ITEM 8. FINANCIAL STATEMENTS AND SUPPLEMENTARY DATA

INCOME STATEMENTS

(In millions, except per share amounts)

Year Ended June 30,	**2017**	**2016**	**2015**
Revenue:			
Product	**$ 57,190**	$ 61,502	$ 75,956
Service and other	**32,760**	23,818	17,624
Total revenue	**89,950**	85,320	93,580
Cost of revenue:			
Product	**15,175**	17,880	21,410
Service and other	**19,086**	14,900	11,628
Total cost of revenue	**34,261**	32,780	33,038
Gross margin	**55,689**	52,540	60,542
Research and development	**13,037**	11,988	12,046
Sales and marketing	**15,539**	14,697	15,713
General and administrative	**4,481**	4,563	4,611
Impairment, integration, and restructuring	**306**	1,110	10,011
Operating income	**22,326**	20,182	18,161
Other income (expense), net	**823**	(431)	346
Income before income taxes	**23,149**	19,751	18,507
Provision for income taxes	**1,945**	2,953	6,314
Net income	**$ 21,204**	$ 16,798	$ 12,193
Earnings per share:			
Basic	**$ 2.74**	$ 2.12	$ 1.49
Diluted	**$ 2.71**	$ 2.10	$ 1.48
Weighted average shares outstanding:			
Basic	**7,746**	7,925	8,177
Diluted	**7,832**	8,013	8,254
Cash dividends declared per common share	**$ 1.56**	$ 1.44	$ 1.24

See accompanying notes.

COMPREHENSIVE INCOME STATEMENTS

(In millions)

Year Ended June 30,	**2017**	**2016**	**2015**
Net income	**$ 21,204**	$ 16,798	$ 12,193
Other comprehensive income (loss):			
Net unrealized gains (losses) on derivatives (net of tax effects of **$(5)**, $(12), and $20)	**(218)**	(238)	559
Net unrealized losses on investments (net of tax effects of **$(613)**, $(121), and $(197))	**(1,116)**	(228)	(362)
Translation adjustments and other (net of tax effects of **$9**, $(33), and $16)	**228**	(519)	(1,383)
Other comprehensive loss	**(1,106)**	(985)	(1,186)
Comprehensive income	**$ 20,098**	$ 15,813	$ 11,007

See accompanying notes. Refer to Note 19 — Accumulated Other Comprehensive Income for further information.

BALANCE SHEETS

(In millions)

June 30,	2017	2016
Assets		
Current assets:		
Cash and cash equivalents	**$ 7,663**	$ 6,510
Short-term investments (including securities loaned of **$3,694** and $204)	**125,318**	106,730
Total cash, cash equivalents, and short-term investments	**132,981**	113,240
Accounts receivable, net of allowance for doubtful accounts of **$405** and $426	**19,792**	18,277
Inventories	**2,181**	2,251
Other	**4,897**	5,892
Total current assets	**159,851**	139,660
Property and equipment, net of accumulated depreciation of **$24,179** and $19,800	**23,734**	18,356
Equity and other investments	**6,023**	10,431
Goodwill	**35,122**	17,872
Intangible assets, net	**10,106**	3,733
Other long-term assets	**6,250**	3,416
Total assets	**$ 241,086**	$ 193,468
Liabilities and stockholders' equity		
Current liabilities:		
Accounts payable	**$ 7,390**	$ 6,898
Short-term debt	**9,072**	12,904
Current portion of long-term debt	**1,049**	0
Accrued compensation	**5,819**	5,264
Income taxes	**718**	580
Short-term unearned revenue	**34,102**	27,468
Securities lending payable	**97**	294
Other	**6,280**	5,949
Total current liabilities	**64,527**	59,357
Long-term debt	**76,073**	40,557
Long-term unearned revenue	**10,377**	6,441
Deferred income taxes	**531**	1,476
Other long-term liabilities	**17,184**	13,640
Total liabilities	**168,692**	121,471
Commitments and contingencies		
Stockholders' equity:		
Common stock and paid-in capital – shares authorized 24,000; outstanding **7,708** and 7,808	**69,315**	68,178
Retained earnings	**2,648**	2,282
Accumulated other comprehensive income	**431**	1,537
Total stockholders' equity	**72,394**	71,997
Total liabilities and stockholders' equity	**$ 241,086**	$ 193,468

See accompanying notes.

CASH FLOWS STATEMENTS

(In millions)

Year Ended June 30,	2017	2016	2015
Operations			
Net income	**$ 21,204**	$ 16,798	$ 12,193
Adjustments to reconcile net income to net cash from operations:			
Goodwill and asset impairments	**0**	630	7,498
Depreciation, amortization, and other	**8,778**	6,622	5,957
Stock-based compensation expense	**3,266**	2,668	2,574
Net recognized gains on investments and derivatives	**(2,073)**	(223)	(443)
Deferred income taxes	**(3,296)**	332	224
Deferral of unearned revenue	**67,711**	57,072	45,072
Recognition of unearned revenue	**(57,735)**	(48,498)	(44,920)
Changes in operating assets and liabilities:			
Accounts receivable	**(925)**	(530)	1,456
Inventories	**50**	600	(272)
Other current assets	**1,066**	(1,167)	62
Other long-term assets	**(539)**	(41)	346
Accounts payable	**81**	88	(1,054)
Other current liabilities	**386**	(260)	(624)
Other long-term liabilities	**1,533**	(766)	1,599
Net cash from operations	**39,507**	33,325	29,668
Financing			
Proceeds from issuance (repayments) of short-term debt, maturities of 90 days or less, net	**(4,963)**	7,195	4,481
Proceeds from issuance of debt	**44,344**	13,884	10,680
Repayments of debt	**(7,922)**	(2,796)	(1,500)
Common stock issued	**772**	668	634
Common stock repurchased	**(11,788)**	(15,969)	(14,443)
Common stock cash dividends paid	**(11,845)**	(11,006)	(9,882)
Other, net	**(190)**	(369)	362
Net cash from (used in) financing	**8,408**	(8,393)	(9,668)
Investing			
Additions to property and equipment	**(8,129)**	(8,343)	(5,944)
Acquisition of companies, net of cash acquired, and purchases of intangible and other assets	**(25,944)**	(1,393)	(3,723)
Purchases of investments	**(176,905)**	(129,758)	(98,729)
Maturities of investments	**28,044**	22,054	15,013
Sales of investments	**136,350**	93,287	70,848
Securities lending payable	**(197)**	203	(466)
Net cash used in investing	**(46,781)**	(23,950)	(23,001)
Effect of foreign exchange rates on cash and cash equivalents	**19**	(67)	(73)
Net change in cash and cash equivalents	**1,153**	915	(3,074)
Cash and cash equivalents, beginning of period	**6,510**	5,595	8,669
Cash and cash equivalents, end of period	**$ 7,663**	$ 6,510	$ 5,595

See accompanying notes.

STOCKHOLDERS' EQUITY STATEMENTS

(In millions)

Year Ended June 30,	**2017**	**2016**	**2015**
Common stock and paid-in capital			
Balance, beginning of period	**$ 68,178**	$ 68,465	$ 68,366
Common stock issued	**772**	668	634
Common stock repurchased	**(2,987)**	(3,689)	(3,700)
Stock-based compensation expense	**3,266**	2,668	2,574
Stock-based compensation income tax benefits	**0**	0	588
Other, net	**86**	66	3
Balance, end of period	**69,315**	68,178	68,465
Retained earnings			
Balance, beginning of period	**2,282**	9,096	17,710
Net income	**21,204**	16,798	12,193
Common stock cash dividends	**(12,040)**	(11,329)	(10,063)
Common stock repurchased	**(8,798)**	(12,283)	(10,744)
Balance, end of period	**2,648**	2,282	9,096
Accumulated other comprehensive income			
Balance, beginning of period	**1,537**	2,522	3,708
Other comprehensive loss	**(1,106)**	(985)	(1,186)
Balance, end of period	**431**	1,537	2,522
Total stockholders' equity	**$ 72,394**	$ 71,997	$ 80,083

See accompanying notes.

NOTES TO FINANCIAL STATEMENTS

NOTE 1 — ACCOUNTING POLICIES

Accounting Principles

The consolidated financial statements and accompanying notes are prepared in accordance with accounting principles generally accepted in the United States of America ("U.S. GAAP").

We have recast certain prior period amounts to conform to the current period presentation, with no impact on consolidated net income or cash flows.

Principles of Consolidation

The consolidated financial statements include the accounts of Microsoft Corporation and its subsidiaries. Intercompany transactions and balances have been eliminated. Equity investments through which we are able to exercise significant influence over but do not control the investee and are not the primary beneficiary of the investee's activities are accounted for using the equity method. Investments through which we are not able to exercise significant influence over the investee and which do not have readily determinable fair values are accounted for under the cost method.

