146	(2,080)	292
Net (loss)/income attributable to EGT Stockholders	\$ (309)	\$ 43	\$ (3,102)	\$ 1,499
Other comprehensive income, net of tax				
Foreign currency translation adjustments				
Foreign currency translation adjustments	5	87	(244)	167
Less: reclassification adjustments to net loss			32	
Foreign currency translation adjustments, net	5	87	(212)	167
Other comprehensive income/(loss), net of tax	\$ 5	\$ 87	\$ (212)	\$ 167
Comprehensive (loss)/ income attributable to EGT Stockholders	\$ (304)	\$ 130	\$ (3,314)	\$ 1,666
Basic and diluted earnings per share:				
(Loss)/earnings from continuing operations	\$ (0.01)	\$	\$ (0.03)	\$ 0.04
(Loss)/earnings from discontinued operations, net of tax	\$	\$	\$ (0.07)	\$ 0.01
(Loss)/earnings	\$ (0.01)	\$	\$ (0.10)	\$ 0.05
Weighted average common shares outstanding				
Basic	30,025	29,926	30,024	29,915
Diluted	30,025	29,926	30,024	30,793

The notes to consolidated financial statements are an integral part of these consolidated statements.

**ENTERTAINMENT GAMING ASIA INC. AND SUBSIDIARIES**  
**Consolidated Statements of Cash Flows**  
**(amounts in thousands)**  
**(Unaudited)**

	Nine-Month Periods Ended September 30,	
	2013	2012
Cash flows from operating activities:		
Net (loss)/income	\$(3,102)	\$ 1,499
Adjustments to reconcile net (loss)/income to net cash (used in)/provided by operating activities:		
Foreign currency gains	(3)	(287)
Depreciation of gaming equipment and property and equipment	3,934	3,822
Amortization of casino contracts	1,851	1,847
Amortization of intangible assets	226	215
Amortization of contract amendment fees	81	81
Stock-based compensation expense	554	675
Gain on disposition of gaming equipment		(31)
Impairment of assets		114
Bad debt recoveries	(15)	(61)
Loss on disposition of subsidiary, including property and equipment	999	
Changes in operating assets and liabilities:		
Accounts receivable and other receivables	388	392
Inventories	(258)	(190)
Prepaid expenses and other current assets	537	94
Prepays, deposits and other assets	(475)	(1,226)
Accounts payable	(1,124)	233
Amounts due to a related party	20	(14)
Accrued expenses and other liabilities	(887)	(38)
Income tax payable	(26)	30
Customer deposits and other current liabilities	211	288
Net cash provided by operating activities	2,911	7,443
Cash flows from investing activities:		
Construction/purchase of property and equipment	(4,088)	(2,465)
Purchases of gaming machines and systems	(4,740)	(1,633)
Acquisition of technical know-how		(254)
Addition of project costs		(491)
Proceeds from sale of subsidiary related to discontinued operations	365	
Proceeds from sale of gaming machines, property and equipment		72
Net cash used in investing activities	(8,463)	(4,771)
Cash flows from financing activities:		



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Repayment of short-term debt and leases		(328)
Repayment of notes payable		(4,629)
Exercise of stock options		28
Net cash used in financing activities		(4,929)
Effect of exchange rate changes on cash	(173)	128
Decrease in cash and cash equivalents	(5,725)	(2,129)
Cash and cash equivalents at beginning of period	10,365	12,759
Cash and cash equivalents at end of period	\$4,640	\$ 10,630
Supplemental disclosure of cash flow information		
Interest paid	\$	\$ 136
Income tax paid	\$	\$ 68
Non-cash investing/financing activities		
Purchase of gaming machines and systems	\$659	\$
Issuance of restricted/performance stock	\$99	\$ 179

The notes to consolidated financial statements are an integral part of these consolidated statements.

**ENTERTAINMENT GAMING ASIA INC. AND SUBSIDIARIES**  
**Notes to Consolidated Financial Statements**

**Note 1. Description of Business and Significant Accounting Policies**

The business activities of the Company entail the owning and leasing of electronic gaming machines (EGMs) placed in premier hotels and other venues in Cambodia and the Philippines, the development and operation of casinos and gaming establishments under the Dreamworld brand in select emerging markets in the Indo-China region and the design, manufacture and distribution of gaming chips and plaques under the Dolphin brand to major casinos primarily in Southeast Asia and Australia. Previously, the Company was engaged in the design, manufacture and distribution of other, non-gaming plastic products, primarily for the automotive industry. These operations were sold on March 28, 2013 and related historical revenues and expenses have been reclassified as discontinued operations. The accounting policies of these segments are consistent with the Company's policies for the accompanying consolidated financial statements.

Effective since January 1, 2012, the Company adopted the FASB issued ASU 2011-05, *Comprehensive Income (Topic 220): Presentation of Comprehensive Income, as amended by ASU 2011-12, Comprehensive Income (Topic 220): Deferral of the Effective Date for Amendments to the Presentation of Reclassifications of Items Out of Accumulated Other Comprehensive Income in Accounting Standards Update No. 2011-05*. The amended standards eliminate the option to present components of other comprehensive income as part of the statement of changes in stockholders' equity and require that all changes in stockholders' equity - except investments by, and distributions to, owners - be presented either in a single continuous statement of comprehensive income or in two separate but consecutive statements. The adoption of these amended standards revised the manner which entities present comprehensive income in their financial statements. In addition, the amended standards require to present the changes in accumulated other comprehensive income by component in the statement of stockholders' equity or in the notes to the financial statements. The Company has elected to present the other comprehensive income in a single continuous statement of comprehensive income and present the changes in accumulated other comprehensive income in the statement of stockholders' equity. The adoption of the amended standards did not have any impact on the Company's financial position, results of operations, or earnings per share. The new presentation required by the amended standards has been applied retrospectively to all periods presented.

***Basis of Presentation***

These consolidated financial statements are prepared pursuant to generally accepted accounting principles in the United States for interim financial information and with the instructions to Form 10-Q and Rule 8-03 of Regulation S-X promulgated by the Securities and Exchange Commission ("SEC") and reflect all adjustments, consisting of normal recurring adjustments and other adjustments, which management believes are necessary to fairly present the financial position, results of operations and cash flows of the Company, for the respective periods presented. The results of operations for an interim period are not necessarily indicative of the results that may be expected for any other interim period or the year as a whole. The accompanying unaudited consolidated financial statements should be read in conjunction with the consolidated financial statements and notes thereto in the Company's Annual Report on Form 10-K for the year ended December 31, 2012 filed with the SEC on March 28, 2013. Certain previously reported amounts have been reclassified to conform to the current period presentation.

The Company effected a 1-for-4 reverse stock split of its common shares as of June 12, 2012. All historical share amounts and share price information presented in the financial statements and notes have been proportionally adjusted to reflect the impact of this reverse stock split, including but not limited to basic and diluted weighted-average shares issued and outstanding.

***Principles of Consolidation***

These consolidated financial statements include the accounts of Entertainment Gaming Asia Inc. and all its subsidiaries. All intercompany balances and transactions have been eliminated in consolidation.

***Use of Estimates***

The Company is required to make estimates, judgments and assumptions that it believes are reasonable based on its historical experience, contract terms, observance of known trends in the Company and the industry as a whole, and information available from other outside sources. These estimates affect the reported amounts of assets, liabilities, revenues and expenses and related disclosures of contingent assets and liabilities. On a regular basis, the Company evaluates its estimates, including those related to revenue recognition, product returns, long-lived assets, inventory obsolescence, stock-based compensation, income taxes, bad debts, warranty obligations, long-term contracts, contingencies and litigation. Actual results may differ from those estimates.

***Discontinued Operations***

A discontinued operation is a component of an entity that either has been disposed of, or that is classified as held for sale, and (i) represents a separate major line of business or geographical area of operations; and (ii) is a part of a single coordinated plan to dispose of a separate major line of business or geographical area of operations; or (iii) is a subsidiary acquired exclusively with a view to resale.

Non-current assets held for discontinued operations are carried at the lower of carrying amount or fair value less costs to sell. Any gain or loss from disposal of a business, together with the results of these operations until the date of disposal, is reported separately as discontinued operations. The financial information of discontinued operations is excluded from the respective captions in the Company's consolidated statements of comprehensive income and related notes for all years presented.

### ***Cash and Cash Equivalents***

All highly-liquid instruments with original maturities of three months or less are considered cash equivalents. The Company places its cash and temporary investments with financial institutions. As of September 30, 2013, the Company had deposits in excess of Federal Deposit Insurance Corporation (FDIC) insured limits by approximately \$4.4 million.

### ***Accounts Receivable and Allowance for Doubtful Accounts***

Accounts receivable are stated at face value less any allowances for doubtful accounts. Allowances for doubtful accounts are maintained at levels determined by Company management to adequately provide for uncollectible amounts. In determining the estimated uncollectable amounts, the Company evaluates a combination of factors, including, but not limited to, activity in the related market, financial condition of customers, specific customer collection experience and history of write-offs and collections. Interest income is imposed on overdue accounts receivable after the Company evaluates a combination of factors, including but not limited to, customer collection experiences, customer relationship and contract terms. Accounts receivable balances are written off after all collection efforts have been exhausted.

### ***Inventories***

Inventories are stated at the lower of cost, determined using the first-in, first-out method, or market. Cost elements included in work-in-process and finished goods include raw materials, direct labor and manufacturing overheads.

### ***Long-Lived Assets***

The Company accounts for impairment of long-lived assets in accordance with Financial Accounting Standards Board (FASB) ASC 360, *Property, Plant and Equipment*. Long-lived assets are reviewed for impairment whenever events or changes in circumstances indicate that the carrying amount of an asset may not be recoverable. In such instances, the Company estimates the undiscounted future cash flows that result from the use of the asset and its ultimate disposition. If the sum of the undiscounted cash flows is less than the carrying value, the Company recognizes an impairment loss, measured as the amount by which the carrying value exceeds the fair value of the asset, determined principally using discounted cash flows. There were no impairment charges for long-lived assets for the three-month and nine-month periods ended September 30, 2013. Impairment charges of approximately \$42,000 and \$114,000 were recognized for long-lived assets for the three-month and nine-month periods ended September 30, 2012, respectively.

### ***Prepays, Deposits and Other Assets***

Prepays, deposits and other assets consist primarily of prepaid leases, prepaid value-added taxes in foreign countries, prepayments to suppliers, rental and utilities deposits and restricted cash as lease security. The Company had restricted cash in the amounts of \$NIL and \$331,000 as of September 30, 2013 and December 31, 2012, respectively, in the form of certificates of deposits as security on leases.

### ***Gaming Equipment***

Gaming equipment consists primarily of electronic gaming machines (EGMs) and systems. Gaming equipment is stated at cost. The Company depreciates new gaming equipment over a five-year useful life and depreciates refurbished gaming equipment over a three-year useful life once placed in service. Depreciation of gaming equipment of approximately \$981,000 and \$1.2 million and \$3.1 million and \$3.5 million was included in cost of gaming operations in the consolidated statements of comprehensive income for the three-month and nine-month periods ended September 30, 2013 and 2012, respectively.

***Property and Equipment***

Property and equipment are stated at cost. Depreciation is computed using the straight-line method over the useful lives of the assets currently estimated to be three to twenty years, which in the case of leasehold improvements, is limited to the life of the lease and throughout the renewal period as long as renewal is reasonably assured.

Depreciation of property and equipment of approximately \$194,000 and \$22,000 and \$475,000 and \$54,000 was recorded in the cost of gaming operations in the consolidated statements of comprehensive income for the three-month and nine-month periods ended September 30, 2013 and 2012, respectively.

Depreciation of property and equipment of approximately \$100,000 and \$22,000 and \$208,000 and \$55,000 was included in cost of gaming products in the consolidated statements of comprehensive income for the three-month and nine-month periods ended September 30, 2013 and 2012, respectively.

#### ***Goodwill and Intangible Assets, Including Casino Contracts***

Intangible assets consist of patents, trademarks, technical know-how, gaming operation agreement, casino contracts and goodwill. Intangible assets other than goodwill are amortized on the straight-line basis over the period of time the asset is expected to contribute directly or indirectly to future cash flows, which ranges from four to ten years. The straight-line amortization method is utilized because the Company believes there is no more reliably determinable method of reflecting the pattern for which the economic benefits of the intangible assets are consumed or otherwise used.

Amortization expenses related to casino contracts were approximately \$613,000 and \$617,000 and \$1.9 million and \$1.8 million for the three-month and nine-month periods ended September 30, 2013 and 2012, respectively. Amortization expenses related to other gaming related intangibles were approximately \$63,000 and \$63,000 and \$189,000 and \$189,000 for the three-month and nine-month periods ended September 30, 2013 and 2012, respectively. The amounts were accounted for as cost of gaming operations in the consolidated statements of comprehensive income. Amortization expenses related to technical know-how were approximately \$7,000 and \$6,000 and \$20,000 and \$9,000 for the three-month and nine-month periods ended September 30, 2013 and 2012, respectively. The amounts were accounted for as cost of gaming products in the consolidated statements of comprehensive income. Amortization expenses related to patents and trademarks were approximately \$6,000 and \$6,000 and \$18,000 and \$18,000 for the three-month and nine-month periods ended September 30, 2013 and 2012, respectively. The amounts were accounted for as selling, general and administrative expenses in the consolidated statements of comprehensive income.

The Company measures and tests finite-lived intangibles for impairment when there are indicators of impairment in accordance with ASC 360-10-05, *Property, Plant and Equipment*.

The Company measures and tests Goodwill for impairment, at least annually in accordance with ASC 350-10-05, *Intangibles - Goodwill and Other*.

Impairment testing for goodwill and other intangibles requires judgment, including the identification of reporting units, allocation of related goodwill, assignment of corporate shared assets and liabilities to reporting units, estimated future cash flows and determinations of fair values. While the Company believes its estimates of future revenues and cash flows are reasonable, different assumptions could materially affect the assessment of useful lives, recoverability and fair values. No impairment charges relating to intangible assets were recorded for the three-month and nine-month periods ended September 30, 2013 and 2012, respectively.

#### ***Additional Paid-In-Capital***

During the nine-month period ended September, 30 2013, the increase in additional paid-in-capital account mainly represented issuance of non-cash stock option compensation.

#### ***Litigation and Other Contingencies***

In the performance of its ordinary course of business operations, the Company is subject to risks of various legal matters, litigation and claims of various types. The Company has regular litigation reviews, including updates from corporate and outside counsel, to assess the need for accounting recognition or disclosure of these contingencies. The status of a significant claim is summarized in Note 16.

ASC 450, *Contingencies*, requires that liabilities for contingencies be recorded when it is probable that a liability has been incurred and that the amount can be reasonably estimated. Significant management judgment is required related to contingent liabilities and the outcome of litigation because both are difficult to predict. For a contingency for which an unfavorable outcome is reasonably possible and which is significant, the Company discloses the nature of the contingency and, when feasible, an estimate of the possible loss.

### ***Revenue Recognition***

The Company recognizes revenue when all of the following have been satisfied:

- Persuasive evidence of an arrangement exists;
- The price to the customer is fixed and determinable;
- Delivery has occurred and any acceptance terms have been fulfilled;
- No significant contractual obligations remain; and
- Collection is reasonably assured.

### *Gaming Revenue and Promotional Allowances*

The Company earns recurring gaming revenue from its slot and casino operations.

For slot operations, the Company earns recurring gaming revenue by providing customers with EGMs and casino management systems which track game performance and provide statistics on installed EGMs owned by the Company and leased to venue owners. Revenues are recognized on the contractual terms of the slot agreements between the Company and the venue owners and are based on the Company's share of net winnings, net of customer incentives and commitment fees.

Revenues are recognized as earned with the exception of one of the Company's venues in which revenues were recognized when the payment for net winnings was received as the collections from this venue were not reasonably assured. The slot contract with this venue owner was terminated on July 31, 2012 and the Company collected the balance of payments in the fourth quarter of 2012.

Commitment fees paid to the venue operators relating to contract amendments which are not recoverable from daily net win are capitalized as assets and amortized as a reduction of revenue over the term of the amended contracts. The Company had commitment fee balances related to contract amendments of approximately \$261,000 and \$342,000 as of September 30, 2013 and December 31, 2012, respectively.

For casino operations, the Company's revenues are measured by the aggregate net difference between gaming wins and losses, with liabilities recognized for funds deposited by customers before gaming play occurs and for chips in the customers' possession, if any. Cash discounts, other cash incentives related to casino play and commissions rebated through junkets or tour guides, if any, to customers are recorded as a reduction to casino revenue. Consequently, the Company's casino revenues are reduced by discounts and commissions.

The Company does not accrue a jackpot liability for its slot machine base and progressive jackpots because it can avoid payment of such amounts. Regulations do not prohibit removal of gaming machines from the gaming floor without payment of such jackpots.

Promotional allowances represent goods and services, which would be accounted for as revenue if sold, that a casino gives to customers as an inducement to gamble at that establishment. Such goods and services include food and beverages. The Company includes the retail value of promotional allowances in gross revenues and deducts it from gross revenues to reach net revenues on the face of the consolidated statements of comprehensive income.

The Company also earns recurring gaming revenue by providing customers with table game equipment and casino management services owned and rendered by the Company and leased to the gaming promoters.

Revenues from gaming table leasing arrangements are recognised as earned over the contractual terms of the arrangement between the Company and the gaming promoters.

### *Gaming Products Sales*

The Company recognizes revenue from the sale of its gaming products to end users upon shipment against customer contracts or purchase orders.

The Company also recognizes revenue from the sale of its products to end users on bill-and-hold arrangements when all of the following have been satisfied:

- The risk of ownership must be passed to the buyer;



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- The customer must have a fixed commitment to purchase the goods;
- The buyer, not the Company, must request that the transaction be on bill and hold basis;
- There must be a fixed schedule for the delivery of goods;
- The Company must not have specific performance obligations such that the earning process is not complete;
- The ordered goods must be segregated from the Company's inventory and not subject to being used to fill other orders, and;
- The product must be complete and ready for shipment.

There were no sales related to bill-and-hold arrangements for both the three-month and nine-month periods ended September 30, 2013 and 2012.

### ***Stock-Based Compensation***

Under the fair value recognition provisions of ASC 718, *Compensation-Stock Compensation*, the Company recognizes stock-based compensation expenses for all service-based awards to employees and non-employee directors with graded vesting schedules on the straight-line basis over the requisite service period for the entire award. Estimates are revised if subsequent information indicates that forfeitures will differ from previous estimates, and the cumulative effect on compensation cost of a change in the estimated forfeitures is recognized in the period of the change. For non-employee awards, the Company remeasures compensation cost each period until the service condition is complete and recognizes compensation cost on the straight-line basis over the requisite service period. Option valuation models require the input of highly subjective assumptions, and changes in the assumptions used can materially affect the fair value estimates. Judgment is required in estimating stock price volatility, forfeiture rates, expected dividends, and expected terms that options remain outstanding. For restricted stock awards with performance conditions, the Company evaluates if performance conditions are probable in each reporting period. The compensation expense of restricted awards is recognized ratably over the implicit service period if achieving performance conditions is probable. Cumulative catch-up adjustments are required in the event of changes in assessment of probability. See Note 12 for additional information relating to stock-based compensation assumptions. Stock-based compensation expense totaled approximately \$109,000 and \$123,000 and \$554,000 and \$675,000 for the three-month and nine-month periods ended September 30, 2013 and 2012, respectively.

### ***Product Development***

Product development expenses are charged to expense as incurred. Employee related costs associated with product development are included in product development expenses. Product development expenses were approximately \$51,000 and \$87,000 and \$206,000 and \$273,000 for the three-month and nine-month periods ended September 30, 2013 and 2012, respectively. The decrease was primarily a result of reduced product development activities for the gaming products division during the relocation and early operation of the new manufacturing facilities in Hong Kong during the nine-month period ended September 30, 2013.

### ***Leases***

Leases are classified at the inception date as either a capital lease or an operating lease. A lease is a capital lease if any of the following conditions exists:

- Ownership is transferred to the lessee by the end of the lease term;
- There is a bargain purchase option;
- The lease term is at least 75% of the property's estimated remaining economic life; or
- The present value of the minimum lease payments at the beginning of the lease term is 90% or more of the fair value of the leased property to the lessor at the inception date.

A capital lease is accounted for as if there was an acquisition of an asset and an incurrence of an obligation at the inception of the lease. All other leases are accounted for as operating leases wherein rental payments are expensed as incurred. The Company had no capital leases as of September 30, 2013.

### ***Income Taxes***

The Company is subject to income taxes in the United States (including federal and state) and several foreign jurisdictions in which it operates. Deferred income tax balances reflect the effects of temporary differences between the carrying amounts of assets and liabilities and their tax basis and are stated at enacted tax rates expected to be in effect when taxes are actually paid or recovered. ASC 740, *Income Taxes*, requires that deferred tax assets be evaluated for future realization and reduced by a valuation allowance to the extent the Company believes a portion

will not be realized. The Company considers many factors when assessing the likelihood of future realization of its deferred tax assets, including its recent cumulative earnings experience and expectations of future taxable income by taxing jurisdiction, the carry-forward periods available to the Company for tax reporting purposes, and other relevant factors.

The Company accounts for uncertain tax positions in accordance with ASC 740, which contains a two-step approach to recognizing and measuring uncertain tax positions. The first step is to evaluate the tax position for recognition by determining if the weight of available evidence indicates it is more likely than not that the position will be sustained on audit, including resolution of related appeals or litigation processes, if any. The second step is to measure the tax benefit as the largest amount which is more than 50% likely to be realized upon ultimate settlement. The Company considers many factors when evaluating and estimating its tax positions and tax benefits, which may require periodic adjustments and which may not accurately anticipate actual outcomes. The Company recognizes interest and penalties, if any, related to unrecognized tax benefits in the provision for income taxes in the statements of comprehensive income.

On December 31, 2010, the Company effected a Quasi-Reorganization. As of that date, the Company's deferred taxes were reported in conformity with applicable income tax accounting standards described above, net of applicable valuation allowances. Deferred tax assets and liabilities were recognized for differences between the assigned values and the tax basis of the recognized assets and liabilities with corresponding valuation allowances as appropriate. In accordance with the Quasi-Reorganization requirements, pre-existing tax benefits realized subsequent to the Quasi-Reorganization are recorded directly in equity.

***(Loss)/Earnings Per Share***

Basic (loss)/earnings per share are computed by dividing the reported net (loss)/earnings by the weighted average number of shares of common stock outstanding during the period. Diluted earnings per share is computed by dividing the net income by the weighted average number of shares of common stock and shares issuable from stock options and restricted shares during the period. The computation of diluted earnings per share excludes the impact of stock options and restricted shares that are anti-dilutive. There is no difference in diluted loss per share from basic loss per share as the assumed exercise of common stock equivalents would have an anti-dilutive effect due to losses.

***Foreign Currency Translations and Transactions***

The functional currency of the Company's international subsidiaries, except for its operations in Cambodia whose functional currency is the U.S. dollar, is generally the local currency. For these subsidiaries, the Company translates the assets and liabilities at exchange rates in effect at the balance sheet date and income and expense accounts at average exchange rates during the year. Resulting currency translation adjustments are recorded directly to accumulated other comprehensive income within stockholders' equity. Gains and losses resulting from transactions in non-functional currencies are recorded in the consolidated statements of comprehensive income.

Below is a summary of closing exchange rates as of September 30, 2013 and December 31, 2012 and average exchange rates for the three-month and nine-month periods ended September 30, 2013 and 2012, respectively.

(\$1 to foreign currency)	September 30, 2013	December 31, 2012
Australian dollar	1.07	0.96
Philippine peso	43.31	41.19
Hong Kong dollar	7.75	7.75
Thai baht	31.40	30.84

	Three-Month Periods Ended September 30,		Nine-Month Periods Ended September 30,	
(\$1 to foreign currency)	2013	2012	2013	2012
Australian dollar	1.09	0.96	1.02	0.97
Philippine peso	43.73	42.03	42.16	42.70
Hong Kong dollar	7.76	7.76	7.76	7.76
Thai baht	31.51	31.44	30.47	31.35

***Fair Value Measurements***

Fair value is defined under ASC 820, *Fair Value Measurements and Disclosures*, as the exchange price that would be received for an asset or paid to transfer a liability (an exit price) in the principal or most advantageous market for the asset or liability in an orderly transaction between market participants on the measurement date. Valuation techniques used to measure fair value under ASC 820 must maximize the use of observable inputs and minimize the use of unobservable inputs. The standard establishes a fair value hierarchy based on three levels of input, of which the first two are considered observable and the last unobservable.

- Level 1 Quoted prices in active markets for identical assets or liabilities. These are typically obtained from real-time quotes for transactions in active exchange markets involving identical assets.
- Level 2 Input, other than quoted prices included within Level 1, which are observable for the asset or liability, either directly or indirectly. These are typically obtained from readily-available pricing sources for comparable instruments.

- Level 3 Unobservable input, where there is little or no market activity for the asset or liability. This input reflects the reporting entity's own assumptions of the data that participants would use in pricing the asset or liability, based on the best information available under the circumstances.

As of September 30, 2013, the fair values of cash and cash equivalents, accounts receivable and accounts payable approximate carrying values due to the short maturity of these items.

### ***Guarantees***

The Company recognizes a guarantee at its inception which is the greater of (i) the fair value of the guarantee and (ii) the contingent liability amount. The fair value of a guarantee is determined by using expected present value measurement techniques. The initial liability recognized is amortized over the guarantee period. The Company does not accrue any guarantee liabilities as of the balance sheet dates.

### ***Recently Issued Accounting Standards***

In February 2013, the FASB issued ASU 2013-02, *Reporting of Amounts Reclassified Out of Accumulated Other Comprehensive Income*. The amendments do not change the current requirements for reporting net income or other comprehensive income in financial statements. However, the amendments require an entity to provide information about the amounts reclassified out of accumulated other comprehensive income by component. In addition, an entity is required to present, either on the face of the statement when net income is presented or in the notes, significant amounts reclassified out of accumulated other comprehensive income by the respective line items of net income but only if the amount reclassified is required under U.S. GAAP to be reclassified to net income in its entirety in the same reporting period. For public entities, the amendments are effective prospectively for reporting periods beginning after December 15, 2012. The Company has adopted this update (see Note 18 "Accumulated Other Comprehensive Income.")

**Note 2. Segments**

The Company currently conducts business in two operating segments: (i) gaming operations, which includes electronic gaming machine (EGM) participation and casino operations; and (ii) gaming products, which consist of the design, manufacture and distribution of gaming chips and plaques and, as of October 2013, the distribution of third-party gaming products in select locations in Indo-China and the Philippines. Previously, the Company was also engaged in the design, manufacture and distribution of other non-gaming plastic products, primarily for the automotive industry. These operations were sold on March 28, 2013 and the related historical revenues and expenses have been reclassified as discontinued operations. The accounting policies of these segments are consistent with the Company's policies for the accompanying consolidated financial statements.

(amounts in thousands)	Three-Month Periods Ended September 30,		Nine-Month Periods Ended September 30,	
	2013	2012	2013	2012
Revenues:				
Gaming operations	\$4,546	\$ 4,480	\$15,505	\$ 14,634
Gaming products	1,106	1,718	2,695	3,228
Total revenues	\$5,652	\$ 6,198	\$18,200	\$ 17,862
Operating (loss)/income:				
Gaming operations gross profit (1)	\$1,513	\$ 1,479	\$5,213	\$ 6,442
Gaming products gross profit/(loss)	(25)	192	(477)	472
Corporate and other operating costs and expenses	(1,769)	(1,776)	(5,502)	(5,797)
Total operating (loss)/income	\$(281)	\$ (105)	\$(766)	\$ 1,117
Depreciation and amortization:				
Gaming operations	\$1,867	\$ 1,968	\$5,672	\$ 5,668
Gaming products	130	36	276	86
Corporate	11	10	26	29
Total depreciation and amortization	\$2,008	\$ 2,014	\$5,974	\$ 5,783

(1) Gaming operations gross profit included impairment of assets for the three-month and nine-month periods ended September 30, 2012.

Geographic segment revenues for the three-month and nine-month periods ended September 30, 2013 and 2012 consisted of the following:

(amounts in thousands)	Three-Month Periods Ended September 30,		Nine-Month Periods Ended September 30,	
	2013	2012	2013	2012
Cambodia	\$ 3,759	\$ 3,609	\$ 13,011	\$ 11,971
Macau	185	84	886	748
Philippines	1,186	871	3,445	2,941
Australia	517	1,610	680	2,111
Other	5	24	178	91
	\$ 5,652	\$ 6,198	\$ 18,200	\$ 17,862

For the three-month and nine-month periods ended September 30, 2013 and 2012, in the gaming operations segment, the largest customer represented 66% and 70% and 63% and 73%, respectively, of total gaming operations revenue.

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For the three-month and nine-month periods ended September 30, 2013 and 2012, in the gaming products segment, the largest customer represented 36% and 93% and 22% and 48%, respectively, of total gaming products sales.

### **Note 3. Inventories**

Inventories consisted of the following:

(amounts in thousands)	September 30, 2013 (Unaudited)	December 31, 2012
Raw materials	\$ 887	\$ 867
Work-in-process	224	49
Finished goods	216	924
Spare parts	90	106
Casino inventories	26	101
	\$ 1,443	\$ 2,047

Inventories decreased primarily due to the sale of the non-gaming operations of the Dolphin Australia business on March 28, 2013.