Estimates and Assumptions

Preparing financial statements requires management to make estimates and assumptions that affect the reported amounts of assets, liabilities, revenue, and expenses. Examples of estimates include: loss contingencies; product warranties; the fair value of and/or potential impairment of goodwill and intangible assets for our reporting units; product life cycles; useful lives of our tangible and intangible assets; allowances for doubtful accounts; allowances for product returns; the market value of, and demand for, our inventory; and stock-based compensation forfeiture rates. Examples of assumptions include: the elements comprising a software arrangement, including the distinction between upgrades or enhancements and new products; when technological feasibility is achieved for our products; the potential outcome of future tax consequences of events that have been recognized on our consolidated financial statements or tax returns; and determining when investment impairments are other-than-temporary. Actual results and outcomes may differ from management's estimates and assumptions.

Foreign Currencies

Assets and liabilities recorded in foreign currencies are translated at the exchange rate on the balance sheet date. Revenue and expenses are translated at average rates of exchange prevailing during the year. Translation adjustments resulting from this process are recorded to other comprehensive income ("OCI").

Product Revenue and Service and Other Revenue

Product revenue includes sales from operating systems; cross-device productivity applications; server applications; business solution applications; desktop and server management tools; software development tools; video games; hardware such as PCs, tablets, gaming and entertainment consoles, phones, other intelligent devices, and related accessories; and training and certification of computer system integrators and developers.

Service and other revenue includes sales from cloud-based solutions that provide customers with software, services, platforms, and content such as Microsoft Office 365, Microsoft Azure, Microsoft Dynamics 365, and Xbox Live; solution support; and consulting services. Service and other revenue also includes sales from online advertising and LinkedIn.

Revenue Recognition

Revenue is recognized when persuasive evidence of an arrangement exists, delivery has occurred, the fee is fixed or determinable, and collectability is probable. Revenue generally is recognized net of allowances for returns and any taxes collected from customers and subsequently remitted to governmental authorities.

Revenue recognition for multiple-element arrangements requires judgment to determine if multiple elements exist, whether elements can be accounted for as separate units of accounting, and if so, the fair value for each of the elements.

Microsoft enters into arrangements that can include various combinations of software, services, and hardware. Where elements are delivered over different periods of time, and when allowed under U.S. GAAP, revenue is allocated to the respective elements based on their relative selling prices at the inception of the arrangement, and revenue is recognized as each element is delivered. We use a hierarchy to determine the fair value to be used for allocating revenue to elements: (i) vendor-specific objective evidence of fair value (“VSOE”), (ii) third-party evidence, and (iii) best estimate of selling price (“ESP”). For software elements, we follow the industry specific software guidance which only allows for the use of VSOE in establishing fair value. Generally, VSOE is the price charged when the deliverable is sold separately or the price established by management for a product that is not yet sold if it is probable that the price will not change before introduction into the marketplace. ESPs are established as best estimates of what the selling prices would be if the deliverables were sold regularly on a stand-alone basis. Our process for determining ESPs requires judgment and considers multiple factors that may vary over time depending upon the unique facts and circumstances related to each deliverable.

Revenue for retail packaged products, products licensed to original equipment manufacturers (“OEMs”), and perpetual licenses under certain volume licensing programs generally is recognized as products are shipped or made available.

Technology guarantee programs are accounted for as multiple-element arrangements as customers receive free or significantly discounted rights to use upcoming new versions of a software product if they license existing versions of the product during the eligibility period. Revenue is allocated between the existing product and the new product, and revenue allocated to the new product is deferred until that version is delivered. The revenue allocation is based on the VSOE of fair value of the products. The VSOE of fair value for upcoming new products are based on the price determined by management having the relevant authority when the element is not yet sold separately, but is expected to be sold in the near future at the price set by management.

Software updates that will be provided free of charge are evaluated on a case-by-case basis to determine whether they meet the definition of an upgrade and create a multiple-element arrangement, which may require revenue to be deferred and recognized when the upgrade is delivered, or if it is determined that implied post-contract customer support (“PCS”) is being provided, the arrangement is accounted for as a multiple-element arrangement and all revenue from the arrangement is deferred and recognized over the implied PCS term when the VSOE of fair value does not exist. If updates are determined to not meet the definition of an upgrade, revenue is generally recognized as products are shipped or made available.

Customers purchasing a Windows 10 license will receive unspecified updates and upgrades over the life of their Windows 10 device at no additional cost. As these updates and upgrades will not be sold on a stand-alone basis, we are unable to establish VSOE of fair value. Accordingly, revenue from licenses of Windows 10 is recognized ratably over the estimated life of the related device, which ranges between two to four years.

Certain volume licensing arrangements include a perpetual license for current products combined with rights to receive unspecified future versions of software products, which we have determined are additional software products and are therefore accounted for as subscriptions, with billings recorded as unearned revenue and recognized as revenue ratably over the coverage period. Arrangements that include term-based licenses for current products with the right to use unspecified future versions of the software during the coverage period, are also accounted for as subscriptions, with revenue recognized ratably over the coverage period. Revenue from cloud-based services arrangements that allow for the use of a hosted software product or service over a contractually determined period of time without taking possession of software are accounted for as subscriptions with billings recorded as unearned revenue and recognized as revenue ratably over the coverage period beginning on the date the service is made available to customers. Revenue from cloud-based services arrangements that are provided on a consumption basis (for example, the amount of storage used in a particular period) is recognized commensurate with the customer utilization of such resources.

Some volume licensing arrangements include time-based subscriptions for cloud-based services and software offerings that are accounted for as subscriptions. These arrangements are considered multiple-element arrangements. However, because all elements are accounted for as subscriptions and have the same coverage period and delivery pattern, they have the same revenue recognition timing.

Revenue related to Surface devices, Xbox consoles, games published by us, phones, and other hardware components is generally recognized when ownership is transferred to the resellers or to end customers when selling directly through Microsoft retail stores and online marketplaces. A portion of revenue may be deferred when these products are combined with software elements, and/or services. Revenue related to licensing for games published by third parties for use on the Xbox consoles is recognized when games are manufactured by the game publishers.

Display advertising revenue is recognized as advertisements are displayed. Search advertising revenue is recognized when the ad appears in the search results or when the action necessary to earn the revenue has been completed. Consulting services revenue is recognized as services are rendered, generally based on the negotiated hourly rate in the consulting arrangement and the number of hours worked during the period. Consulting revenue for fixed-price services arrangements is recognized as services are provided.

Cost of Revenue

Cost of revenue includes: manufacturing and distribution costs for products sold and programs licensed; operating costs related to product support service centers and product distribution centers; costs incurred to include software on PCs sold by OEMs, to drive traffic to our websites, and to acquire online advertising space; costs incurred to support and maintain Internet-based products and services, including datacenter costs and royalties; warranty costs; inventory valuation adjustments; costs associated with the delivery of consulting services; and the amortization of capitalized software development costs. Capitalized software development costs are amortized over the estimated lives of the products.

Product Warranty

We provide for the estimated costs of fulfilling our obligations under hardware and software warranties at the time the related revenue is recognized. For hardware warranties, we estimate the costs based on historical and projected product failure rates, historical and projected repair costs, and knowledge of specific product failures (if any). The specific hardware warranty terms and conditions vary depending upon the product sold and the country in which we do business, but generally include parts and labor over a period generally ranging from 90 days to three years. For software warranties, we estimate the costs to provide bug fixes, such as security patches, over the estimated life of the software. We regularly reevaluate our estimates to assess the adequacy of the recorded warranty liabilities and adjust the amounts as necessary.

Research and Development

Research and development expenses include payroll, employee benefits, stock-based compensation expense, and other headcount-related expenses associated with product development. Research and development expenses also include third-party development and programming costs, localization costs incurred to translate software for international markets, and the amortization of purchased software code and services content. Such costs related to software development are included in research and development expense until the point that technological feasibility is reached, which for our software products, is generally shortly before the products are released to production. Once technological feasibility is reached, such costs are capitalized and amortized to cost of revenue over the estimated lives of the products.

Sales and Marketing

Sales and marketing expenses include payroll, employee benefits, stock-based compensation expense, and other headcount-related expenses associated with sales and marketing personnel, and the costs of advertising, promotions, trade shows, seminars, and other programs. Advertising costs are expensed as incurred. Advertising expense was $1.5 billion, $1.6 billion, and $1.9 billion in fiscal years 2017, 2016, and 2015, respectively.

Stock-Based Compensation

Compensation cost for stock awards, which include restricted stock units (“RSUs”) and performance stock units (“PSUs”), is measured at the fair value on the grant date and recognized as expense, net of estimated forfeitures, over the related service or performance period. The fair value of stock awards is based on the quoted price of our common stock on the grant date less the present value of expected dividends not received during the vesting period. We measure the fair value of PSUs using a Monte Carlo valuation model. Compensation cost for RSUs is recognized using the straight-line method and for PSUs is recognized using the accelerated method.

Compensation expense for the employee stock purchase plan (“ESPP”) is measured as the discount the employee is entitled to upon purchase and is recognized in the period of purchase.