### **Note 4. Prepaid Expenses and Other Current Assets**

Prepaid expenses and other current assets consisted of the following:

(amounts in thousands)	September 30, 2013 (Unaudited)	December 31, 2012
Prepayments to suppliers	\$ 252	\$ 174
Restricted cash		168
Prepaid leases	58	45
	\$ 310	\$ 387

### **Note 5. Receivables**

Accounts and other receivables consisted of the following:

(amounts in thousands)	September 30, 2013 (Unaudited)	December 31, 2012
Trade accounts	\$ 1,390	\$ 1,856
Other	461	112
	1,851	1,968
Less: allowance for doubtful accounts		(15)
Net	\$ 1,851	\$ 1,953

**Note 6. Gaming Equipment**

Gaming equipment is stated at cost. The major categories of gaming equipment and accumulated depreciation consisted of the following:

(amounts in thousands)	Useful Life (years)	September 30, 2013 (Unaudited)	December 31, 2012
EGMs	3-5	\$17,954	\$16,222
Systems	5	1,625	1,093
Other gaming equipment	3-5	320	150
		19,899	17,465
Less: accumulated depreciation		(10,624)	(7,741)
		\$9,275	\$9,724

Depreciation expense of approximately \$981,000 and \$1.2 million and \$3.1 million and \$3.5 million was included in cost of gaming operations in the consolidated statements of comprehensive income for the three-month and nine-month periods ended September 30, 2013 and 2012, respectively.

**Note 7. Property and Equipment**

Property and equipment are stated at cost and consisted of the following:

(amounts in thousands)	Useful Life (years)	September 30, 2013 (Unaudited)	December 31, 2012
Equipment, vehicles, furniture and fixtures	3-10	\$ 4,384	\$ 2,900
Land and building	5-20	4,583	2,483
Leasehold improvements	1-2	882	180
Construction in progress	N/A	638	1,477
		10,487	7,040
Less: accumulated depreciation		(1,317)	(870)
		\$ 9,170	\$ 6,170

Depreciation of property and equipment of approximately \$194,000 and \$22,000 and \$475,000 and \$54,000 was recorded in cost of gaming operations in the consolidated statements of comprehensive income for the three-month and nine-month periods ended September 30, 2013 and 2012, respectively.

Depreciation of property and equipment of approximately \$100,000 and \$22,000 and \$208,000 and \$55,000 was included in cost of gaming products in the consolidated statement of comprehensive income for the three-month and nine-month periods ended September 30, 2013 and 2012, respectively.

**Note 8. Goodwill and Intangible Assets, including Casino Contracts**

Intangible assets, if any, are stated at cost. Intangible assets consisted of the following:

(amounts in thousands)	Useful Life (years)	September 30, 2013 (Unaudited)	December 31, 2012
Gaming operation agreement	4-5	\$ 1,193	\$ 1,232



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Less: accumulated amortization		(504)	(315)
Goodwill	N/A	362	380
Patents	5-6	114	114
Less: accumulated amortization		(56)	(42)
Trademarks	5-9	26	26
Less: accumulated amortization		(9)	(6)
Technical know-how	10	261	259
Less: accumulated amortization		(35)	(15)
Casino contracts	5-6	12,819	12,934
Less: accumulated amortization		(6,751)	(4,952)
		\$ 7,420	\$ 9,615

Amortization expense for finite-lived intangible assets was approximately \$688,000 and \$693,000 and \$2.1 million and \$2.1 million for the three-month and nine-month periods ended September 30, 2013 and 2012, respectively.

Goodwill movements during the periods consisted of the following:

(amounts in thousands)	2013 (Unaudited)	2012
Balance as of January 1	\$ 380	\$ 357
Foreign currency translation adjustment	(18)	23
Balance as of September 30/December 31	\$ 362	\$ 380

**Note 9. Prepaids, Deposits and Other Assets**

Prepaids, deposits and other assets consisted of the following:

(amounts in thousands)	September 30, 2013 (Unaudited)	December 31, 2012
Prepaid taxes	\$ 981	\$ 922
Prepaid leases	717	747
Prepayments to suppliers	506	585
Deposits on EGM orders	26	257
Rentals, utilities and other deposits	416	240
Restricted cash		163
	\$ 2,646	\$ 2,914

As of September 30, 2013, prepaid leases consisted of land lease prepayments of approximately \$224,000 and \$493,000 for the casino projects located in the respective Cambodian provinces of Kampot and Pailin.

**Note 10. Accrued Expenses**

Accrued expenses consisted of the following:

(amounts in thousands)	September 30, 2013 (Unaudited)	December 31, 2012
Payroll and related costs	\$ 197	\$ 1,292
Legal, accounting and tax	359	336
Withholding tax expenses	550	514
Rental expenses	34	
Raw materials	173	
Other	436	477
	\$ 1,749	\$ 2,619

Payroll and related costs as of December 31, 2012 included accruals of approximately \$726,000 related to the Company's prior operations in Australia. These accruals were fully settled during the three-month period ended March 31, 2013.

**Note 11. Other Liabilities**

Other liabilities consisted of the following:

(amounts in thousands)	September 30, 2013 (Unaudited)	December 31, 2012
Other tax liabilities	\$ 667	\$ 555
Provision for long service leave (1)		369
Others	83	154
	\$ 750	\$ 1,078

(1) Provision for long service leave was settled during the sale of the non-gaming operations in March 2013.

**Note 12. Stock-Based Compensation*****Options***

The Company effected a 1-for-4 reverse stock split of its common shares as of June 12, 2012. All historical share amounts and share price information presented in this Note 12 have been proportionally adjusted to reflect the impact of this reverse stock split.

At the annual shareholders meeting held on September 8, 2008, a new stock option plan, the "2008 Stock Incentive Plan" (the "2008 Plan"), was voted on and became effective on January 1, 2009, which replaced two previous plans, the Amended and Restated 1999 Stock Option Plan and the Amended and Restated 1999 Directors' Stock Option Plan (the "Stock Option Plans"), thereby terminating both of the Stock Option Plans on December 31, 2008.

The 2008 Plan allows for incentive awards to eligible recipients consisting of:

- Options to purchase shares of common stock that qualify as incentive stock options within the meaning of the Internal Revenue Code;
- Non-statutory stock options that do not qualify as incentive options;
- Restricted stock awards; and

Performance stock awards which are subject to future achievement of performance criteria or free of any performance or vesting.

The maximum number of shares reserved for issuance under the 2008 Plan was originally 1,250,000 shares, and in July 2010 the Company's shareholders approved an increase in the number of shares reserved for issuance to 2,500,000 shares. At the annual shareholders meeting held on July 13, 2012, the Company's shareholders approved a further increase in the number of shares reserved for issuance to 3,750,000 shares. The exercise price shall not be less than 100% of the fair market value of one share of common stock on the date of grant, unless the participant owns more than 10% of the total combined voting power of all classes of stock of the Company or any parent or subsidiary corporation of the Company, in which case the exercise price shall then be 110% of the fair market value. The outstanding stock options generally vest from six-months and one-day to over three years and have ten-year contractual terms.

During the nine-month period ended September 30, 2013, stock options for the purchase of 360,000 shares of common stock were granted with a weighted average exercise price of \$1.93 and weighted average fair value of \$1.18(2012: \$1.06) per share and will vest from six-month and one day to three-year periods. During the nine-month period ended September 30, 2013, 50,000 shares of restricted stock awards with a fair value of \$1.97 per share were issued. The shares of restricted stock shall vest, subject to and upon the recipient's achievement of key operational and financial performance milestones. For restricted stock awards with performance conditions, the Company evaluates if performance conditions are probable in each reporting period. The compensation expense of restricted awards is recognized ratably over the implicit service period if achieving performance conditions is probable. Cumulative catch-up adjustments are required in the event of any changes in the assessment of probabilities.

During the nine-month period ended September 30, 2013 there was no exercise of outstanding stock options.

Prior to January 1, 2009, the Company had two stock options plans, the Amended and Restated 1999 Stock Option Plan and the Amended and Restated 1999 Directors' Stock Option Plan (the "Previous Stock Option Plans"), through which 3,750,000 shares and 75,000 shares were authorized, respectively. Both Previous Stock Option Plans expired on December 31, 2008. However, options granted under the Previous Stock Option Plans that were outstanding as of the date of termination remain outstanding and subject to termination according to their terms.

As of September 30, 2013, stock options for the purchase of 936,864 and 22,500 shares of common stock, respectively, were outstanding in relation to the Amended and Restated 1999 Stock Option Plan and the Amended and Restated 1999 Director's Stock Option Plan.

As of September 30, 2013, there were no outstanding non-plan options to purchase common stock. All previously granted non-plan options had expired by December 31, 2012. The non-plan options were issued to certain employees and non-employees of EGT Entertainment Holding as approved by the Company's stockholders in September 2007 pursuant to the initial closing of the transactions under the Securities Purchase and Product Participation Agreement dated June 12, 2007 between the Company and EGT Entertainment Holding.

As of September 30, 2013, stock options for the purchase of 2,340,708 shares of common stock were outstanding under the 2008 Plan.

As of September 30, 2013, 2,792,155 stock options were exercisable with a weighted average exercise price of \$2.18, a weighted average fair value of \$0.83 and an aggregate intrinsic value of approximately \$738,000. The total fair value of shares vested during the nine-month period ended September 30, 2013 was approximately \$747,000. The total compensation cost related to unvested shares as of September 30, 2013 was approximately \$390,000. The amount is expected to be recognized over 1.83 years.

A summary of all current and expired plans as of September 30, 2013 and changes during the period then ended consisted of the following:

	Number of Shares	Weighted Average Exercise Price	Weighted Average Remaining Contractual Life (in years)	Aggregate Intrinsic Value (in thousands)
Outstanding as of December 31, 2012	2,956,738	\$ 2.13	6.13	\$ 2,293
Granted	360,000	1.93		
Exercised				
Forfeited or expired	(16,666)	2.16		

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Outstanding as of September 30, 2013	3,300,072	2.11	5.61	738
Exercisable as of September 30, 2013	2,792,155	\$ 2.18	5.08	\$ 738

***Recognition and Measurement***

The fair value of each stock-based award to employees and non-employee directors is estimated on the measurement date which generally is the grant date while awards to non-employees are measured at the earlier of the performance commitment date or the service completion date using the Black-Scholes-Merton option-pricing model. Option valuation models require the input of highly subjective assumptions, and changes in assumptions used can materially affect the fair value estimates. The Company estimates the expected life of the award by taking into consideration the vesting period, contractual term, historical exercise data, expected volatility, blackout periods and other relevant factors. Volatility is estimated by evaluating the Company's historical volatility data. The risk-free interest rate on the measurement date is based on U.S. Treasury constant maturity rates for a period approximating the expected life of the award. The Company historically has not paid dividends and it does not expect to pay dividends in the foreseeable future and, therefore, the expected dividend rate is zero.

**Restricted Stock**

	Number of shares	Weighted Average Fair Value at Grant Date	Weighted Average Remaining Contractual Life (in years)
Unvested balance as of December 31, 2012		\$	
Granted	50,000	1.97	0.25
Vested (1)	(37,500)	1.97	0.25
Unvested balance as of September 30, 2013	12,500	\$ 1.97	0.25

(1) Vested shares included 37,500 shares of restricted common stock issued in 2013 for which final vesting is subject to the approval by the Company's compensation committee.

The following table summarizes the range of assumptions utilized in the Black-Scholes-Merton option-pricing model for the valuation of stock options granted during the nine-month periods ended September 30, 2013 and 2012.

	Nine-Month Periods Ended September 30,			
	2013		2012	
Range of values:	Low	High	Low	High
Expected volatility	73.41 %	76.49 %	79.15 %	127.83 %
Expected dividends				
Expected term (in years)	3.73	9.70	3.73	9.97
Risk free rate	0.55 %	2.67 %	0.56 %	1.95 %

For stock-based compensation accrued to employees and non-employee directors, the Company recognizes stock-based compensation expense for all service-based awards with graded vesting schedules on the straight-line basis over the requisite service period for the entire award. Initial accruals of compensation expense are based on the estimated number of shares for which requisite service is expected to be rendered. Estimates are revised if subsequent information indicates that forfeitures will differ from previous estimates, and the cumulative effect on compensation cost of a change in the estimated forfeitures is recognized in the period of the change.

For non-employee awards, the Company remeasures compensation cost each period until the service condition is complete and recognizes compensation cost on the straight-line basis over the requisite service period.

The Company estimates forfeitures and recognizes compensation cost only for those awards expected to vest assuming all awards would vest and reverses recognized compensation cost for forfeited awards when the awards are actually forfeited.

For awards with service conditions and graded vesting that were granted prior to the adoption of ASC 718, the Company estimates the requisite service period and the number of shares expected to vest, and recognizes compensation expense for each tranche on the straight-line basis over the estimated requisite service period.

**Note 13. Related Party Transactions**

Effective January 1, 2010, the Company began sub-leasing office space from Melco Services Limited, a wholly-owned subsidiary of Melco International Development Limited, which is also the parent of the Company's principal shareholder, EGT Entertainment Holding. This sub-lease expired at the end of March 2013 and, subsequently, the Company moved its principal executive office to the premises of the new Hong Kong Dolphin

facilities. The relocation of the Company's principal executive office serves to minimize costs and improve oversight of the Dolphin operations.

On April 21, 2008, the Company entered into a Trade Credit Facility Agreement (the "Facility Agreement") with Elixir International Limited, a company which used to be a wholly-owned subsidiary of EGT Entertainment Holding, the Company's principal shareholder. Upon entering into the Agreement, the Company issued the first note pursuant to the terms of the Facility Agreement in the principal amount of \$15.0 million. This amount extinguished a then trade payable of an equivalent amount to Elixir International with respect to EGMs previously acquired.

As a result of the disposal of Elixir International by EGT Entertainment Holding, Elixir International Limited assigned and novated all its rights and obligations under the Facility Agreement and the related promissory note (as amended) to EGT Entertainment Holding in April 2010.

Subsequent to its origination, the Facility Agreement was amended three times, mostly recently on May 25, 2010 on which date the Company issued a new note to replace the previous terms. Under these most recent terms, the Company paid total principal and interest of approximately \$6.2 million and \$143,000, respectively in equal monthly installments to EGT Entertainment Holding for the year ended December 31, 2012. As of December 31, 2012, the notes payable to EGT Entertainment Holding were fully settled.