Income Taxes

Income tax expense includes U.S. and international income taxes, the provision for U.S. taxes on undistributed earnings of international subsidiaries not deemed to be permanently reinvested, and interest and penalties on uncertain tax positions. Certain income and expenses are not reported in tax returns and financial statements in the same year. The tax effect of such temporary differences is reported as deferred income taxes. Deferred tax assets are reported net of a valuation allowance when it is more likely than not that a tax benefit will not be realized. All deferred income taxes are classified as long-term on our consolidated balance sheets.

Fair Value Measurements

We account for certain assets and liabilities at fair value. The hierarchy below lists three levels of fair value based on the extent to which inputs used in measuring fair value are observable in the market. We categorize each of our fair value measurements in one of these three levels based on the lowest level input that is significant to the fair value measurement in its entirety. These levels are:

- *Level 1* – inputs are based upon unadjusted quoted prices for identical instruments in active markets. Our Level 1 non-derivative investments primarily include U.S. government securities, domestic and international equities, and actively traded mutual funds. Our Level 1 derivative assets and liabilities include those actively traded on exchanges.
- *Level 2* – inputs are based upon quoted prices for similar instruments in active markets, quoted prices for identical or similar instruments in markets that are not active, and model-based valuation techniques (e.g. the Black-Scholes model) for which all significant inputs are observable in the market or can be corroborated by observable market data for substantially the full term of the assets or liabilities. Where applicable, these models project future cash flows and discount the future amounts to a present value using market-based observable inputs including interest rate curves, credit spreads, foreign exchange rates, and forward and spot prices for currencies and commodities. Our Level 2 non-derivative investments consist primarily of foreign government bonds, corporate notes and bonds, mortgage- and asset-backed securities, U.S. government and agency securities, common and preferred stock, and certificates of deposit. Our Level 2 derivative assets and liabilities primarily include certain over-the-counter option and swap contracts.
- *Level 3* – inputs are generally unobservable and typically reflect management’s estimates of assumptions that market participants would use in pricing the asset or liability. The fair values are therefore determined using model-based techniques, including option pricing models and discounted cash flow models. Our Level 3 non-derivative assets and liabilities primarily comprise investments in common and preferred stock, and goodwill and intangible assets, when they are recorded at fair value due to an impairment charge. Unobservable inputs used in the models are significant to the fair values of the assets and liabilities.

We measure certain assets, including our cost and equity method investments, at fair value on a nonrecurring basis when they are deemed to be other-than-temporarily impaired. The fair values of these investments are determined based on valuation techniques using the best information available, and may include quoted market prices, market comparables, and discounted cash flow projections. An impairment charge is recorded when the cost of the investment exceeds its fair value and this condition is determined to be other-than-temporary.

Our other current financial assets and our current financial liabilities have fair values that approximate their carrying values.

Financial Instruments

Investments

We consider all highly liquid interest-earning investments with a maturity of three months or less at the date of purchase to be cash equivalents. The fair values of these investments approximate their carrying values. In general, investments with original maturities of greater than three months and remaining maturities of less than one year are classified as short-term investments. Investments with maturities beyond one year may be classified as short-term based on their highly liquid nature and because such marketable securities represent the investment of cash that is available for current operations. All cash equivalents and short-term investments are classified as available-for-sale and realized gains and losses are recorded using the specific identification method. Changes in market value, excluding other-than-temporary impairments, are reflected in OCI.

Equity and other investments classified as long-term include both debt and equity instruments. Debt and publicly-traded equity securities are classified as available-for-sale and realized gains and losses are recorded using the specific identification method. Changes in the market value of available-for-sale securities, excluding other-than-temporary impairments, are reflected in OCI. Common and preferred stock and other investments that are restricted for more than one year or are not publicly traded are recorded at cost or using the equity method.

We lend certain fixed-income and equity securities to increase investment returns. These transactions are accounted for as secured borrowings and the loaned securities continue to be carried as investments on our consolidated balance sheets. Cash and/or security interests are received as collateral for the loaned securities with the amount determined based upon the underlying security lent and the creditworthiness of the borrower. Cash received is recorded as an asset with a corresponding liability.

Investments are considered to be impaired when a decline in fair value is judged to be other-than-temporary. Fair value is calculated based on publicly available market information or other estimates determined by management. We employ a systematic methodology on a quarterly basis that considers available quantitative and qualitative evidence in evaluating potential impairment of our investments. If the cost of an investment exceeds its fair value, we evaluate, among other factors, general market conditions, credit quality of debt instrument issuers, the duration and extent to which the fair value is less than cost, and for equity securities, our intent and ability to hold, or plans to sell, the investment. For fixed-income securities, we also evaluate whether we have plans to sell the security or it is more likely than not that we will be required to sell the security before recovery. We also consider specific adverse conditions related to the financial health of and business outlook for the investee, including industry and sector performance, changes in technology, and operational and financing cash flow factors. Once a decline in fair value is determined to be other-than-temporary, an impairment charge is recorded to other income (expense), net and a new cost basis in the investment is established.

Derivatives

Derivative instruments are recognized as either assets or liabilities and are measured at fair value. The accounting for changes in the fair value of a derivative depends on the intended use of the derivative and the resulting designation.

For derivative instruments designated as fair value hedges, the gains (losses) are recognized in earnings in the periods of change together with the offsetting losses (gains) on the hedged items attributed to the risk being hedged. For options designated as fair value hedges, changes in the time value are excluded from the assessment of hedge effectiveness and are recognized in earnings.

For derivative instruments designated as cash flow hedges, the effective portion of the gains (losses) on the derivatives is initially reported as a component of OCI and is subsequently recognized in earnings when the hedged exposure is recognized in earnings. For options designated as cash flow hedges, changes in the time value are excluded from the assessment of hedge effectiveness and are recognized in earnings. Gains (losses) on derivatives representing either hedge components excluded from the assessment of effectiveness or hedge ineffectiveness are recognized in earnings.

For derivative instruments that are not designated as hedges, gains (losses) from changes in fair values are primarily recognized in other income (expense), net. Other than those derivatives entered into for investment purposes, such as commodity contracts, the gains (losses) are generally economically offset by unrealized gains (losses) in the underlying available-for-sale securities, which are recorded as a component of OCI until the securities are sold or other-than-temporarily impaired, at which time the amounts are reclassified from accumulated other comprehensive income (“AOCI”) into other income (expense), net.

Allowance for Doubtful Accounts

The allowance for doubtful accounts reflects our best estimate of probable losses inherent in the accounts receivable balance. We determine the allowance based on known troubled accounts, historical experience, and other currently available evidence. Activity in the allowance for doubtful accounts was as follows:

(In millions)

Year Ended June 30,	**2017**	**2016**	**2015**
Balance, beginning of period	**$ 426**	$ 335	$ 301
Charged to costs and other	**85**	146	77
Write-offs	**(106)**	(55)	(43)
Balance, end of period	**$ 405**	$ 426	$ 335

Inventories

Inventories are stated at average cost, subject to the lower of cost or market. Cost includes materials, labor, and manufacturing overhead related to the purchase and production of inventories. We regularly review inventory quantities on hand, future purchase commitments with our suppliers, and the estimated utility of our inventory. If our review indicates a reduction in utility below carrying value, we reduce our inventory to a new cost basis through a charge to cost of revenue.

Property and Equipment

Property and equipment is stated at cost less accumulated depreciation, and depreciated using the straight-line method over the shorter of the estimated useful life of the asset or the lease term. The estimated useful lives of our property and equipment are generally as follows: computer software developed or acquired for internal use, three to seven years; computer equipment, two to three years; buildings and improvements, five to 15 years; leasehold improvements, three to 20 years; and furniture and equipment, one to 10 years. Land is not depreciated.

Goodwill

Goodwill is tested for impairment at the reporting unit level (operating segment or one level below an operating segment) on an annual basis (May 1 for us) and between annual tests if an event occurs or circumstances change that would more likely than not reduce the fair value of a reporting unit below its carrying value.

Intangible Assets

All of our intangible assets are subject to amortization and are amortized using the straight-line method over their estimated period of benefit, ranging from one to 15 years. We evaluate the recoverability of intangible assets periodically by taking into account events or circumstances that may warrant revised estimates of useful lives or that indicate the asset may be impaired.

Recent Accounting Guidance

Accounting for Income Taxes – Intra-Entity Asset Transfers

In October 2016, the Financial Accounting Standards Board (“FASB”) issued new guidance requiring an entity to recognize the income tax consequences of an intra-entity transfer of an asset other than inventory when the transfer occurs, rather than when the asset has been sold to an outside party. This guidance is effective for us beginning July 1, 2018, with early adoption permitted beginning July 1, 2017. We plan to adopt the guidance effective July 1, 2018. Adoption of the guidance will be applied using a modified retrospective approach through a cumulative-effect adjustment to retained earnings as of the effective date. A cumulative-effect adjustment will capture the write-off of income tax consequences deferred from past intra-entity transfers involving assets other than inventory and new deferred tax assets for amounts not recognized under current U.S. GAAP. We anticipate this guidance will have a material impact on our consolidated balance sheets upon adoption, and continue to evaluate any impacts to our accounting policies, processes, and systems.