Significant revenues, purchases and expenses arising from transactions with related parties consisted of the following:

(amounts in thousands)	Three-Month Periods Ended September 30,		Nine-Month Periods Ended September 30,	
	2013	2012	2013	2012
EGT Entertainment Holding				
Principal and interest payments	\$	\$ 1,588	\$	\$ 4,765
Melco Crown Gaming (Macau) Limited				
Trade sales of gaming products	\$ 185	\$	\$ 815	\$ 616
Melco Services Limited				
Technical services	\$ 1	\$ 8	\$ 10	\$ 24
Office rental	2	38	51	113
Golden Future (Management Services) Ltd				
Management services	\$ 59	\$	\$ 80	\$

#### **Note 14. Income Taxes**

The Company recorded income tax benefit/(expense) of approximately \$11,000 and \$(34,000) and \$(38,000) and \$(124,000) for the three-month and nine-month periods ended September 30, 2013 and 2012, respectively. The Company's effective income tax rates were (3.4)% and 49.3% and 3.9% and (9.3)% for the three-month and nine-month periods ended September 30, 2013 and 2012, respectively. The Company's EGT Cambodia and Dreamworld Casino (Pailin) operations are tax exempt, paying a fixed monthly tax rather than a tax on income. The change in effective tax rate was mainly due to an increase in consolidated pre-tax loss.

The Company has been subjected to income tax examinations by tax authorities in jurisdictions in which it operates. During the years ended December 31, 2011 and 2012, the United States Internal Revenue Service (the "IRS") conducted an audit of the Company's 2008 and 2009 tax returns in the United States. On January 23, 2013, the IRS formally notified the Company that it had completed the review of the examination of the above-mentioned years with no changes to the Company's tax position.

The Company's 2008 to 2012 Australian income tax returns remain open to examination by the Australian Taxation Office. The Company's 2009 to 2012 Cambodian income tax returns remain open to examination by the General Department of Taxation. The Company's 2009 to 2012 Philippines income tax returns remain open to examination by the Philippines Bureau of Internal Revenue.

#### **Note 15. Discontinued Operations**

From July 2006 until March 2013, the Company conducted the development, manufacture and sale of gaming chips and plaques from its subsidiary, Dolphin Products Pty Limited ("Dolphin Australia") in Melbourne, Australia. It also conducted the development, manufacture and sale of non-gaming plastic products for a number of industries, including the automotive industry, from the Melbourne facility.

On February 22, 2013, the Company entered into a Share Sale Agreement with the then general manager of the Dolphin Australia operations, pursuant to which it agreed to sell him the portion of its business dedicated to the non-gaming plastic products, mainly automotive parts. The sale was completed on March 28, 2013. In connection



with the sale of non-gaming operations, the Company relocated its gaming products operations, which included gaming chips and plaques, from Melbourne, Australia to Hong Kong. Commercial production in the new facility commenced in May 2013.

Prior to the completion of the sale, the Company transferred out of Dolphin Australia to Elixir Gaming Technologies (Hong Kong) Limited and a newly formed Dolphin Products Limited company in Hong Kong, both of which are subsidiaries wholly-owned by the Company, all inventory on hand and all assets and operations relating to the Company's gaming chips and plaques operations, including all trademarks, patent rights and other intellectual property.

The purchase price received pursuant to the Share Sale Agreement was AUD350,000. The Company also agreed to assume Dolphin Australia's liabilities for (i) severance under Australian labor laws for those employees to be terminated by Dolphin Australia as part of the transactions, approximately \$750,000, (ii) the lease for the Melbourne facility through the end of its present term expiring in January 2014, net of sub-lease income, approximately \$350,000, and (iii) all Dolphin Australia payables, net of receivables, relating to both gaming and non-gaming operations up to March 28, 2013.

The buyer owed the Company \$1.1 million for the settlement of working capital related to the sale of the non-gaming Dolphin assets. As of September 30, 2013, the outstanding balance was approximately \$27,000.

As part of the sale transaction, the Company also agreed to grant Dolphin Australia a non-transferable, substantially royalty-free license to utilize certain trademarks and patent rights in connection with Dolphin Australia's manufacture and sale of plastic products for the non-gaming industries.

The following table details selected financial information for the discontinued operations in the consolidated statements of comprehensive income.

(amounts in thousands)	Three-Month Periods Ended September 30,		Nine-Month Periods Ended September 30,	
	2013	2012	2013	2012
Income from operations	\$	\$ 79	\$ 188	\$ 74
Loss on disposal			(2,442)	
Other income (1)		67	146	218
Income tax benefit (2)			28	
Income/(loss) from discontinued operations, net of tax	\$	\$ 146	\$ (2,080)	\$ 292

(1) Other income represented recognized government grant income from discontinued operations.

(2) Income tax benefit represented a reversal of previously recognized uncertain tax benefits.

## Note 16. Commitments and Contingencies

### Legal Matters

#### *Prime Mover/Strata Litigation*

On March 26, 2010, a complaint (as subsequently amended on May 28, 2010) (the "Complaint") was filed by certain of the Company's shareholders including Prime Mover Capital Partners L.P., Strata Fund L.P., Strata Fund Q.P. L.P., and Strata Offshore Fund, Ltd (collectively, the "Plaintiffs") in the United States District Court for the Southern District of New York against certain defendants including the Company and certain other of our current and former directors and officers.

The Complaint alleges claims related to disclosures concerning the Company's electronic gaming machine participation business (the "Slot Business"), including but not limited to the alleged violations of Sections 10(b) and 20(a) of the Securities Exchange Act of 1934 and Rule 10b-5 promulgated thereunder, violations of Nevada Revised Statutes Sections 90.580(e) and 90.660(3), breach of fiduciary duty, and negligent misrepresentations. The Plaintiffs allege that the Company and certain other defendants made false and misleading statements about the Slot Business in filings with the SEC, press releases, and other industry and investor conferences and meetings during the period from June 13, 2007 to August 13, 2008 and that the Plaintiffs then purchased the securities at the inflated prices and later suffered economic losses when the price of our securities decreased.

On June 22, 2011, the court dismissed all of the Plaintiffs' claims except for two breach-of-contract counts against the Company. All claims against the current and former officers and directors were dismissed. On December 20, 2011 the Plaintiffs filed a second amended Complaint (the "Second Amended Complaint") for re-pleading all the securities claims against the Company and all the relevant current and/or former officers and directors.

On September 27, 2012, the District Court dismissed Plaintiffs' Second Amended Complaint in its entirety. On September 28, 2012, the clerk entered a judgment against the Plaintiffs. Accordingly, all claims against the Company and the current and former officers and directors, including the Plaintiffs' breach of contract claims, were dismissed.

On October 25, 2012, the Plaintiffs filed a Notice of Appeal seeking review by the Second Circuit Court of Appeals of the District Court's order and judgment dismissing the Second Amended Complaint. The parties have filed their respective briefs (the Plaintiffs did not file a reply brief, however) and requested oral argument. The Second Circuit granted the parties' requests for oral argument, which is scheduled for December 10, 2013. The Second Circuit has the ability to affirm or reverse the District Court's order and judgment in whole or in part, and can decide to reinstate some or all of the claims from Plaintiffs' Second Amended Complaint.

The Plaintiffs seek unspecified damages, as well as interest, costs and attorneys' fees. The Company intends to defend itself vigorously against the Plaintiffs' claims. As the litigation is at a preliminary stage, it is not possible to predict the likely outcome of the case or the probable loss, if any, or the continuation of insurance coverage and, accordingly, no accrual has been made for any possible losses in connection with this matter.

**Note 17. (Loss)/Earnings Per Share**

Computation of the basic and diluted (loss)/earnings per share from continuing operations consisted of the following:

(amounts in thousands, except per share data)	Three-Month Periods Ended September 30, 2013			2012		
	Loss	Number of Shares	Per Share Amount	Loss	Number of Shares	Per Share Amount
Basic						
Net loss attributable to equity shareholders	\$ (309)	30,025	\$ (0.01)	\$ (103)	29,926	\$
Effect of dilutive securities						
Dilutive stock options/restricted shares (1)						
Diluted						
Net loss attributable to equity shareholders plus assumed conversion	\$ (309)	30,025	\$ (0.01)	\$ (103)	29,926	\$
(amounts in thousands, except per share data)	Nine-Month Periods Ended September 30, 2013			2012		
	Loss	Number of Shares	Per Share Amount	Income	Number of Shares	Per Share Amount
Basic						
Net (loss)/income attributable to equity shareholders	\$ (1,022)	30,024	\$ (0.03)	\$ 1,207	29,915	\$ 0.04
Effect of dilutive securities						
Dilutive stock options/restricted shares (1)					878	
Diluted						
Net (loss)/income attributable to equity shareholders plus assumed conversion	\$ (1,022)	30,024	\$ (0.03)	\$ 1,207	30,793	\$ 0.04

(1) For the three-month and nine-month periods ended September 30, 2013, there were no differences in diluted loss per share from basic loss per share as the assumed exercise of common stock equivalents would have an anti-dilutive effect due to losses.

Outstanding stock options for 2,425,072 and 1,412,220 shares of common stock were excluded from the calculation of diluted earnings per share for the three-month periods ended September 30, 2013 and 2012, respectively as their effect would have been anti-dilutive. Outstanding stock options for 2,425,072 and 1,935,903 shares of common stock were excluded from the calculation of diluted earnings per share for the nine-month periods ended September 30,

2013 and 2012, respectively as their effect would have been anti-dilutive.

**Note 18. Accumulated Other Comprehensive Income**

The accumulated balances in respect of other comprehensive income consisted of the following:

(amounts in thousands)	Unrealized Actuarial Income	Foreign Currency Translation	Accumulated Other Comprehensive Income
Balances, January 1, 2012	\$ (14)	\$ 573	\$ 559
Current period other comprehensive income	76	294	370
Balances, December 31, 2012	62	867	929
Current period other comprehensive loss		(244)	(244)
Amounts reclassified from accumulated other comprehensive income to net loss on disposal of subsidiary (1)		32	32
Balances, September 30, 2013	\$ 62	\$ 655	\$ 717

(1) Amount represented reclassification from accumulated other comprehensive income to net loss from discontinued operations on disposal of a subsidiary.

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

***CAUTIONARY STATEMENT***

The following discussion and analysis should be read in conjunction with our unaudited consolidated financial statements and the related notes thereto contained elsewhere in this report. The information contained in this quarterly report on Form 10-Q is not a complete description of our business or the risks associated with an investment in our common stock. We urge you to carefully review and consider the various disclosures made by us in this report and in our other reports filed with the Securities and Exchange Commission, or SEC, including our annual report on Form 10-K for the year ended December 31, 2012, filed with the SEC on March 28, 2013 and subsequent reports on Form 8-K, which discuss our business in greater detail.

In this report we make, and from time to time we otherwise make, written and oral statements regarding our business and prospects, such as projections of future performance, statements of management's plans and objectives, forecasts of market trends, and other matters that are forward-looking statements within the meaning of Section 27A of the Securities Act of 1933 and Section 21E of the Securities Exchange Act of 1934. Statements containing the words or phrases "will likely result," "are expected to," "will continue," "is anticipated," "estimates," "projects," "believes," "anticipates," "intends," "target," "goal," "plans," "objective," "should" or similar expressions identify forward-looking statements which may appear in documents, reports, filings with the Securities and Exchange Commission, news releases, written or oral presentations made by officers or other representatives made by us to analysts, stockholders, investors, news organizations and others, and discussions with management and other of our representatives. For such statements, we claim the protection of the safe harbor for forward-looking statements contained in the Private Securities Litigation Reform Act of 1995.

Our future results, including results related to forward-looking statements, involve a number of risks and uncertainties. No assurance can be given that the results reflected in any forward-looking statements will be achieved. Any forward-looking statement speaks only as of the date on which such statement is made. Our forward-looking statements are based upon assumptions that are sometimes based upon estimates, data, communications and other information from suppliers, government agencies and other sources that may be subject to revision. Except as required by law, we do not undertake any obligation to update or keep current either (i) any forward-looking statement to reflect events or circumstances arising after the date of such statement, or (ii) the important factors that could cause our future results to differ materially from historical results or trends, results anticipated or planned by us, or which are reflected from time to time in any forward-looking statement.

There are several important factors that could cause our future results to differ materially from historical results or trends, results anticipated or planned by us, or results that are reflected from time to time in any forward-looking statement. Some of these important factors, but not necessarily all important factors, are included in this Management's Discussion and Analysis of Financial Condition and Results of Operations and in the section "Risk Factors" in our annual report on Form 10-K for the year ended December 31, 2012 filed with the SEC on March 28, 2013.

We own or have rights to certain trademarks that we used in connection with our business or products, including, but not limited to, Dolphin . Other than this trademark, this report also makes reference to trademarks and trade names of other companies.

On June 12, 2012, we effected a 1-for-4 reverse stock split of our common stock and corresponding decrease in the number of authorized shares of common stock. All historical share amounts and share information presented in the financial statements and notes have been proportionally adjusted to reflect the impact of this reverse stock split, including but not limited to basic and diluted weighted-average shares issued and outstanding. Certain reclassifications have been made to the prior periods' financial statements to conform to the current period's presentation.

On March 28, 2013, we sold a portion of our subsidiary, Dolphin Products Pty Limited, business dedicated to the manufacture and sale of non-gaming plastic products, mainly automotive parts. Revenues of these non-gaming products and our gaming chips and plaques were previously consolidated under the reporting segment "Other Products." After the sale, we renamed "Other Products" as "Gaming Products" and this segment now comprises our gaming chips and plaques operations and, beginning in October 2013, the distribution of third-party gaming products to select locations in Indo-China and the Philippines. All related historical revenues and expenses from the sold non-gaming assets have been reclassified as discontinued operations.

## Overview

We are a gaming company focused on capitalizing on the growth opportunities in emerging gaming markets of Asia. We generate revenue in two principal ways: gaming operations and gaming product sales. Our gaming operations comprise slot operations in Cambodia and the Philippines and the development and operation of regional style casinos and gaming venues under our Dreamworld brand in Indo-China. Our gaming products comprise the manufacture and sale of gaming chips and plaques under our Dolphin brand and the distribution of gaming products in select markets for third-party suppliers.

### **Entertainment Gaming Asia Business Operations**

During the nine-month period ended September 30, 2013, we expanded gaming operations with the opening of a new property, Dreamworld Club (Poipet). In addition, we completed the restructuring of our legacy businesses with the divestiture of a low-margin, non-gaming business and relocation and repositioning of the gaming products division.

Our consolidated revenue for the three-month and nine-month periods ended September 30, 2013 was approximately \$5.7 million and \$18.2 million, of which revenue from the gaming operations and gaming products segments comprised 80% and 20% and 85% and 15%, respectively, of consolidated revenue. This compares to consolidated revenue of approximately \$6.2 million and \$17.9 million for the three-month and nine-month periods ended September 30, 2012, of which revenue from the gaming operations and gaming products segments comprised 72% and 28% and 82% and 18%, respectively, of consolidated revenue.