Financial Instruments – Credit Losses

In June 2016, the FASB issued a new standard to replace the incurred loss impairment methodology under current U.S. GAAP with a methodology that reflects expected credit losses and requires consideration of a broader range of reasonable and supportable information to inform credit loss estimates. We will be required to use a forward-looking expected credit loss model for accounts receivables, loans, and other financial instruments. Credit losses relating to available-for-sale debt securities will also be recorded through an allowance for credit losses rather than as a reduction in the amortized cost basis of the securities. The standard will be effective for us beginning July 1, 2020, with early adoption permitted beginning July 1, 2019. Adoption of the standard will be applied using a modified retrospective approach through a cumulative-effect adjustment to retained earnings as of the effective date. We are currently evaluating the impact of this standard on our consolidated financial statements, including accounting policies, processes, and systems.

Leases

In February 2016, the FASB issued a new standard related to leases to increase transparency and comparability among organizations by requiring the recognition of right-of-use (“ROU”) assets and lease liabilities on the balance sheet. Most prominent among the changes in the standard is the recognition of ROU assets and lease liabilities by lessees for those leases classified as operating leases under current U.S. GAAP. Under the standard, disclosures are required to meet the objective of enabling users of financial statements to assess the amount, timing, and uncertainty of cash flows arising from leases. We will be required to recognize and measure leases existing at, or entered into after, the beginning of the earliest comparative period presented using a modified retrospective approach, with certain practical expedients available.

The standard will be effective for us beginning July 1, 2019, with early adoption permitted. We elected to early adopt the standard effective July 1, 2017 concurrent with our adoption of the new standard related to revenue recognition. We elected the available practical expedients on adoption. In preparation for adoption of the standard, we have implemented internal controls and key system functionality to enable the preparation of financial information.

The standard will have a material impact on our consolidated balance sheets, but will not have a material impact on our consolidated income statements. The most significant impact will be the recognition of ROU assets and lease liabilities for operating leases, while our accounting for capital leases remains substantially unchanged.

Adoption of the standard will result in the recognition of additional ROU assets and lease liabilities for operating leases of $6.6 billion and $5.2 billion as of June 30, 2017 and 2016, respectively. See Expected Impacts to Reported Results below for the impact of adoption of the standard on our consolidated financial statements.

Financial Instruments – Recognition, Measurement, Presentation, and Disclosure

In January 2016, the FASB issued a new standard related to certain aspects of recognition, measurement, presentation, and disclosure of financial instruments. Most prominent among the changes in the standard is the requirement for changes in the fair value of our equity investments, with certain exceptions, to be recognized through net income rather than OCI. The standard will be effective for us beginning July 1, 2018. Adoption of the standard will be applied using a modified retrospective approach through a cumulative-effect adjustment to retained earnings as of the effective date. We are currently evaluating the impact of this standard on our consolidated financial statements, including accounting policies, processes, and systems.

Revenue from Contracts with Customers

In May 2014, the FASB issued a new standard related to revenue recognition. Under the standard, revenue is recognized when a customer obtains control of promised goods or services in an amount that reflects the consideration the entity expects to receive in exchange for those goods or services. In addition, the standard requires disclosure of the nature, amount, timing, and uncertainty of revenue and cash flows arising from contracts with customers.

The guidance permits two methods of adoption: retrospectively to each prior reporting period presented (full retrospective method), or retrospectively with the cumulative effect of initially applying the guidance recognized at the date of initial application (modified retrospective method). We will adopt the standard using the full retrospective method to restate each prior reporting period presented.

The standard will be effective for us beginning July 1, 2018, with early adoption permitted. We elected to early adopt the standard effective July 1, 2017. In preparation for adoption of the standard, we have implemented internal controls and key system functionality to enable the preparation of financial information and have reached conclusions on key accounting assessments related to the standard, including our assessment that the impact of accounting for costs incurred to obtain a contract is immaterial.

The most significant impact of the standard relates to our accounting for software license revenue. Specifically, for Windows 10, we will recognize revenue predominantly at the time of billing and delivery rather than ratably over the life of the related device. For certain multi-year commercial software subscriptions that include both distinct software licenses and Software Assurance, we will recognize license revenue at the time of contract execution rather than over the subscription period. Due to the complexity of certain of our commercial license subscription contracts, the actual revenue recognition treatment required under the standard will depend on contract-specific terms and in some instances may vary from recognition at the time of billing. Revenue recognition related to our hardware, cloud offerings such as Office 365, LinkedIn, and professional services will remain substantially unchanged.

Adoption of the standard will result in the recognition of additional revenue of $6.6 billion and $5.8 billion for fiscal year 2017 and 2016, respectively, and an increase in the provision for income taxes of $2.5 billion and $2.1 billion, respectively, primarily due to the net change in Windows 10 revenue recognition. In addition, adoption of the standard will result in an increase in accounts receivable and other current and long-term assets of $2.7 billion and $4.2 billion, as of June 30, 2017 and 2016, respectively, driven by unbilled receivables from upfront recognition of revenue for certain multi-year commercial software subscriptions that include both distinct software licenses and Software Assurance; a reduction of unearned revenue of $17.8 billion and $11.7 billion as of June 30, 2017 and 2016, respectively, driven by the upfront recognition of license revenue from Windows 10 and certain multi-year commercial software subscriptions; and an increase in deferred income taxes of $5.2 billion and $4.8 billion as of June 30, 2017 and 2016, respectively, driven by the upfront recognition of revenue. See Expected Impacts to Reported Results below for the impact of adoption of the standard on our consolidated financial statements.

Expected Impacts to Reported Results

Adoption of the standards related to revenue recognition and leases is expected to impact our reported results as follows:

(In millions, except earnings per share)				**Year Ended June 30, 2017**
	As Reported	**New Revenue Standard Adjustment**	**New Lease Standard Adjustment**	**As Adjusted**
Income statements:				
Revenue	**$ 89,950**	**$ 6,621**	**$ 0**	**$ 96,571**
Provision for income taxes	**1,945**	**2,467**	**0**	**4,412**
Net income	**21,204**	**4,285**	**0**	**25,489**
Diluted earnings per share	**2.71**	**0.54**	**0**	**3.25**

(In millions, except earnings per share)				**Year Ended June 30, 2016**
	As Reported	**New Revenue Standard Adjustment**	**New Lease Standard Adjustment**	**As Adjusted**
Income statements:				
Revenue	$ 85,320	$ 5,834	$ 0	$ 91,154
Provision for income taxes	2,953	2,147	0	5,100
Net income	16,798	3,741	0	20,539
Diluted earnings per share	2.10	0.46	0	2.56

(In millions)				June 30, 2017
	As Reported	New Revenue Standard Adjustment	New Lease Standard Adjustment	As Adjusted
Balance sheets:				
Accounts receivable, net	**$ 19,792**	**$ 2,639**	**$ 0**	**$ 22,431**
Operating lease right-of-use assets	**0**	**0**	**6,555**	**6,555**
Other current and long-term assets	**11,147**	**32**	**0**	**11,179**
Unearned revenue	**44,479**	**(17,823)**	**0**	**26,656**
Deferred income taxes	**531**	**5,203**	**0**	**5,734**
Operating lease liabilities	**0**	**0**	**5,372**	**5,372**
Other current and long-term liabilities	**23,464**	**(26)**	**1,183**	**24,621**
Stockholders' equity	**72,394**	**15,317**	**0**	**87,711**

(In millions)				June 30, 2016
	As Reported	New Revenue Standard Adjustment	New Lease Standard Adjustment	As Adjusted
Balance sheets:				
Accounts receivable, net	$ 18,277	$ 2,359	$ 0	$ 20,636
Operating lease right-of-use assets	0	0	5,198	5,198
Other current and long-term assets	9,308	1,872	0	11,180
Unearned revenue	33,909	(11,716)	0	22,193
Deferred income taxes	1,476	4,837	0	6,313
Operating lease liabilities	0	0	4,257	4,257
Other current and long-term liabilities	19,589	17	941	20,547
Stockholders' equity	71,997	11,093	0	83,090

Adoption of the standards related to revenue recognition and leases had no impact to cash from or used in operating, financing, or investing on our consolidated cash flows statements.

NOTE 2 — EARNINGS PER SHARE

Basic earnings per share ("EPS") is computed based on the weighted average number of shares of common stock outstanding during the period. Diluted EPS is computed based on the weighted average number of shares of common stock plus the effect of dilutive potential common shares outstanding during the period using the treasury stock method. Dilutive potential common shares include outstanding stock options and stock awards.

The components of basic and diluted EPS were as follows:

(In millions, except earnings per share)

Year Ended June 30,	2017	2016	2015
Net income available for common shareholders (A)	**$ 21,204**	$ 16,798	$ 12,193
Weighted average outstanding shares of common stock (B)	**7,746**	7,925	8,177
Dilutive effect of stock-based awards	**86**	88	77
Common stock and common stock equivalents (C)	**7,832**	8,013	8,254
Earnings Per Share			
Basic (A/B)	**$ 2.74**	$ 2.12	$ 1.49
Diluted (A/C)	**$ 2.71**	$ 2.10	$ 1.48

Anti-dilutive stock-based awards excluded from the calculations of diluted EPS were immaterial during the periods presented.

NOTE 3 — OTHER INCOME (EXPENSE), NET

The components of other income (expense), net were as follows:

(In millions)

Year Ended June 30,	**2017**	**2016**	**2015**
Dividends and interest income	**$ 1,387**	$ 903	$ 766
Interest expense	**(2,222)**	(1,243)	(781)
Net recognized gains on investments	**2,583**	668	716
Net losses on derivatives	**(510)**	(443)	(423)
Net gains (losses) on foreign currency remeasurements	**(164)**	(121)	335
Other, net	**(251)**	(195)	(267)
Total	**$ 823**	$ (431)	$ 346

Following are details of net recognized gains (losses) on investments during the periods reported:

(In millions)

Year Ended June 30,	**2017**	**2016**	**2015**
Other-than-temporary impairments of investments	**$ (55)**	$ (322)	$ (183)
Realized gains from sales of available-for-sale securities	**3,064**	1,376	1,176
Realized losses from sales of available-for-sale securities	**(426)**	(386)	(277)
Total	**$ 2,583**	$ 668	$ 716

NOTE 4 — INVESTMENTS

Investment Components

The components of investments, including associated derivatives, were as follows:

(In millions)	Cost Basis	Unrealized Gains	Unrealized Losses	Recorded Basis	Cash and Cash Equivalents	Short-term Investments	Equity and Other Investments
June 30, 2017							
Cash	**$ 3,624**	**$ 0**	**$ 0**	**$ 3,624**	**$ 3,624**	**$ 0**	**$ 0**
Mutual funds	**1,478**	**0**	**0**	**1,478**	**1,478**	**0**	**0**
Commercial paper	**319**	**0**	**0**	**319**	**69**	**250**	**0**
Certificates of deposit	**1,358**	**0**	**0**	**1,358**	**972**	**386**	**0**
U.S. government and agency securities	**112,119**	**85**	**(360)**	**111,844**	**16**	**111,828**	**0**
Foreign government bonds	**5,276**	**2**	**(13)**	**5,265**	**1,504**	**3,761**	**0**
Mortgage- and asset-backed securities	**3,921**	**14**	**(4)**	**3,931**	**0**	**3,931**	**0**
Corporate notes and bonds	**4,786**	**61**	**(12)**	**4,835**	**0**	**4,835**	**0**
Municipal securities	**284**	**43**	**0**	**327**	**0**	**327**	**0**
Common and preferred stock	**2,472**	**3,062**	**(34)**	**5,500**	**0**	**0**	**5,500**
Other investments	**523**	**0**	**0**	**523**	**0**	**0**	**523**
Total	**$ 136,160**	**$ 3,267**	**$ (423)**	**$ 139,004**	**$ 7,663**	**$ 125,318**	**$ 6,023**

(In millions)	Cost Basis	Unrealized Gains	Unrealized Losses	Recorded Basis	Cash and Cash Equivalents	Short-term Investments	Equity and Other Investments
June 30, 2016							
Cash	$ 3,501	$ 0	$ 0	$ 3,501	$ 3,501	$ 0	$ 0
Mutual funds	1,012	0	0	1,012	1,012	0	0
Commercial paper	298	0	0	298	298	0	0
Certificates of deposit	1,000	0	0	1,000	868	132	0
U.S. government and agency securities	89,970	245	(11)	90,204	100	90,104	0
Foreign government bonds	5,502	10	(18)	5,494	731	4,763	0
Mortgage- and asset-backed securities	4,789	21	(2)	4,808	0	4,808	0
Corporate notes and bonds	6,509	110	(35)	6,584	0	6,584	0
Municipal securities	285	57	0	342	0	342	0
Common and preferred stock	5,597	4,452	(236)	9,813	0	0	9,813
Other investments	615	0	0	615	0	(3)	618
Total	$ 119,078	$ 4,895	$ (302)	$ 123,671	$ 6,510	$ 106,730	$ 10,431

As of June 30, 2017 and 2016, the recorded bases of common and preferred stock that are restricted for more than one year or are not publicly traded were $1.1 billion and $767 million, respectively. These investments are carried at cost and are reviewed quarterly for indicators of other-than-temporary impairment. It is not practicable for us to reliably estimate the fair value of these investments.

As of June 30, 2017, collateral received under agreements for loaned securities was $3.7 billion, which was primarily comprised of U.S. government and agency securities. As of June 30, 2016, collateral received under agreements for loaned securities was $294 million, which was primarily comprised of cash.

Unrealized Losses on Investments

Investments with continuous unrealized losses for less than 12 months and 12 months or greater and their related fair values were as follows:

(In millions)	Less than 12 Months		12 Months or Greater			Total
	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses	Total Fair Value	Total Unrealized Losses
June 30, 2017						
U.S. government and agency securities	**$ 87,558**	**$ (348)**	**$ 371**	**$ (12)**	**$ 87,929**	**$ (360)**
Foreign government bonds	**4,006**	**(2)**	**23**	**(11)**	**4,029**	**(13)**
Mortgage- and asset-backed securities	**1,068**	**(3)**	**198**	**(1)**	**1,266**	**(4)**
Corporate notes and bonds	**669**	**(8)**	**177**	**(4)**	**846**	**(12)**
Common and preferred stock	**69**	**(6)**	**148**	**(28)**	**217**	**(34)**
Total	**$ 93,370**	**$ (367)**	**$ 917**	**$ (56)**	**$ 94,287**	**$ (423)**

(In millions)	Less than 12 Months		12 Months or Greater			Total
	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses	Total Fair Value	Total Unrealized Losses
June 30, 2016						
U.S. government and agency securities	$ 5,816	$ (3)	$ 432	$ (8)	$ 6,248	$ (11)
Foreign government bonds	3,452	(3)	35	(15)	3,487	(18)
Mortgage- and asset-backed securities	844	(1)	322	(1)	1,166	(2)
Corporate notes and bonds	1,180	(11)	788	(24)	1,968	(35)
Common and preferred stock	896	(147)	390	(89)	1,286	(236)
Total	$ 12,188	$ (165)	$ 1,967	$ (137)	$ 14,155	$ (302)

Unrealized losses from fixed-income securities are primarily attributable to changes in interest rates. Unrealized losses from domestic and international equities are due to market price movements. Management does not believe any remaining unrealized losses represent other-than-temporary impairments based on our evaluation of available evidence.

Debt Investment Maturities

(In millions)	Cost Basis	Estimated Fair Value
June 30, 2017		
Due in one year or less	$ 18,212	$ 18,188
Due after one year through five years	102,374	102,168
Due after five years through 10 years	6,478	6,504
Due after 10 years	999	1,019
Total	$ 128,063	$ 127,879

NOTE 5 — DERIVATIVES

We use derivative instruments to manage risks related to foreign currencies, equity prices, interest rates, and credit; to enhance investment returns; and to facilitate portfolio diversification. Our objectives for holding derivatives include reducing, eliminating, and efficiently managing the economic impact of these exposures as effectively as possible.

Our derivative programs include strategies that both qualify and do not qualify for hedge accounting treatment. All notional amounts presented below are measured in U.S. dollar equivalents.

Foreign Currency

Certain forecasted transactions, assets, and liabilities are exposed to foreign currency risk. We monitor our foreign currency exposures daily to maximize the economic effectiveness of our foreign currency hedge positions. Option and forward contracts are used to hedge a portion of forecasted international revenue for up to three years in the future and are designated as cash flow hedging instruments. Principal currencies hedged include the euro, Japanese yen, British pound, Canadian dollar, and Australian dollar. As of June 30, 2017 and 2016, the total notional amounts of these foreign exchange contracts sold were $8.9 billion and $8.4 billion, respectively.

Foreign currency risks related to certain non-U.S. dollar denominated securities are hedged using foreign exchange forward contracts that are designated as fair value hedging instruments. As of June 30, 2017 and 2016, the total notional amounts of these foreign exchange contracts sold were $5.1 billion and $5.3 billion, respectively.

Certain options and forwards not designated as hedging instruments are also used to manage the variability in foreign exchange rates on certain balance sheet amounts and to manage other foreign currency exposures. As of June 30, 2017, the total notional amounts of these foreign exchange contracts purchased and sold were $8.8 billion and $10.6 billion, respectively. As of June 30, 2016, the total notional amounts of these foreign exchange contracts purchased and sold were $12.0 billion and $11.7 billion, respectively.

Equity

Securities held in our equity and other investments portfolio are subject to market price risk. Market price risk is managed relative to broad-based global and domestic equity indices using certain convertible preferred investments, options, futures, and swap contracts not designated as hedging instruments. From time to time, to hedge our price risk, we may use and designate equity derivatives as hedging instruments, including puts, calls, swaps, and forwards. As of June 30, 2017, the total notional amounts of equity contracts purchased and sold for managing market price risk were $1.9 billion and $2.4 billion, respectively, of which $1.6 billion and $1.8 billion, respectively, were designated as hedging instruments. As of June 30, 2016, the total notional amounts of equity contracts purchased and sold for managing market price risk were $1.3 billion and $2.2 billion, respectively, of which $737 million and $986 million, respectively, were designated as hedging instruments.