We have developed our business model with the goal of creating growth potential and the ability to generate quality recurring cash flow. We believe that this model combined with our established presence and strong relationships in our markets provide us a solid foundation from which to capitalize on the growth opportunities in our target markets in Asia. We seek to improve revenue by making our gaming properties quality leaders in their markets by providing our customers with their favorite games, superior customer service and attractive and comfortable surroundings. We seek to increase and expand our diversified revenue streams through our gaming products division. We seek to improve margins by focusing on operational efficiency and cost control. Our long-term strategy includes responsible investment in improving and maintaining our existing operations and selectively securing new projects that will serve to enhance our presence and build deeper brand equity in the Dreamworld name in our markets. We intend to implement these strategies in ways that we believe will benefit our shareholders.

### ***Slot Operations***

Our slot operations involve the leasing of electronic gaming machines (“EGMs”) on a revenue sharing basis to gaming establishments. We utilize our operational experience, established market presence and key relationships to identify and develop new gaming venues, acquire EGMs, casino management systems and other gaming peripherals directly from manufacturers, dealers and suppliers and install the same in our contracted venues. In addition, we assist the venue owners in brand-building and marketing promotions.

For certain of our slot contracts, such as with NagaWorld Resorts, Sokha Hotels and Resorts (“Sokha”) and Dreamworld Club (Poipet) in Cambodia, we also function as a manager of the EGM operations. In these venues, we either jointly manage with the relevant casino owner, as is the case with NagaWorld Resorts and Sokha, or exclusively manage, as is the case with Dreamworld Club (Poipet), the slot floor operations and design marketing programs and slot promotions for our designated gaming spaces. We also hire, train and manage the floor staff and set high expectations on the level of customer service.

As of September 30, 2013, our slot operations were located in two countries, Cambodia and the Philippines, and totaled 1,698 EGM seats in operation in a total of six venues. In Cambodia, we had a total of 1,133 EGM seats in operation in three venues. In the Philippines, we had a total of 565 EGM seats in operation in three venues. Due to our ongoing efforts to improve the returns for the slot operations, we seek to selectively add new venues and refine existing operations to focus on those venues with the greatest potential.



In Cambodia, our slot operations largely focus on operating a substantial portion of the gaming machine area in prime casino floor locations at NagaWorld, a wholly-owned subsidiary of Hong Kong listed NagaCorp Ltd. (HKSE: 3918). NagaWorld is a premier luxury destination gaming resort and the only licensed full service casino in a designated area around the capital city of Phnom Penh. In December 2008, we established a relationship with NagaCorp to place EGMs on a revenue sharing or participation basis at NagaWorld and jointly operate those EGMs with them. Due to our successful performance, we subsequently amended our contract and expanded our relationship with NagaWorld to 670 EGM seats under contract. Our slot operations in NagaWorld are a primary contributor to our slot revenue and cash flow.

Our current operations in NagaWorld are governed under the Machines Operation and Participation Consolidation Agreement dated December 31, 2009, which was subsequently amended on May 25, 2010. Under the terms of these agreements, we and NagaWorld control the operation of a total of 670 of our EGMs, including floor staff and respective audit rights. We and NagaWorld split the win per unit per day from all the 670 EGMs and certain operating costs related to marketing and floor staff on a respective basis of 25%/75%. Win per unit per day from all the 670 EGMs are settled and our share is distributed daily to us. The contract term is six years commencing from March 1, 2010.

Our slot operations in Cambodia also include Thansur Bokor Highland Resort, a casino resort developed by leading Cambodian hotelier, Sokha, in a tourist area of the Kampot Province. The resort officially opened in May 2012 but portions of the initial phase of the property including the entertainment complex were not completed until early 2013. To-date, we have placed approximately 200 EGMs in this venue. Under the terms of the agreement, we have the ability to place up to 250 EGM seats and jointly manage these slot operations in the resort. We and Sokha split the gross win and certain operating expenses for the placed EGMs on a respective basis of 27/73%. The contract duration is five years commencing from May 2012. This project expanded our gaming operations in the Indo-China region with a prominent partner with multiple hotel and resort properties in Cambodia.

Our most recent slot operations project in Cambodia is Dreamworld Club (Poipet). Unlike our other slot operations, we solely developed and operate this property. Dreamworld Club (Poipet) is a standalone slot hall with approximately 300 EGM seats, which we developed as an extension of the existing casino owned by a local company. It is prominently located in the established gaming market of Poipet in the Banteay Meanchey Province of Northwestern Cambodia near the Thailand border. Dreamworld Club (Poipet) soft opened in March 2013 and the official grand opening was held in May 2013.

Dreamworld Club (Poipet) operates under a machine operation and participation agreement with a local partner that owns and operates an existing casino in Poipet. Under the terms of the agreement, the local partner allocated part of its land with an area of approximately 16,000 square feet to us to develop and construct, at our own design, budget and cost, the slot venue. We and the local partner split the win per unit per day from all the EGMs placed by us at Dreamworld Club (Poipet) and certain operating costs related to marketing and floor staff on a respective basis of 40%/60%. The initial project term is five years beginning from the commercial launch of the slot hall in 2013 with an option to renew for an additional five years subject to the achievement of certain financial milestones during the initial five-year period.

Total capital expenditures for Dreamworld Club (Poipet), which principally included the development and construction of the facility and gaming equipment, were approximately \$7.5 million, including approximately \$5.0 million to source top-of-the-line EGMs. We are responsible for all capital expenditures for Dreamworld Club (Poipet) and those expenditures have been funded through our internal cash resources.

In the Philippines, our slot operations comprise three venues in the greater Manila area. For these three venues, our share of the net win per unit per day ranges from 15% to 35%. The typical initial term for these contracts is five years with renewal options. The strong Philippine economy, the interest of the government to expand gaming in the country

and close geographic proximity to major markets in Asia, among other reasons, has led to increased development of major casinos in the market. While this results in increasing competition for our venues in this market, we believe we have a solid customer base as our venues there tend to attract locals in their respective areas.

We remain focused on enhancing returns on assets in the Philippines through efforts to implement, with the support of our venue owner partners, targeted marketing programs to maintain and expand our local customer base and to strategically manage the machine mix in our contracted venues. Also, we proactively solicit feedback from our customers on such matters as gaming offerings, customer service, entertainment and atmosphere and, with the support of our venue owner partners, seek to make improvements where possible to address customer preferences and strengthen their loyalty.

In addition, we continue to selectively pursue additional slot operations projects in our target markets. Total company-wide EGM placements can fluctuate due to our strategic efforts to optimize average daily net wins. In the event that the EGM performance at a contracted venue does not meet our original expectations, and to the extent permitted under the terms of the relevant contracts, we may discuss with the venue owner withdrawing all or a portion of our EGMs from such venue for future redeployment in new or existing venues with better performance prospects.

### *Casino Operations*

Our casino operations presently comprise one property, Dreamworld Casino (Pailin) which opened in May 2012. This property is located in the emerging gaming market in the Pailin Province of Northwestern Cambodia next to the Thailand border.

During the last several months, we have repositioned these operations with a goal to improve the earnings performance. Under the new operating model, we have leased 10 gaming tables to a third-party operator. This allows us to leverage the operator's existing player network in Thailand providing us with increased quality player traffic. In addition, in early November 2013, we added semi-live multi-game electronic gaming tables with 30 seats, increasing the EGM base from 58 to 88 seats. We placed these machines on a revenue sharing basis resulting in minimal capital investment to us. We believe these changes to the operating model will provide recurring income and the ability to substantially reduce operating costs.

Dreamworld Casino (Pailin) is constructed on land leased from a local land owner and, in consideration, the land owner is entitled to receive monthly rental fee in the amount of \$5,000 and 20% of the profit before depreciation (the total gross revenue of the casino less any payouts paid to customers, operating expenses, and gaming and non-gaming taxes on the casino's revenue). The initial lease term is 20 years, commencing in September 2011 and is subject to renewal by the parties in writing.

The initial phase of Dreamworld Casino (Pailin) measures approximately 16,000 square feet. The local partner also owns property adjacent to Dreamworld Casino (Pailin) measuring nearly 250,000 square feet. We had an option to lease this adjacent property when it became available to develop additional phases of the Dreamworld Casino (Pailin). The adjacent property became available for lease during the three-month period ended September 30, 2013 and we declined the option to lease this property.

Total capital expenditures for the initial phase of Dreamworld Casino (Pailin) were approximately \$2.5 million, which was paid solely by us from internal cash resources.

In addition to Dreamworld Casino (Pailin), we have another casino development project in the pipeline, Dreamworld Casino (Kampot). In partnership with a local land owner, we intend to develop a small casino in the Kampot Province of Southwestern Cambodia near the Vietnam border on land owned by the local partner. Depending on demand and the availability of capital, there is the potential to add, at a future date, additional casino floor space and equipment as well as complementary facilities such as hotel rooms, a spa and other entertainment amenities.

Under the terms of the partnership, the local partner will lease us the land for a period of 25 years for an annual fee of \$1 and we will provide funding for all development, construction and pre-opening costs for the Dreamworld Casino (Kampot) and all necessary gaming equipment. We and the local partner will split Dreamworld Casino (Kampot)'s profit before depreciation (the total gross revenue of the casino less any payouts paid to customers, operating expenses, and gaming and non-gaming taxes on the casino's revenue) on a respective basis of 60%/40%. Total capital expenditures for the initial phase of Dreamworld Casino (Kampot) are projected to be approximately \$1.2 million as the EGMs will be sourced from existing inventory.

The development timeline for Dreamworld Casino (Kampot) is under review. We have deferred construction of this project until the market has demonstrated a more developed player base and previously planned infrastructure improvements in the area are in place.

We also own a parcel of land with total area of approximately seven acres in the Takeo Province of Cambodia near the Vietnam border and were granted in-principle approval to build and open a casino-hotel in the Takeo Province by the Cambodian government. We do not expect to commit significant capital to the project on this land until the market has

demonstrated a more developed player base.

We continue to selectively pursue additional casino development projects that will enable us to expand our market presence and increase brand equity in our Dreamworld name in the Indo-China region. We seek markets that offer an established player base and projects that would provide meaningful scale to our operations. While there is no guarantee we will be successful in signing new projects, we aim to secure projects that will add meaningful scale to our gaming operations and provide the opportunity for higher net returns.

### ***Gaming Products***

During the nine-month period ended September 30, 2013, we successfully completed our plans to restructure our legacy operations. On March 28, 2013, we completed the sale of the non-gaming manufacturing portion of the operations in a management-led buyout for total consideration of AUD350,000. In connection with the sale, in March 2013, we commenced the relocation of our manufacturing facilities for the gaming products portion of the business, namely gaming chips and plaques, to Hong Kong from Australia. Commercial operation of the new Hong Kong facilities, which are also the new home of our corporate headquarters, began in May 2013.

These actions not only enabled us to exit a non-core, low-margin business but also provide the opportunity to enhance the profitability of our gaming products division through lower cost labor, elimination of redundant support functions, further automation and improved R&D capabilities, as well as to better penetrate and service the growing Asian gaming markets. In addition, it improves our ability to expand our product mix to include other gaming products, which could add incremental revenue streams and further enhance our competitive positioning.

We recorded one-time cash costs associated with the above sale and relocation, which included severance and relocation charges, of approximately \$1.3 million. These costs were all incurred during the three-month period ended March 31, 2013 and were funded from our available working capital.

As part of our strategy to fully leverage our relationships in Asia and existing infrastructure in both Indo-China and the Philippines, we have been seeking opportunities to expand the gaming products division beyond gaming chips and plaques with the distribution of third-party gaming products. In September 2013, we signed a distribution agreement with LT Game Limited, which grants us the exclusive right to market and sell LTG gaming products to designated casinos and gaming venues within Cambodia, Vietnam and the Philippines. The initial duration of the agreement is six months in Cambodia and Vietnam and one year in the Philippines. Subject to the achievement of certain sales targets, we are entitled to renew the agreement for successive one year periods under the same terms. We are actively seeking additional distribution opportunities to expand our product mix.

With a quality product line, streamlined operating structure, solid existing customer base and high-security production facilities in close proximity to the growing Asian gaming markets, we believe that we have all the right and necessary elements to best serve our target markets and are poised to benefit from the major casino development anticipated over the next several years in Asia. While we anticipate continued uneven order flow on a quarter to quarter basis, our efforts are expected to result in overall improved recurring revenue and earnings growth potential for these operations.

### Results of Operations for the Three-Month and Nine-Month Periods Ended September 30, 2013 and 2012

The following is a schedule summarizing operating results on a consolidated basis and separately by each of our two operating segments, gaming operations and gaming products, for the three-month and nine-month periods ended September 30, 2013 and 2012.

On February 22, 2013, we entered into a share sale agreement pursuant to which we agreed to sell the portion of our subsidiary, Dolphin Products Pty Limited (“Dolphin Australia”), business dedicated to the manufacture and sale of non-gaming plastic products, mainly automotive parts. The sale closed on March 28, 2013. All historical revenues and expenses associated with our non-gaming plastic products operations for the periods ended September 30, 2013 and 2012 have been reclassified as discontinued operations.

(amounts in thousands, except per share data)	Three-Month Periods Ended September 30,		Nine-Month Periods Ended September 30,	
	2013	2012	2013	2012
Total:				
Revenues	\$ 5,652	\$ 6,198	\$ 18,200	\$ 17,862
Gross profit	\$ 1,488	\$ 1,713	\$ 4,736	\$ 7,028
Gross margin percentage	26	% 28	% 26	% 39
Adjusted EBITDA from continuing operations (1)	\$ 1,798	\$ 2,124	\$ 5,545	\$ 7,949
Operating (loss)/income from continuing operations	\$ (281)	\$ (105)	\$ (766)	\$ 1,117
Net (loss)/income from continuing operations	\$ (309)	\$ (103)	\$ (1,022)	\$ 1,207

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Net (loss)/income	\$ (309)	\$ 43	\$ (3,102)	\$ 1,499
Basic and diluted (loss)/earnings per share from continuing operations	\$ (0.01)	\$	\$ (0.03)	\$ 0.04
Weighted average common shares outstanding				
Basic	30,025	29,926	30,024	29,915
Diluted	30,025	29,926	30,024	30,793
Gaming operations:				
Revenues	\$ 4,546	\$ 4,480	\$ 15,505	\$ 14,634
Gross profit	\$ 1,513	\$ 1,521	\$ 5,213	\$ 6,556
Gross margin percentage	33 %	34 %	34 %	45 %
Gaming products:				
Revenues	\$ 1,106	\$ 1,718	\$ 2,695	\$ 3,228
Gross (loss)/profit	\$ (25)	\$ 192	\$ (477)	\$ 472
Gross margin percentage	NM	11 %	NM	15 %

(1) “Adjusted EBITDA” is net (loss)/income from continuing operations before interest, taxes, depreciation, amortization, stock-based compensation, and other non-cash operating income and expenses. Adjusted EBITDA is presented exclusively as a supplemental disclosure because our management believes that it is widely used to measure the performance, and as a basis for valuation, of gaming companies. Our management uses Adjusted EBITDA as a measure of the operating performance of its segments and to compare the operating performance of its operations with those of its competitors. We also present Adjusted EBITDA because it is used by some investors as a way to measure a company’s ability to incur and service debt, make capital expenditures and meet working capital requirements. Gaming companies have historically reported EBITDA as a supplement to financial measures in accordance with generally accepted accounting principles in the United States (“GAAP”). Adjusted EBITDA should not be considered as an alternative to operating income as an indicator of our performance, as an alternative to cash flows from operating activities as a measure of liquidity, or as an alternative to any other measure determined in accordance with GAAP. Unlike net income/(loss), Adjusted EBITDA does not include depreciation or interest expense and, therefore, does not reflect current or future capital expenditures or the cost of capital. We compensate for these limitations by using Adjusted EBITDA as only one of several comparative tools, together with GAAP measurements, to assist in the evaluation of operating performance. Such GAAP measurements include operating income, net income, cash flows from operations and cash flow data. We have significant uses of cash flows, including capital expenditures, interest payments, debt principal repayments, taxes and other non-recurring charges, which are not reflected in Adjusted EBITDA. Our calculation of Adjusted EBITDA may be different from the calculation methods used by other companies and, therefore, comparability may be limited.