Interest Rate

Securities held in our fixed-income portfolio are subject to different interest rate risks based on their maturities. We manage the average maturity of our fixed-income portfolio to achieve economic returns that correlate to certain broad-based fixed-income indices using exchange-traded option and futures contracts, and over-the-counter swap and option contracts, none of which are designated as hedging instruments. As of June 30, 2017, the total notional amounts of fixed-interest rate contracts purchased and sold were $233 million and $352 million, respectively. As of June 30, 2016, the total notional amounts of fixed-interest rate contracts purchased and sold were $328 million and $2.4 billion, respectively.

In addition, we use “To Be Announced” forward purchase commitments of mortgage-backed assets to gain exposure to agency mortgage-backed securities. These meet the definition of a derivative instrument in cases where physical delivery of the assets is not taken at the earliest available delivery date. As of June 30, 2017 and 2016, the total notional derivative amounts of mortgage contracts purchased were $567 million and $548 million, respectively.

Credit

Our fixed-income portfolio is diversified and consists primarily of investment-grade securities. We use credit default swap contracts, not designated as hedging instruments, to manage credit exposures relative to broad-based indices and to facilitate portfolio diversification. We use credit default swaps as they are a low-cost method of managing exposure to individual credit risks or groups of credit risks. As of June 30, 2017, the total notional amounts of credit contracts purchased and sold were $267 million and $63 million, respectively. As of June 30, 2016, the total notional amounts of credit contracts purchased and sold were $440 million and $273 million, respectively.

Commodity

We use broad-based commodity exposures to enhance portfolio returns and to facilitate portfolio diversification. We use swaps, futures, and option contracts, not designated as hedging instruments, to generate and manage exposures to broad-based commodity indices. We use derivatives on commodities as they can be low-cost alternatives to the purchase and storage of a variety of commodities, including, but not limited to, precious metals, energy, and grain. As of June 30, 2017, the total notional amounts of commodity contracts purchased were $19 million. As of June 30, 2016, the total notional amounts of commodity contracts purchased and sold were $631 million and $162 million, respectively.

Credit-Risk-Related Contingent Features

Certain of our counterparty agreements for derivative instruments contain provisions that require our issued and outstanding long-term unsecured debt to maintain an investment grade credit rating and require us to maintain minimum liquidity of $1.0 billion. To the extent we fail to meet these requirements, we will be required to post collateral, similar to the standard convention related to over-the-counter derivatives. As of June 30, 2017, our long-term unsecured debt rating was AAA, and cash investments were in excess of $1.0 billion. As a result, no collateral was required to be posted.

Fair Values of Derivative Instruments

The following table presents the fair values of derivative instruments designated as hedging instruments ("designated hedge derivatives") and not designated as hedging instruments ("non-designated hedge derivatives"). The fair values exclude the impact of netting derivative assets and liabilities when a legally enforceable master netting agreement exists and fair value adjustments related to our own credit risk and counterparty credit risk:

	June 30, 2017						June 30, 2016			
	Assets				Liabilities		Assets			Liabilities
(In millions)	Short-term Investments	Other Current Assets	Equity and Other Investments	Other Long-term Assets	Other Current Liabilities	Other Long-term Liabilities	Short-term Investments	Other Current Assets	Equity and Other Investments	Other Current Liabilities
Non-designated Hedge Derivatives										
Foreign exchange contracts	**$ 9**	**$ 203**	**$ 0**	**$ 6**	**$ (134)**	**$ (8)**	$ 33	$ 156	$ 0	$ (296)
Equity contracts	**3**	**0**	**0**	**0**	**(6)**	**0**	23	0	0	(16)
Interest rate contracts	**3**	**0**	**0**	**0**	**(7)**	**0**	10	0	0	(25)
Credit contracts	**5**	**0**	**0**	**0**	**(1)**	**0**	6	0	0	(5)
Total	**$ 20**	**$ 203**	**$ 0**	**$ 6**	**$ (148)**	**$ (8)**	$ 72	$ 156	$ 0	$ (342)
Designated Hedge Derivatives										
Foreign exchange contracts	**$ 80**	**$ 133**	**$ 0**	**$ 0**	**$ (3)**	**$ 0**	$ 1	$ 392	$ 0	$ (263)
Equity contracts	**0**	**0**	**67**	**0**	**(186)**	**0**	0	0	18	(25)
Total	**$ 80**	**$ 133**	**$ 67**	**$ 0**	**$ (189)**	**$ 0**	$ 1	$ 392	$ 18	$ (288)
Total gross amounts of derivatives	**$ 100**	**$ 336**	**$ 67**	**$ 6**	**$ (337)**	**$ (8)**	$ 73	$ 548	$ 18	$ (630)
Gross derivatives either offset or subject to an enforceable master netting agreement	**$ 100**	**$ 336**	**$ 67**	**$ 6**	**$ (334)**	**$ (8)**	$ 69	$ 548	$ 18	$ (630)
Gross amounts of derivatives offset on the balance sheet	**(20)**	**(132)**	**(67)**	**(8)**	**221**	**7**	(74)	(302)	(25)	398
Net amounts presented on the balance sheet	**80**	**204**	**0**	**(2)**	**(113)**	**(1)**	(5)	246	(7)	(232)
Gross amounts of derivatives not offset on the balance sheet	**0**	**0**	**0**	**0**	**0**	**0**	0	0	0	0
Cash collateral received	**0**	**0**	**0**	**0**	**(228)**	**0**	0	0	0	(250)
Net amount	**$ 80**	**$ 204**	**$ 0**	**$ (2)**	**$ (341)**	**$ (1)**	$ (5)	$ 246	$ (7)	$ (482)

See also Note 4 – Investments and Note 6 – Fair Value Measurements.

Fair Value Hedge Gains (Losses)

We recognized in other income (expense), net the following gains (losses) on contracts designated as fair value hedges and their related hedged items:

(In millions)

Year Ended June 30,	2017	2016	2015
Foreign Exchange Contracts			
Derivatives	**$ 441**	$ (797)	$ 741
Hedged items	**(386)**	838	(725)
Total amount of ineffectiveness	**$ 55**	$ 41	$ 16
Equity Contracts			
Derivatives	**$ (74)**	$ (76)	$ (107)
Hedged items	**74**	76	107
Total amount of ineffectiveness	**$ 0**	$ 0	$ 0
Amount of equity contracts excluded from effectiveness assessment	**$ (80)**	$ (10)	$ 0

Cash Flow Hedge Gains (Losses)

We recognized the following gains (losses) on foreign exchange contracts designated as cash flow hedges:

(In millions)

Year Ended June 30,	2017	2016	2015
Effective Portion			
Gains recognized in other comprehensive income (net of tax effects of **$4**, $24 and $35)	**$ 328**	$ 351	$ 1,152
Gains reclassified from accumulated other comprehensive income into revenue	**555**	625	608
Amount Excluded from Effectiveness Assessment and Ineffective Portion			
Losses recognized in other income (expense), net	**(389)**	(354)	(346)

We estimate that $130 million of net derivative gains included in AOCI as of June 30, 2017 will be reclassified into earnings within the following 12 months. No significant amounts of gains (losses) were reclassified from AOCI into earnings as a result of forecasted transactions that failed to occur during fiscal year 2017.

Non-Designated Derivative Gains (Losses)

Gains (losses) from changes in fair values of derivatives that are not designated as hedges are primarily recognized in other income (expense), net. These amounts are shown in the table below, with the exception of gains (losses) on derivatives presented in income statement line items other than other income (expense), net, which were immaterial for the periods presented. Other than those derivatives entered into for investment purposes, such as commodity contracts, the gains (losses) below are generally economically offset by unrealized gains (losses) in the underlying available-for-sale securities and gains (losses) from foreign exchange rate changes on certain balance sheet amounts.