A reconciliation of EBITDA from continuing operations, as adjusted, to the net (loss)/income from continuing operations is provided below.

(amounts in thousands)	Three-Month Periods Ended September 30,		Nine-Month Periods Ended September 30,	
	2013	2012	2013	2012
Net (loss)/income from continuing operations	\$ (309)	\$ (103)	\$ (1,022)	\$ 1,207
GAAP				
Interest expense	1	20	5	109
Interest income		(4)	(4)	(32)
Income tax (benefit)/expenses	(11)	34	38	124
Depreciation and amortization	2,008	2,014	5,974	5,783
Stock-based compensation expenses	109	123	554	675
Impairment of assets		42		114
Gain on dispositions		(2)		(31)
EBITDA from continuing operations, as adjusted	\$ 1,798	\$ 2,124	\$ 5,545	\$ 7,949

Total revenue decreased approximately \$546,000 to \$5.7 million for the three-month period ended September 30, 2013 compared to approximately \$6.2 million in the same period of the prior year due to lower revenue from gaming products partially offset by higher revenue from gaming operations. Gaming products contributed \$1.1 million to consolidated revenue driven by existing customer reorders compared to the prior year period, which benefited from a large one-time order of \$1.6 million related to the casino rebranding of an existing customer. Revenue from gaming operations increased primarily as a result of incremental revenue from Dreamworld Casino (Pailin), which opened in May 2012, and Dreamworld Club (Poipet), which officially opened in May 2013 partially offset by lower slot operations revenue primarily from NagaWorld and the Philippines, as described in greater detail below.

Gross profit decreased approximately \$225,000 to \$1.5 million for the three-month period ended September 30, 2013 compared to approximately \$1.7 million in the same period of the prior year. The decrease was primarily due to lower slot operations revenue for NagaWorld and lower revenue and production efficiencies for the gaming products division, partially offset by higher gross profit for the Philippines slot operations primarily due to lower depreciation expense as a result of the increase in fully depreciated gaming assets during the three-month period ended September 30, 2013.

Operating loss from continuing operations increased approximately \$176,000 to \$281,000 for the three-month period ended September 30, 2013 compared to approximately \$105,000 in the same period of the prior year primarily due to the lower gross profit explained above partially offset by slightly lower operating expenses.

Net loss from continuing operations increased approximately \$206,000 to \$309,000 for the three-month period ended September 30, 2013 compared to approximately \$103,000 in the same period of the prior year primarily as a result of the higher operating loss explained above and foreign currency losses, which were approximately \$39,000 compared to gains of approximately \$55,000 in the prior year period. Net loss increased approximately \$352,000 to a loss of \$309,000 from the three-month period ended September 30, 2013 compared to net income of approximately \$43,000 in the same period of the prior year. The net income for the three-month period ended September 30, 2012 included approximately \$146,000 in net income from discontinued operations.



Total revenue increased approximately \$338,000 to \$18.2 million for the nine-month period ended September 30, 2013 compared to approximately \$17.9 million in the same period of the prior year due to higher revenue from gaming operations partially offset by lower revenue from gaming products. Revenue from gaming operations increased primarily as a result of increased revenue from Dreamworld Casino (Pailin) and incremental revenue from Dreamworld Club (Poipet) partially offset by lower revenue from slot operations, as described in greater detail below. Revenue from gaming products decreased as a result of lower production volumes during the 2013 period primarily due to the reason stated above and the shortened production period due to the strategic relocation of the manufacturing facilities from Australia to Hong Kong, which commenced in March 2013 and was completed in May 2013.

Gross profit decreased approximately \$2.3 million to \$4.7 million for the nine-month period ended September 30, 2013 compared to approximately \$7.0 million in the same period of the prior year driven by declines in both divisions. For gaming products, gross profit declined due to lower production volumes and higher costs primarily related to relocation to and initial set up and ramp up of the new manufacturing facilities in Hong Kong. Gaming operations gross profit declined due to lower slot operations revenue from NagaWorld, as described in greater detail below, incremental operating costs for Dreamworld Club (Poipet) and higher gross margin loss for the casino operations given Dreamworld Casino (Pailin) operated for the full nine-month period in 2013 compared to a less than five-month period for the same period in 2012. The decline in gaming operations gross profit was partially offset by higher gross profit for the Philippines slot operations for the reason stated above.

Operating loss from continuing operations increased approximately \$1.9 million to a loss of \$766,000 for the nine-month period ended September 30, 2013 compared to operating income from continuing operations of approximately \$1.1 million in the same period of the prior year. The increase in operating loss from continuing operations was primarily a result of the lower gross profit explained above partially offset by a decrease in operating expenses.

Net loss from continuing operations increased approximately \$2.2 million to a loss of \$1.0 million for the nine-month period ended September 30, 2013 compared to net income from continuing operations of approximately \$1.2 million in the same period of the prior year. The increase in net loss from continuing operations was primarily a result of the operating loss explained above and foreign currency losses of approximately \$228,000 compared to gains of approximately \$269,000 in the prior year period. Net loss increased approximately \$4.6 million to a loss of \$3.1 million for the nine-month period ended September 30, 2013 compared to net income of approximately \$1.5 million in the same period of the prior year. The net loss for the nine-month period ended September 30, 2013 included a net loss from discontinued operations of approximately \$2.1 million compared to net income from discontinued operations of approximately \$292,000 in the prior year period.

## Gaming Operations

Revenues from gaming operations consisted of slot and casino development operations as detailed below.

(amounts in thousands, except per unit data)	Three-Month Periods Ended September 30,		Nine-Month Periods Ended September 30,	
	2013	2012	2013	2012
Net revenue to the Company				
Cambodia slot operations (1)	\$ 3,327	\$ 3,269	\$ 10,545	\$ 11,140
Philippines slot operations	787	871	2,527	2,941
Net revenue from slot operations	4,114	4,140	13,072	14,081
Dreamworld Casino (Pailin)	432	340	2,433	553
Consolidated total	\$ 4,546	\$ 4,480	\$ 15,505	\$ 14,634

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Slot operations average net win/unit/  
day (2)

Cambodia slot operations	\$ 126	\$ 175	\$ 150	\$ 208
Philippines slot operations	\$ 73	\$ 74	\$ 78	\$ 73
Consolidated total	\$ 108	\$ 132	\$ 124	\$ 145

	September 30, 2013	2012
EGM seats in operation		
Cambodia slot operations(1)	1,133	839
Philippines slot operations	565	581
EGM seats in slot operations	1,698	1,420
Dreamworld Casino (Pailin)	58	50
Consolidated total	1,756	1,470

- (1) Includes Dreamworld Club (Poipet), which operates under a machine operation and participation agreement. Dreamworld Club (Poipet) soft opened on March 28, 2013 and the grand opening was on May 9, 2013.
- (2) Average net win figures (“WUD”) exclude EGM seats in operation during venue soft launch opening periods, if applicable, and include revenue recognized on a cash basis in the calculation of WUD for venues for which revenues are recognized on a cash basis. During the three-month period ended September 30, 2013, no EGM seats were excluded from the WUD calculation. During the nine-month period ended September 30, 2013, one venue in Cambodia operated during a soft launch and during the three-month and nine-month periods ended September 30, 2012, one venue in Cambodia operated during a soft launch and one venue in the Philippines recognized revenue on a cash basis. There were no material differences to average WUD figures for the above-mentioned periods had these seats been included in the WUD calculations.

Revenue from gaming operations increased approximately \$66,000 to \$4.5 million for the three-month period ended September 30, 2013 compared to approximately \$4.5 million in the same period of the prior year. The increase was primarily a result of incremental revenue from Dreamworld Club (Poipet), which officially opened in May 2013, and an increase in revenue from Dreamworld Casino (Pailin), which was largely offset by lower revenue from the remaining slot operations.

Slot operations contributed approximately \$4.1 million to total gaming revenue for the three-month period ended September 30, 2013 essentially unchanged with the prior year period. Revenue from the Cambodia slot operations increased approximately \$58,000 to \$3.3 million for the three-month period ended September 30, 2013 compared to \$3.3 million in the same period in the prior year as incremental revenue for Dreamworld Club (Poipet) partially offset a revenue decline for NagaWorld and, to a lesser extent, Thansur Bokor during the quarter.

Dreamworld Club (Poipet) posted sequential quarterly improvement for the three-month period ended September 30, 2013 and we are focused on continuing to ramp up these operations with targeted marketing programs focused on building and growing a quality player base. Slot operations in NagaWorld contributed \$3.0 million in revenue for the three-month period ended September 30, 2013 compared to \$3.2 million in the prior year period primarily due to lower player traffic as a result of events related to the national elections held in July 2013.

Average net win per machine for the Cambodia slot operations decreased \$49 to \$126 for the three-month period ended September 30, 2013 compared to \$175 for the same period of the prior year. The decline in average net win per machine was primarily due to the addition of EGMs in Dreamworld Club (Poipet) in the WUD calculation as this venue has relatively lower average net win per machine and a decline in NagaWorld and Thansur Bokor average net wins during the three-month period ended September 30, 2013.

Revenue from the Philippines slot operations decreased approximately \$84,000 to \$787,000 for the three-month period ended September 30, 2013 compared to \$871,000 in the same period of the prior year primarily due to a lower installed machine base, higher jackpot payouts and increased competition due to the opening of a new casino resort in Manila earlier in 2013.

Average net win per machine for the Philippines slot operations declined slightly to \$73 for the three-month period ended September 30, 2013 compared to \$74 in the prior year period mainly due to the lower installed base with better performing machines.

We continue our efforts to improve overall returns for our operations in the Philippines. These efforts include: implementing, with the support of our venue owner partners, targeted marketing programs and proactive machine mix management. With increasing competition from the development of major integrated casino resorts in Manila, we are focused on improving player loyalty through marketing programs and providing a wide range of preferred gaming machines and superior services to the local customer bases.

Dreamworld Casino (Pailin) contributed approximately \$432,000 to gaming operations revenue for the three-month period ended September 30, 2013 compared to \$340,000 in the same period of the prior year and \$907,000 for the three-month period ended June 30, 2013. The sequential decline was due to decreased player traffic levels for the three-month period ended September 30, 2013 as a result of our efforts to reduce the use of high-cost, mass market tour groups.

We are focused on improving the financial performance of Dreamworld Casino (Pailin) and during the three-month period ended September 30, 2013, we began to implement a new lower-cost operating plan, which we believe will improve bottom-line performance. Under the new operating model, we have leased 10 gaming tables to a third-party operator. We believe this will allow us to leverage the operator's existing player network in Thailand and provide us with increased quality player traffic. In addition, in early November 2013, we added semi-live multi-game electronic gaming tables with 30 seats, increasing the EGM base from 58 to 88 seats. We placed these machines on a revenue sharing basis resulting in minimal capital investment. These changes to the operating model provide us quality recurring income and the ability to substantially reduce operating costs. While the plan was not in full effect during the three-month period ended September 30, 2013, we reduced cash operating expenses approximately \$519,000 to \$703,000 compared to approximately \$1.2 million for the three-month period ended June 30, 2013. Despite the quarterly sequential revenue decline, these efforts served to narrow the operating loss for Dreamworld Casino (Pailin).

Gross profit from gaming operations was approximately \$1.5 million for the three-month period ended September 30, 2013 essentially unchanged from the same period of the prior year as lower revenue from the NagaWorld slot operations and higher operating costs for Dreamworld Casino (Pailin) were principally offset by lower depreciation expense for the Philippines slot operations for the three-month period ended September 30, 2013. Cost of gaming operations for the three-month period ended September 30, 2013 included approximately \$1.2 million of depreciation on gaming and property equipment, \$613,000 amortization of casino contracts, \$63,000 amortization of other gaming related intangibles and \$1.2 million of other operating costs.

Revenue from gaming operations increased approximately \$871,000 to \$15.5 million for the nine-month period ended September 30, 2013 compared to approximately \$14.6 million in the same period of the prior year. The increase in revenue was primarily a result of Dreamworld Casino (Pailin), which contributed revenue of approximately \$2.4 million for the nine-month period ended September 30, 2013 compared to approximately \$553,000 from the opening in May 2012 until September 30, 2012, and incremental revenue from Dreamworld Club (Poipet). The increase in gaming operations revenue was partially offset by lower slot operations revenue from NagaWorld and the Philippines.

Slot operations contributed approximately \$13.1 million to total gaming revenue for the nine-month period ended September 30, 2013 compared to approximately \$14.1 million for the same period in the prior year period. Revenue from the Cambodia slot operations decreased approximately \$595,000 to \$10.5 million for the nine-month period ended September 30, 2013 compared to \$11.1 million for the same period in the prior year primarily as a result a decrease in revenue from the NagaWorld slot operations partially offset by incremental revenue for Dreamworld Club (Poipet). NagaWorld slot operations revenue was negatively impacted by reduced player traffic in the three-month period ended September 30, 2013 for the reasons stated above and lower player traffic in February 2013 due to an observed, week-long official mourning period for the deceased former King of Cambodia during the beginning of the month and a several-day strike by NagaWorld workers at the end of the month.

Average net win per machine for the Cambodia slot operations decreased \$58 to \$150 for the nine-month period ended September 30, 2013 compared to \$208 for the same period of the prior year. The decline in average net win per machine was primarily due to the addition of EGMs in Dreamworld Club (Poipet) and Thansur Bokor in the WUD calculation as these venues have relatively lower average net win per machine and a decline in NagaWorld average net win during the nine-month period ended September 30, 2013.

Revenue from the Philippines slot operations decreased approximately \$414,000 to \$2.5 million for the nine-month period ended September 30, 2013 compared to approximately \$2.9 million in the same period of the prior year primarily due to the lower machine base and increased competition in the market. However, average net win per machine improved \$5 to \$78 for the nine-month period ended September 30, 2013 compared to \$73 in the same period of the prior year for the same reasons as stated above.

Gross profit from gaming operations decreased approximately \$1.3 million to \$5.2 million for the nine-month period ended September 30, 2013 compared to approximately \$6.6 million in the same period of the prior year primarily due to lower revenue for the slot operations, incremental operating costs for Dreamworld Club (Poipet) and higher gross margin loss for the casino operations as Dreamworld Casino (Pailin) operated for a nine-month period in 2013 compared to a less than five-month period for the same period in 2012. Cost of gaming operations for the nine-month period ended September 30, 2013 included approximately \$3.6 million of depreciation on gaming and property equipment, \$1.9 million of amortization of casino contracts, \$189,000 of amortization of other gaming related intangibles and \$4.7 million of other operating costs.

As of September 30, 2013, we had a total of 2,027 EGM seats of which 271 were held in inventory and 1,756 were in operation. Of the 1,756 EGM seats in operation, 1,191 were in four venues in Cambodia (including Dreamworld Casino (Pailin) and Dreamworld Club (Poipet)) and 565 were in three venues in the Philippines.

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(amounts in thousands, except per unit data)	September 30, 2013		December 31, 2012	
	Units	Carrying Value	Units	Carrying Value
EGMs and systems used in operations (1) (2)	1,756	\$ 8,978	1,457	\$ 5,377
EGMs and systems held for future use	271	297	455	4,347
Total EGMs and systems	2,027	\$ 9,275	1,912	\$ 9,724

(1) EGMs and systems used in operations as of September 30, 2013 and December 31, 2012 included 12 EGM seats, which were in operation on a trial basis subject to achieving certain performance objectives prior to acceptance and, as a result, their carrying values were not included.

(2) Includes both slot operations and Dreamworld Casino (Pailin).

Due to our ongoing efforts to improve the returns on our slot operations, we seek to refine the existing operating machine base to focus on those venues with the greatest potential and selectively add new venues. In October 2013, we added 30 EGM seats on a participation basis in Dreamworld Casino (Pailin). In March 2013, we soft opened Dreamworld Club (Poipet) in Cambodia with 166 EGM seats. This venue officially opened in May 2013 with approximately 300 EGM seats. In March 2012, we soft opened Thansur Bokor in Cambodia with 87 EGM seats. This venue officially opened in May 2012 with approximately 200 EGM seats. During the period from May to July 2012, we terminated three contracts, one in Cambodia and two in the Philippines, with a combined total of 273 EGMs seats as these venues were not performing up to expectations.

## Gaming Products

Gaming products revenue, which consisted of gaming chips and plaques sales, decreased approximately \$612,000 to \$1.1 million for the three-month period ended September 30, 2013 compared to approximately \$1.7 million in the same period of the prior year. The three-month period ended September 30, 2013 was comprised solely of reorders from our customer base compared to the three-month period ended September 30, 2012, which included a \$1.6 million one-time order for a large rebranding for an existing customer.

Gross margin loss on gaming products increased approximately \$217,000 to a loss of \$25,000 for the three-month period ended September 30, 2013 compared to gross profit of approximately \$192,000 in the same period of the prior year. The increase in gross loss was mainly due to lower production efficiencies given the ramping up of the new production facilities and further efforts to enhance the production capacity and response time for large orders. As a result, we believe the third quarter of 2013 was not representative of the new cost structure for the Dolphin operations.

Gaming products revenue decreased approximately \$533,000 to \$2.7 million for the nine-month period ended September 30, 2013 compared to approximately \$3.2 million in the same period of the prior year. The decline was due to the reasons stated above and a shortened production period due to the relocation of the production facilities from Australia to Hong Kong in the first half of 2013.

Gross margin loss on gaming products increased approximately \$949,000 to a loss of \$477,000 for the nine-month period ended September 30, 2013 compared to a profit of approximately \$472,000 in the same period of the prior year. The increase in gross margin loss was mainly due to the reasons stated above and the relocation and set up of the manufacturing facilities, which resulted in lower production volumes and utilization and cost absorption of the facilities and high non-recurring costs of approximately \$166,000, including consultants, personnel training and manning costs associated with trial runs and equipment installation, for the three-month period ended June 30, 2013. In addition, this division incurred higher labor costs in the three-month period ended March 31, 2013 as a result of increased overtime by the Australian workers due to the expedited fulfillment of orders ahead of the relocation of the plant and absenteeism following the announcement of the relocation of the gaming products business.

As of September 30, 2013, the gaming chips and plaques order backlog was approximately \$1.3 million in revenue.

## Operating Expenses

The schedule of expenses on a consolidated basis consisted of the following:

(amounts in thousands)	Three-Month Periods Ended September 30,		Nine-Month Periods Ended September 30,	
	2013	2012	2013	2012
Selling, general and administrative (1)	\$ 1,558	\$ 1,491	\$ 4,614	\$ 4,712
Stock-based compensation expenses	109	123	554	675
Product development expenses	51	87	206	273
Gain on dispositions		(2)		(31)
Depreciation and amortization	51	77	128	168
Impairment of assets		42		114
	\$ 1,769	\$ 1,818	\$ 5,502	\$ 5,911

(1)

Includes cash selling, general and administrative expenses and excludes non-cash selling, general and administrative expenses such as stock-based compensation expense.

### **Selling, General and Administrative Expenses**

Selling, general and administrative expenses increased approximately \$67,000 to \$1.6 million for the three-month period ended September 30, 2013 compared to \$1.5 million in the same period of the prior year. For the three-month period ended September 30, 2013, salaries and wages, insurance, rent, and other expenses increased approximately \$232,000 primarily due to the increased scale of operations and headcount for the gaming operations and gaming products divisions. This increase was partially offset by declines in other areas. Consulting, accounting, travel and entertainment expenses decreased approximately \$8,000 mainly as a result of lower fees for new and completed projects and decreased traveling required in relation to the new gaming projects. Legal, investor relations, utilities, printing and other expenses decreased approximately \$63,000 primarily due to fewer gaming projects and various cost reduction initiatives. Sales commissions decreased approximately \$94,000 primarily due to lower gaming products sales.

Selling, general and administrative expenses decreased approximately \$98,000 to \$4.6 million for the nine-month period ended September 30, 2013 compared to \$4.7 million in the same period of the prior year. For the nine-month period ended September 30, 2013, consulting, accounting, travel and entertainment expenses decreased approximately \$112,000 mainly as a result of lower fees for new and completed projects and decreased traveling required in relation to the new gaming projects. Legal, investor relations, salaries and wages, utilities, printing and other expenses decreased approximately \$291,000 primarily due to fewer gaming projects and various cost reduction initiatives. Sales commissions decreased approximately \$90,000 primarily due to lower gaming products sales. These decreases were partially offset by increases in salaries and wages, insurance, rent, and other expenses, which increased approximately \$395,000 primarily due to increased scale of operations and headcount for the gaming operations and gaming products divisions.



### **Stock-Based Compensation Expense**

Stock-based compensation expense decreased approximately \$14,000 to \$109,000 for the three-month period ended September 30, 2013 compared to approximately \$123,000 in the prior year period primarily due to a decrease in fair value of stock prices during the three-month period ended September 30, 2013 as compared to the prior year period.

Stock-based compensation expense decreased approximately \$121,000 to \$554,000 for the nine-month period ended September 30, 2013 compared to approximately \$675,000 in the same period of the prior year primarily due to the same reason stated above.

### **Gain on Disposition of Assets**

There were no dispositions of assets for the three-month period ended September 30, 2013. Gain on disposition of assets was \$2,000 for the three-month period ended September 30, 2012, which related to the sale of non-performing EGMs and systems during the period.

There were no dispositions of assets for the nine-month period ended September 30, 2013. Gain on disposition of assets was \$31,000 in the same period of the prior year primarily due to the same reason as stated above.

### **Product Development Expenses**

Product development expenses decreased approximately \$36,000 to \$51,000 for the three-month period ended September 30, 2013 compared to approximately \$87,000 in the prior year period primarily due to reduced product development efforts for gaming products in the early operation of the new production facilities during the three-month period ended September 30, 2013.

Product development expenses decreased approximately \$67,000 to \$206,000 for the nine-month period ended September 30, 2013 compared to approximately \$273,000 in the same period of the prior year primarily due to the reason stated above and reduced development activities during the relocation on the gaming products manufacturing facilities in the three-month period ended June 30, 2013.

### **Depreciation and Amortization Expenses**

Total depreciation and amortization expenses decreased approximately \$26,000 to \$51,000 for the three-month period ended September 30, 2013 compared to approximately \$77,000 in the prior year period primarily as a result of an increase in fully depreciated fixed assets for gaming operations.

Total depreciation and amortization expenses decreased by approximately \$40,000 to \$128,000 for the nine-month period ended September 30, 2013 compared to approximately \$168,000 in the same period of the prior year for the same reason as stated above.

### **Impairment of Assets**

There were no impairments of assets for the three-month and nine-month periods ended September 30, 2013 compared to approximately \$42,000 and \$114,000, respectively, in the same periods of the prior year primarily as a result of the impairment of non-redeployable EGMs related to the closure of non-performing venues during 2012.

### **Other Income/(Expenses)**

Three-Month Periods Ended September 30,    Nine-Month Periods Ended September 30,

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(amounts in thousands)	2013	2012	2013	2012
Interest expense and finance fees	\$ (1)	\$ (20)	\$ (5)	\$ (109)
Interest income		4	4	32
Foreign currency (losses)/gains	(39)	55	(228)	269
Other	1	(3)	11	22
Total	\$ (39)	\$ 36	\$ (218)	\$ 214

**Interest Expense and Finance Fees**

Interest expense and finance fees decreased approximately \$19,000 to \$1,000 for the three-month period ended September 30, 2013 compared to approximately \$20,000 in the same period of the prior year primarily due to the full repayment of notes payable to a related party in December 2012.

Interest expense and finance fees decreased approximately \$104,000 to \$5,000 for the nine-month period ended September 30, 2013 compared to approximately \$109,000 in the same period of the prior year for the same reason as stated above.

### Interest Income

Interest income decreased approximately \$4,000 to \$NIL for the three-month period ended September 30, 2013 compared to approximately \$4,000 in the same period of the prior year primarily as a result of lower bank balances.

Interest income decreased approximately \$28,000 to \$4,000 for the nine-month period ended September 30, 2013 compared to approximately \$32,000 in the same period of the prior year for the same reason as stated above.

### Foreign Currency Transactions

Foreign currency losses increased approximately \$94,000 to a loss of \$39,000 for the three-month period ended September 30, 2013 compared to gains of approximately \$55,000 for the same period in the prior year. The increase was primarily due to the comparatively higher percentage appreciation in the value of U.S. dollar denominated payables from the Philippines operations, where the functional currency is the Philippine peso. In addition, during the three-month period ended September 30, 2013, the U.S. dollar appreciated compared to the Thai baht, which resulted in an exchange loss for the Cambodia operations' baht cage holdings.

Foreign currency losses increased approximately \$497,000 to a loss of \$228,000 for the nine-month period ended September 30, 2013 compared to gains of approximately \$269,000 for the same period in the prior year for the same reasons as stated above and the appreciation of the U.S. dollar compared to the Australian dollar, which resulted in an exchange loss from the other receivables settlement associated with the sale of the non-gaming Dolphin Australia assets, where the functional currency is the Australian dollar.

### Other

Other expense decreased approximately \$4,000 to income of \$1,000 for the three-month period ended September 30, 2013 compared to expense of approximately \$3,000 in the prior year period primarily due to a one-time expense incurred during the three-month period ended September 30, 2012.

Other income decreased approximately \$11,000 to \$11,000 for the nine-month period ended September 30, 2013 compared to approximately \$22,000 in the prior year period primarily due to the lower miscellaneous income received by the Australian operations in the 2013 period as these operations were disposed of in March 2013.

### Income Tax Provisions

Effective tax rates were approximately (3.4)% and 49.3% and 3.9% and (9.3)% for the three-month and nine-month periods ended September 30, 2013 and 2012, respectively. We continue to review the treatment of tax losses and future income generated by foreign subsidiaries to minimize taxation costs.

The fixed obligation tax arrangement is subject to annual renewal and negotiation. Earlier this year, the Company renewed the fixed obligation tax arrangement for both EGT Cambodia and Dreamworld Casino (Pailin) for 2013. The fixed tax expenses are included in selling, general and administrative expenses.

(amounts in thousands)	Three-Month Periods Ended September 30,		Nine-Month Periods Ended September 30,	
	2013	2012	2013	2012
Income tax provisions	\$ 11	\$ (34)	\$ (38)	\$ (124)

## **FINANCIAL CONDITION**

### **Liquidity and Capital Resources**

As of September 30, 2013, we had total cash and cash equivalents of approximately \$4.6 million and working capital of approximately \$5.1 million. Our cash and working capital during the nine-month period ended September 30, 2013 was positively impacted by the cash received from slot operations but was negatively impacted by expenses associated with casino and gaming development projects, including the construction and opening of Dreamworld Club (Poipet), the purchase of EGMs for gaming operations and the relocation of Dolphin gaming chips and plaques operations from Australia to Hong Kong.

Total capital expenditure for Dreamworld Club (Poipet), which principally included the development and construction of the facility and approximately \$5.0 million for gaming equipment, totaled approximately \$7.5 million. Of the \$7.5 million total expenditure for Dreamworld Club (Poipet), we had incurred approximately \$7.4 million as of September 30, 2013.

As part of our growth strategy for gaming operations, we expect to purchase EGMs to supplement existing inventory and source future targeted deployment plans. As part of our growth strategy for gaming products, we intend to incur costs related to increasing capacity and enhancing production efficiencies for these operations.

We also continue to pursue other new gaming projects, however, there is no guarantee we will successfully secure any of these new projects.

We presently expect that our capital expenditures for the remainder of 2013 based on our current contractual commitments will be approximately \$300,000 to \$350,000. This includes approximately \$150,000 for EGM and systems purchases, upgrades and general maintenance capital for the gaming operations business and approximately \$150,000 to \$200,000 for equipment and systems purchases and general maintenance capital for the gaming products facility.

We presently expect that our capital expenditures for the 2014 fiscal year based on our current contractual commitments will be approximately \$3.0 to \$4.0 million. This includes approximately \$2.0 to \$3.0 million for EGM and system purchases, upgrades and general maintenance for the gaming operations business and approximately \$1.0 million for equipment purchases and general maintenance capital for the gaming products facility.

We anticipate our available working capital, along with cash expected to be generated from operations, will allow us to meet our capital expenditure needs through 2014.