(In millions)

Year Ended June 30,	**2017**	**2016**	**2015**
Foreign exchange contracts	**$ (117)**	$ (55)	$ (483)
Equity contracts	**(114)**	(21)	(19)
Interest-rate contracts	**14**	10	23
Credit contracts	**5**	(1)	(1)
Commodity contracts	**(22)**	(87)	(223)
Total	**$ (234)**	$ (154)	$ (703)

NOTE 6 — FAIR VALUE MEASUREMENTS

Financial Assets and Liabilities Measured at Fair Value on a Recurring Basis

The following tables present the fair value of our financial instruments that are measured at fair value on a recurring basis:

(In millions)	**Level 1**	**Level 2**	**Level 3**	**Gross Fair Value**	**Netting [a]**	**Net Fair Value**
June 30, 2017						
Assets						
Mutual funds	**$ 1,478**	**$ 0**	**$ 0**	**$ 1,478**	**$ 0**	**$ 1,478**
Commercial paper	**0**	**319**	**0**	**319**	**0**	**319**
Certificates of deposit	**0**	**1,358**	**0**	**1,358**	**0**	**1,358**
U.S. government and agency securities	**109,228**	**2,616**	**0**	**111,844**	**0**	**111,844**
Foreign government bonds	**0**	**5,187**	**0**	**5,187**	**0**	**5,187**
Mortgage- and asset-backed securities	**0**	**3,934**	**0**	**3,934**	**0**	**3,934**
Corporate notes and bonds	**0**	**4,829**	**1**	**4,830**	**0**	**4,830**
Municipal securities	**0**	**327**	**0**	**327**	**0**	**327**
Common and preferred stock	**2,414**	**1,994**	**18**	**4,426**	**0**	**4,426**
Derivatives	**1**	**508**	**0**	**509**	**(227)**	**282**
Total	**$ 113,121**	**$ 21,072**	**$ 19**	**$ 134,212**	**$ (227)**	**$ 133,985**
Liabilities						
Derivatives and other	**$ 0**	**$ 345**	**$ 39**	**$ 384**	**$ (228)**	**$ 156**

(In millions)	Level 1	Level 2	Level 3	Gross Fair Value	Netting [(a)]	Net Fair Value
June 30, 2016						
Assets						
Mutual funds	$ 1,012	$ 0	$ 0	$ 1,012	$ 0	$ 1,012
Commercial paper	0	298	0	298	0	298
Certificates of deposit	0	1,000	0	1,000	0	1,000
U.S. government and agency securities	86,492	3,707	0	90,199	0	90,199
Foreign government bonds	10	5,705	0	5,715	0	5,715
Mortgage- and asset-backed securities	0	4,803	0	4,803	0	4,803
Corporate notes and bonds	0	6,361	1	6,362	0	6,362
Municipal securities	0	342	0	342	0	342
Common and preferred stock	6,918	2,114	18	9,050	0	9,050
Derivatives	6	633	0	639	(401)	238
Total	$ 94,438	$ 24,963	$ 19	$ 119,420	$ (401)	$ 119,019
Liabilities						
Derivatives and other	$ 17	$ 613	$ 0	$ 630	$ (398)	$ 232

(a) *These amounts represent the impact of netting derivative assets and derivative liabilities when a legally enforceable master netting agreement exists and fair value adjustments related to our own credit risk and counterparty credit risk.*

The changes in our Level 3 financial instruments that are measured at fair value on a recurring basis were immaterial during the periods presented.

The following table reconciles the total “Net Fair Value” of assets above to the balance sheet presentation of these same assets in Note 4 – Investments.

(In millions)		
June 30,	**2017**	**2016**
Net fair value of assets measured at fair value on a recurring basis	**$ 133,985**	$ 119,019
Cash	**3,624**	3,501
Common and preferred stock measured at fair value on a nonrecurring basis	**1,073**	767
Other investments measured at fair value on a nonrecurring basis	**523**	618
Less derivative net assets classified as other current and long-term assets	**(202)**	(246)
Other	**1**	12
Recorded basis of investment components	**$ 139,004**	$ 123,671

Financial Assets and Liabilities Measured at Fair Value on a Nonrecurring Basis

During fiscal year 2017 and 2016, we did not record any material other-than-temporary impairments on financial assets required to be measured at fair value on a nonrecurring basis.

NOTE 7 — INVENTORIES

The components of inventories were as follows:

(In millions)

June 30,	2017	2016
Raw materials	**$ 797**	$ 612
Work in process	**145**	158
Finished goods	**1,239**	1,481
Total	**$ 2,181**	$ 2,251

NOTE 8 — PROPERTY AND EQUIPMENT

The components of property and equipment were as follows:

(In millions)

June 30,	2017	2016
Land	**$ 1,107**	$ 824
Buildings and improvements	**16,284**	12,393
Leasehold improvements	**5,064**	3,659
Computer equipment and software	**21,414**	17,391
Furniture and equipment	**4,044**	3,889
Total, at cost	**47,913**	38,156
Accumulated depreciation	**(24,179)**	(19,800)
Total, net	**$ 23,734**	$ 18,356

As of June 30, 2017 and 2016, assets recorded under capital leases were $2.7 billion and $865 million, respectively, and accumulated depreciation associated with capital leases was $161 million and $57 million, respectively. During fiscal years 2017 and 2016, property and equipment acquired under capital leases was $1.8 billion and $413 million, respectively.

During fiscal years 2017, 2016, and 2015, depreciation expense was $6.1 billion, $4.9 billion, and $4.1 billion, respectively.

NOTE 9 — BUSINESS COMBINATIONS

On December 8, 2016, we completed our acquisition of all issued and outstanding shares of LinkedIn Corporation, the world’s largest professional network on the Internet, for a total purchase price of $27.0 billion. The purchase price consisted primarily of cash of $26.9 billion. The acquisition is expected to accelerate the growth of LinkedIn, Office 365, and Dynamics 365. The financial results of LinkedIn have been included in our consolidated financial statements since the date of the acquisition.

The allocation of the purchase price to goodwill was completed as of June 30, 2017. The major classes of assets and liabilities to which we allocated the purchase price were as follows:

(In millions)

Cash and cash equivalents	$ 1,328
Short-term investments	2,110
Other current assets	697
Property and equipment	1,529
Intangible assets	7,887
Goodwill (a)	16,803
Short-term debt (b)	(1,323)
Other current liabilities	(1,117)
Deferred income taxes	(774)
Other	(131)
Total purchase price	$ 27,009

(a) *Goodwill was assigned to our Productivity and Business Processes segment. The goodwill was primarily attributed to increased synergies that are expected to be achieved from the integration of LinkedIn. None of the goodwill is expected to be deductible for income tax purposes.*

(b) *Convertible senior notes issued by LinkedIn on November 12, 2014, substantially all of which were redeemed after our acquisition of LinkedIn. The remaining $18 million of notes are not redeemable and are included in long-term debt on our consolidated balance sheets. See Note 12 – Debt for further information.*

Following are the details of the purchase price allocated to the intangible assets acquired:

(In millions)	Amount	Weighted Average Life
Customer-related	$ 3,607	7 years
Marketing-related (trade names)	2,148	20 years
Technology-based	2,109	3 years
Contract-based	23	5 years
Fair value of intangible assets acquired	$ 7,887	9 years

Our consolidated income statement includes the following revenue and operating loss attributable to LinkedIn since the date of acquisition:

(In millions)

Year Ended June 30,	2017
Revenue	$ 2,268
Operating loss	$ (948)

Following are the supplemental consolidated financial results of Microsoft Corporation on an unaudited pro forma basis, as if the acquisition had been consummated on July 1, 2015:

(In millions, except earnings per share)

Year Ended June 30,	2017	2016
Revenue	**$ 91,668**	$ 88,652
Net income	**20,894**	15,383
Diluted earnings per share	**2.67**	1.92

These pro forma results were based on estimates and assumptions, which we believe are reasonable. They are not the results that would have been realized had we been a combined company during the periods presented and are not necessarily indicative of our consolidated results of operations in future periods. The pro forma results include adjustments related to purchase accounting, primarily amortization of intangible assets. Acquisition costs and other nonrecurring charges were immaterial and are included in the earliest period presented.

NOTE 10 — GOODWILL

Changes in the carrying amount of goodwill were as follows:

(In millions)	June 30, 2015	Acquisitions	Other	June 30, 2016	Acquisitions	Other	June 30, 2017
Productivity and Business Processes	$ 6,309	$ 443	$ (74)	$ 6,678	**$ 17,072** (a)	**$ (11)**	**$ 23,739**
Intelligent Cloud	4,917	549	1	5,467	**49**	**39**	**5,555**
More Personal Computing	5,713	100	(86)	5,727	**115**	**(14)**	**5,828**
Total	$ 16,939	$ 1,092	$ (159)	$ 17,872	**$ 17,236**	**$ 14**	**$ 35,122**

(a) *Includes goodwill related to LinkedIn and other acquisitions. See Note 9 – Business Combinations for further information.*

The measurement periods for the valuation of assets acquired and liabilities assumed end as soon as information on the facts and circumstances that existed as of the acquisition dates becomes available, but do not exceed 12 months. Adjustments in purchase price allocations may require a change in the amounts allocated to goodwill during the periods in which the adjustments are determined.

Any change in the goodwill amounts resulting from foreign currency translations and purchase accounting adjustments are presented as “Other” in the above table. Also included in “Other” are business dispositions and transfers between business segments due to reorganizations, as applicable.

Our accumulated goodwill impairment as of both June 30, 2017 and 2016 was $11.3 billion.

Goodwill Impairment

We test goodwill for impairment annually on May 1 at the reporting unit level, primarily using a discounted cash flow methodology with a peer-based, risk-adjusted weighted average cost of capital. We believe use of a discounted cash flow approach is the most reliable indicator of the fair values of the businesses. Effective May 1, 2017, we prospectively adopted accounting guidance that simplifies our goodwill impairment testing by eliminating the requirement to calculate the implied fair value of goodwill (formerly “Step 2”) in the event that an impairment is identified. Instead, an impairment charge is recorded based on the excess of the reporting unit’s carrying amount over its fair value.