As noted above, however, we continue to pursue additional casino and gaming projects. While there is no guarantee we will be successful in securing new projects, if we were to secure new projects our capital expenditures through 2014 would increase beyond the \$3.0 to \$4.0 million currently contemplated. At this time, we are unable to predict the amount of additional capital expenditures that could be required in 2014 for such potential projects. Where possible, we intend to fund our casino and gaming projects from our cash flow from operations and cash on hand. Further, we will seek to structure the development of these projects in phases to better control and pace the related capital expenditures. However, should we commit to large projects, to the concurrent development of multiple casinos and gaming projects or a new project requires large upfront payments, we may need to acquire additional capital. We would endeavor to obtain any required additional capital from various financing sources including commercial debt financing and the sale of our debt or equity securities. However, there are no commitments or arrangements in place as of the date of this report for receipt of additional capital and there are no assurances we will be able to acquire additional capital if, and when, needed on commercially reasonable terms or at all.

## Cash Flows Summary

(amounts in thousands)	Nine-Month Periods Ended September 30,	
	2013	2012
Cash provided by/(used in):		
Operations	\$ 2,911	\$ 7,443
Investing	(8,463)	(4,771)
Financing		(4,929)
Effect of exchange rate change in cash	(173)	128
	\$ (5,725)	\$ (2,129)

## Operations

Cash provided by operations was approximately \$2.9 million for the nine-month period ended September 30, 2013 compared to \$7.4 million in the same period of the prior year. The decrease in cash provided by operations was primarily due to a decrease of approximately \$1.0 million in slot operations revenue, initial start-up costs for Dolphin

Hong Kong and one-off costs, including severance, relocation charges and contract termination fees, of approximately \$1.3 million associated with the sale of the non-gaming products assets and relocation of the gaming chips and plaques operations from Australia to Hong Kong in the nine-month period ended September 30, 2013. All of the \$1.3 million in one-off costs associated with the sale of the non-gaming products assets and relocation of the gaming chips and plaques operations were incurred in the three-month period ended March 31, 2013. In addition, there was a general reduction in cash of approximately \$1.0 million as part of the settlement of payable balances related to the sale of the Dolphin non-gaming assets.

### ***Investing***

Cash used in investing activities was approximately \$8.5 million for the nine-month period ended September 30, 2013 compared to approximately \$4.8 million in the same period of the prior year. The increase in cash used in investing activities was mainly a result of the capital expenditures related to the construction of Dreamworld Club (Poipet), the new factory renovation and purchase of equipment for the new gaming products manufacturing facility and the purchase of a greater amount of EGMs and related systems in the nine-month period of ended September 30, 2013.

## ***Financing***

Cash used in financing activities was \$NIL for the nine-month period ended September 30, 2013 compared to approximately \$4.9 million in the same period of the prior year. The decrease in cash used in financing activities was primarily a result of the full repayment of the notes payable to EGT Entertainment Holding (see Note 13) in December 2012.

## **CRITICAL ACCOUNTING POLICIES AND ESTIMATES**

Our consolidated financial statements were prepared in conformity with accounting principles generally accepted in the United States. Accordingly, we are required to make estimates incorporating judgments and assumptions we believe are reasonable based on our historical experience, contract terms, observance of known trends in our Company and the industry as a whole, as well as information available from other outside sources. Our estimates affect amounts recorded in the financial statements and actual results may differ from initial estimates.

We consider the following accounting estimates to be the most critical to fully understanding and evaluating our reported financial results. They require us to make subjective or complex judgments about matters that are inherently uncertain or variable. Senior management has discussed the development, selection and disclosure of the following accounting estimates, particularly those considered most sensitive to changes from external factors, with the audit committee of our board of directors.

### **Allowance for Doubtful Accounts Receivable**

As of September 30, 2013, we had net accounts receivable of approximately \$1.4 million, representing 4% of total assets. We specifically analyze the collectability of each account based upon the age of the account, the customer's financial condition, collection history and any other known information, and we provide specific allowances for aged account balances. Revenue is recognized on a cash basis for customers with doubtful accounts receivable. Our allowance for doubtful accounts receivable was approximately \$NIL and \$15,000 as of September 30, 2013 and December 31, 2012.

### **Inventory**

The determination of obsolete or excess inventory requires us to estimate the future demand for our products within specific time horizons, generally one year or less. If we experience a significant unexpected decrease in demand for our products or a higher occurrence of inventory obsolescence because of changes in technology or customer requirements, we could be required to increase our inventory provisions.

### **Gaming Equipment and Property and Equipment**

As of September 30, 2013, we had gaming equipment and property and equipment of approximately \$18.4 million, representing 50% of total assets. We depreciate gaming equipment and property and equipment on a straight-line basis over their estimated useful lives. The estimated useful lives are based on the nature of the assets as well as the current operating strategy and legal considerations such as contractual lives. Future events, such as property expansions, property developments, trends in market demand, new competition, or technology obsolescence, could result in a change in the manner in which we use certain assets and require a change in the estimated useful lives of such assets.

For assets to be held and used, they are reviewed for impairment whenever indicators of impairment exist. If an indicator of impairment exists, we first group assets at the lowest level for which identifiable cash flows are largely independent of the cash flows of other assets and liabilities (the "asset group"). Secondly, we estimate the undiscounted future cash flows that are directly associated with and expected to arise from the use and eventual disposition of such

asset group. If the undiscounted cash flows exceed the carrying value, no impairment is indicated. If the undiscounted cash flows do not exceed the carrying value, then an impairment is measured based on fair value compared to carrying value, with fair value typically based on a discounted cash flow model.

To estimate the undiscounted cash flows of an asset group, we consider potential cash flow scenarios based on management estimates given current conditions. Determining the recoverability of our asset groups is judgmental in nature and requires the use of significant estimates and assumptions, including estimated cash flows, growth rates and future market conditions, among others. Future changes to our estimates and assumptions based upon changes in macro-economic factors, regulatory environments, operating results or management's intentions may result in future changes to the recoverability of the asset group.

#### **Goodwill and Intangible Assets, including Casino Contracts**

As of September 30, 2013, we had intangible assets, including goodwill and casino contracts of \$7.4 million, representing 20% of total assets.



Goodwill is not subject to amortization and is tested for impairment and recoverability annually or more frequently if events or circumstances indicate that the assets might be impaired. The impairment test consists of a comparison of its fair value with its carrying amount. If the carrying amount is not recoverable and exceeds its fair value, an impairment will be recognized in an amount equal to that excess. If its carrying amount does not exceed the fair value, no impairment is recognized.

Finite-life intangible assets, including casino contracts are amortized on a straight-line basis over their estimated useful lives. The estimated useful lives are based on the nature of the assets as well as legal considerations such as contractual life. Future events, such as technology obsolescence could result in a change in the manner in which we use the assets and require a change in the estimated useful lives of such assets. Finite-lived intangible assets, including casino contracts are tested for impairment and recoverability when there are indicators of impairment. The impairment test consists of a comparison of its fair value with its carrying amount. If the carrying amount is not recoverable and exceeds its fair value, an impairment will be recognized in an amount equal to that excess. If its carrying amount does not exceed the fair value, no impairment is recognized.

As of September 30, 2013, we had casino contracts and gaming operation agreement of \$6.8 million, representing 91% of total intangible assets. The fair value of our casino contracts and gaming operation agreement was estimated using a form of the income approach known as the excess earnings method, excess earnings were discounted to present value at rates commensurate with our capital structure and the prevailing borrowing rates within the industry in general. Determining the fair value of the casino contracts and gaming operation agreement is judgmental in nature and requires the use of significant estimates and assumptions, including revenue, operating expenses, growth rates, discount rates and future market conditions, among others. Future changes to our estimates and assumptions based upon changes in macro-economic factors, operating results or management's intentions may result in future changes to the fair value of the casino contracts and gaming operation agreement.

### **Stock-Based Compensation**

We apply ASC 718, *Compensation-Stock Compensation*, to account for stock-based compensation. Under the fair value recognition provisions of ASC 718, we recognize stock-based compensation expense for all service-based awards to employees and non-employee directors with graded vesting schedules on the straight-line basis over the requisite service period for the entire award. Estimates are revised if subsequent information indicates that forfeitures will differ from previous estimates, and the cumulative effect on compensation costs of a change in the estimated forfeitures is recognized in the period of the change. For non-employee awards, we remeasure compensation costs each period until the service condition is complete and recognize compensation costs on the straight-line basis over the requisite service period. Option valuation models require the input of highly subjective assumptions, and changes in the assumptions used can materially affect the fair value estimate. Judgment is required in estimating stock price volatility, forfeiture rates, expected dividends, and expected terms that options remain outstanding. For restricted stock awards with performance conditions, the Company evaluates if performance conditions are probable in each reporting period. The compensation expense of restricted awards is recognized ratably over the implicit service period if achieving performance conditions is probable. Initial accruals of compensation expense are based on the estimated number of shares for which requisite service is expected to be rendered.

Stock-based compensation expense totaled approximately \$109,000 and \$123,000 and \$554,000 and \$675,000 for the three-month and nine-month periods ended September 30, 2013 and 2012, respectively, in the accompanying consolidated statements of comprehensive income.

### **Income Taxes**

We are subject to income taxes in the U.S. (including federal and state) and several foreign jurisdictions in which we operate. We record income taxes under the asset and liability method, whereby deferred tax assets and liabilities are

recognized based on the future tax consequences attributable to temporary differences between the financial statement carrying amounts of existing assets and liabilities and their respective tax bases, and attributable to operating loss and tax credit carryforwards. Accounting standards regarding income taxes requires a reduction of the carrying amounts of deferred tax assets by a valuation allowance, if based on the available evidence it is “more-likely-than-not” that such assets will not be realized. Accordingly, the need to establish valuation allowances for deferred tax assets is assessed at each reporting period based on a “more-likely-than-not” realization threshold. This assessment considers, among other matters, the nature, frequency and severity of current and cumulative losses, forecasts of future profitability, the duration of statutory carryforward periods, our experience with operating loss and tax credit carryforwards not expiring, and implementation of tax planning strategies.

We recorded a valuation allowance to reduce deferred tax assets to the amount that is believed more likely than not to be realized. Management will reassess the realization of deferred tax assets based on the applicable accounting standards for income taxes each reporting period and consider the scheduled reversal of deferred tax liabilities, sources of taxable income and tax planning strategies. To the extent that the financial results of these operations improve and it becomes “more-likely-than-not” that the deferred tax assets are realizable, we will be able to reduce the valuation allowance. For valuation allowance related to deferred tax assets generated prior to Quasi-Reorganization, which was effected on December 31, 2010, reductions in the valuation allowance will be recorded directly in equity.

Significant judgment is required in evaluating our tax positions and determining our provision for income taxes. During the ordinary course of business, there are many transactions for which the tax treatment is uncertain. Accounting standards regarding uncertainty in income taxes provides a two-step approach to recognizing and measuring uncertain tax positions. The first step is to evaluate the tax position for recognition by determining if the weight of available evidence indicates it is “more-likely-than-not” that the position will be sustained on audit, including resolution of related appeals or litigation processes, if any. The second step is to measure the tax benefit as the largest amount which is more than 50% likely, based solely on the technical merits, of being sustained on examinations. We consider many factors when evaluating and estimating our tax positions and tax benefits, which may require periodic adjustments and which may not accurately anticipate actual outcomes. We recognize interest and penalties, if any, related to unrecognized tax benefits in the provision of income taxes in the statements of comprehensive income.

### ***Recently Issued Accounting Standards***

In February 2013, the FASB issued ASU 2013-02, *Reporting of Amounts Reclassified Out of Accumulated Other Comprehensive Income*. The amendments do not change the current requirements for reporting net income or other comprehensive income in financial statements. However, the amendments require an entity to provide information about the amounts reclassified out of accumulated other comprehensive income by component. In addition, an entity is required to present, either on the face of the statement when net income is presented or in the notes, significant amounts reclassified out of accumulated other comprehensive income by the respective line items of net income but only if the amount reclassified is required under U.S. GAAP to be reclassified to net income in its entirety in the same reporting period. For public entities, the amendments are effective prospectively for reporting periods beginning after December 15, 2012. The adoption of ASU 2013-02 did not have a significant effect on the Company’s consolidated financial statements.

### **Off-Balance Sheet Arrangements**

We do not have any off-balance sheet financing arrangements.

### **Item 3. Quantitative and Qualitative Disclosures about Market Risks**

Not applicable.

### **Item 4. Controls and Procedures**

#### ***(a) Evaluation of Disclosure Controls and Procedures.***

Our management, with the participation of our chief executive officer and chief accounting officer, has evaluated the effectiveness of the design and operation of the Company’s disclosure controls and procedures pursuant to Rule 13a-15 of the Securities Exchange Act of 1934. Based on this evaluation, our management concluded that our disclosure controls and procedures were effective as of September 30, 2013.

#### ***(b) Changes in Internal Control Over Financial Reporting.***

There were no changes in our internal control over financial reporting that occurred during the three-month period ended September 30, 2013 that have materially affected, or are reasonably likely to materially affect, our internal controls over financial reporting.



**PART II OTHER INFORMATION****Item 6. Exhibits**

<b>Exhibit No.</b>	<b>Description</b>	<b>Method of Filing</b>
31.1	Certifications Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.	Filed electronically herewith
31.2	Certifications Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.	Filed electronically herewith
32.1	Certification of Principal Executive Officer and Principal Financial Officer pursuant to Section 906 of the Sarbanes-Oxley Act of 2002 (18 U.S.C. Section 1350).	Filed electronically herewith
101.INS**	XBRL Instance Document	Filed electronically herewith
101.SCH**	XBRL Taxonomy Extension Schema Document	Filed electronically herewith
101.CAL**	XBRL Taxonomy Extension Calculation Linkbase Document	Filed electronically herewith
101.LAB**	XBRL Taxonomy Extension Label Linkbase Document	Filed electronically herewith
101.PRE**	XBRL Taxonomy Extension Presentation Linkbase Document	Filed electronically herewith
101.DEF**	XBRL Taxonomy Extension Definition Linkbase Document	Filed electronically herewith

\*\*Pursuant to applicable securities laws and regulations, we are deemed to have complied with the reporting obligation relating to the submission of interactive data files in such exhibits and are not subject to liability under any anti-fraud provisions of the federal securities laws as long as we have made a good faith attempt to comply with the submission requirements and promptly amend the interactive data files after becoming aware that the interactive data files fail to comply with the submission requirements. Users of this data are advised that, pursuant to Rule 406T, these interactive data files are deemed not filed and otherwise are not subject to liability.

**SIGNATURES**

In accordance with the requirements of the Exchange Act, the registrant caused this report to be signed on its behalf by the undersigned, thereunto duly authorized.

**ENTERTAINMENT GAMING ASIA INC.**  
(Registrant)

Date: November 14, 2013

By: /s/ Clarence Chung  
Clarence Chung

Edgar Filing: Entertainment Gaming Asia Inc. - Form 10-Q

Its: President and Chief Executive Officer

Date: November 14, 2013

By: /s/ Andy Tsui  
Andy Tsui

Its: Chief Accounting Officer