No instances of impairment were identified in our May 1, 2017 or May 1, 2016 test. During fiscal year 2015, we recorded impairment charges of $5.1 billion related to goodwill in our previous Phone Hardware reporting unit. Phone Hardware goodwill is included in the Devices reporting unit within More Personal Computing under our current segment structure.

Upon completion of the annual testing as of May 1, 2015, our previous Phone Hardware reporting unit goodwill was determined to be impaired. In the second half of fiscal year 2015, Phone Hardware did not meet its sales volume and revenue goals, and the mix of units sold had lower margins than planned. These results, along with changes in the competitive marketplace and an evaluation of business priorities, led to a shift in strategic direction and reduced future revenue and profitability expectations for the business. As a result of these changes in strategy and expectations, we forecasted reductions in unit volume growth rates and lower future cash flows used to estimate the fair value of the Phone Hardware reporting unit, which resulted in the determination that an impairment adjustment was required.

Because our annual test indicated that Phone Hardware's carrying value exceeded its estimated fair value, Step 2 of the goodwill impairment test was performed specific to Phone Hardware. Under Step 2, the fair value of all Phone Hardware assets and liabilities were estimated, including tangible assets, existing technology, patent agreements, and contractual arrangements, for the purpose of deriving an estimate of the implied fair value of goodwill. The implied fair value of the goodwill was then compared to the recorded goodwill to determine the amount of the impairment. Assumptions used in measuring the value of these assets and liabilities included the discount rates and royalty rates used in valuing the intangible assets, and consideration of the market environment in valuing the tangible assets.

NOTE 11 — INTANGIBLE ASSETS

The components of intangible assets, all of which are finite-lived, were as follows:

(In millions)	Gross Carrying Amount	Accumulated Amortization	Net Carrying Amount	Gross Carrying Amount	Accumulated Amortization	Net Carrying Amount
June 30,			**2017**			**2016**
Technology-based (a)	**$ 7,765**	**$ (4,318)**	**$ 3,447**	$ 5,970	$ (3,648)	$ 2,322
Marketing-related	**4,016**	**(829)**	**3,187**	1,869	(616)	1,253
Contract-based	**841**	**(722)**	**119**	796	(718)	78
Customer-related	**4,045**	**(692)**	**3,353**	465	(385)	80
Total	**$ 16,667(b)**	**$ (6,561)**	**$ 10,106**	$ 9,100	$ (5,367)	$ 3,733

(a) *Technology-based intangible assets included $59 million and $115 million of net carrying amount of software to be sold, leased, or otherwise marketed as of June 30, 2017 and 2016, respectively.*
(b) *Includes intangible assets related to LinkedIn and other additions. See Note 9 – Business Combinations for further information.*

No material impairments of intangible assets were identified during fiscal year 2017.

During fiscal year 2016, we recorded impairment charges of $480 million related to intangible assets in the Devices reporting unit within our More Personal Computing segment. In the fourth quarter of fiscal year 2016, we tested these intangible assets for recoverability due to changes in facts and circumstances associated with the shift in strategic direction and reduced profitability expectations for our phone business. Based on the results of our testing, we determined that the carrying value of the intangible assets was not recoverable, and an impairment charge was recorded to the extent that estimated fair value exceeded carrying value. We primarily used the income approach to determine the fair value of the intangible assets and determine the amount of impairment.

During fiscal year 2015, we recorded impairment charges of $2.2 billion related to intangible assets in our previous Phone Hardware reporting unit. Phone Hardware intangible assets are included in the Devices reporting unit under our current segment structure. In the fourth quarter of fiscal year 2015, we tested these intangible assets for recoverability due to changes in facts and circumstances associated with the shift in strategic direction and reduced profitability expectations for Phone Hardware. Based on the results of our testing, we determined that the carrying value of the intangible assets was not recoverable, and an impairment charge was recorded to the extent that estimated fair value exceeded carrying value. We primarily used a relief from royalty income approach to determine the fair value of the intangible assets and determine the amount of impairment.

These intangible assets impairment charges were included in impairment, integration, and restructuring expenses on our consolidated income statement, and reflected in Corporate and Other in our table of operating income (loss) by segment in Note 21 – Segment Information and Geographic Data.

We estimate that we have no significant residual value related to our intangible assets.

The components of intangible assets acquired during the periods presented were as follows:

(In millions)	Amount	Weighted Average Life	Amount	Weighted Average Life
Year Ended June 30,	**2017**		**2016**	
Customer-related	**$ 3,607**	**7 years**	$ 30	3 years
Technology-based	**2,265**	**2 years**	361	4 years
Marketing-related	**2,148**	**19 years**	2	1 year
Contract-based	**63**	**6 years**	0	n/a
Total	**$ 8,083**	**9 years**	$ 393	4 years

Intangible assets amortization expense was $1.7 billion, $978 million, and $1.3 billion for fiscal years 2017, 2016, and 2015, respectively. Amortization of capitalized software was $55 million, $69 million, and $79 million for fiscal years 2017, 2016, and 2015, respectively.

The following table outlines the estimated future amortization expense related to intangible assets held as of June 30, 2017:

(In millions)	
Year Ending June 30,	
2018	$ 2,190
2019	1,698
2020	1,180
2021	1,006
2022	932
Thereafter	3,100
Total	$ 10,106

NOTE 12 — DEBT

Short-term Debt

As of June 30, 2017, we had $9.1 billion of commercial paper issued and outstanding, with a weighted-average interest rate of 1.01% and maturities ranging from 25 days to 264 days. As of June 30, 2016, we had $12.9 billion of commercial paper issued and outstanding, with a weighted-average interest rate of 0.43% and maturities ranging from 1 day to 99 days. The estimated fair value of this commercial paper approximates its carrying value.

We have two $5.0 billion credit facilities that expire on October 31, 2017 and November 14, 2018, respectively. These credit facilities serve as a back-up for our commercial paper program. As of June 30, 2017, we were in compliance with the only financial covenant in both credit agreements, which requires us to maintain a coverage ratio of at least three times earnings before interest, taxes, depreciation, and amortization to interest expense, as defined in the credit agreements. No amounts were drawn against these credit facilities during any of the periods presented.

Long-term Debt

As of June 30, 2017, the total carrying value and estimated fair value of our long-term debt, including the current portion, were $77.1 billion and $80.3 billion, respectively. As of June 30, 2016, the total carrying value and estimated fair value of our long-term debt were $40.6 billion and $44.0 billion, respectively. These estimated fair values are based on Level 2 inputs.

The components of our long-term debt, including the current portion, and the associated interest rates were as follows:

(In millions, except interest rates)	Face Value	Face Value	Stated Interest Rate	Effective Interest Rate
June 30,	2017	2016		
Notes				
November 15, 2017	$ 600	$ 600	0.875%	1.084%
May 1, 2018	450	450	1.000%	1.106%
November 3, 2018	1,750	1,750	1.300%	1.396%
December 6, 2018	1,250	1,250	1.625%	1.824%
June 1, 2019	1,000	1,000	4.200%	4.379%
August 8, 2019 (a)	2,500	*	1.100%	1.203%
November 1, 2019 (b)	18	*	0.500%	0.500%
February 6, 2020 (c)	1,500	*	1.850%	1.952%
February 12, 2020	1,500	1,500	1.850%	1.935%
October 1, 2020	1,000	1,000	3.000%	3.137%
November 3, 2020	2,250	2,250	2.000%	2.093%
February 8, 2021	500	500	4.000%	4.082%
August 8, 2021 (a)	2,750	*	1.550%	1.642%
December 6, 2021 (d)	1,996	1,944	2.125%	2.233%
February 6, 2022 (c)	1,750	*	2.400%	2.520%
February 12, 2022	1,500	1,500	2.375%	2.466%
November 3, 2022	1,000	1,000	2.650%	2.717%
November 15, 2022	750	750	2.125%	2.239%
May 1, 2023	1,000	1,000	2.375%	2.465%
August 8, 2023 (a)	1,500	*	2.000%	2.101%
December 15, 2023	1,500	1,500	3.625%	3.726%
February 6, 2024 (c)	2,250	*	2.875%	3.041%
February 12, 2025	2,250	2,250	2.700%	2.772%
November 3, 2025	3,000	3,000	3.125%	3.176%
August 8, 2026 (a)	4,000	*	2.400%	2.464%
February 6, 2027 (c)	4,000	*	3.300%	3.383%
December 6, 2028 (d)	1,996	1,944	3.125%	3.218%
May 2, 2033 (d)	627	611	2.625%	2.690%
February 12, 2035	1,500	1,500	3.500%	3.604%
November 3, 2035	1,000	1,000	4.200%	4.260%
August 8, 2036 (a)	2,250	*	3.450%	3.510%
February 6, 2037 (c)	2,500	*	4.100%	4.152%
June 1, 2039	750	750	5.200%	5.240%
October 1, 2040	1,000	1,000	4.500%	4.567%
February 8, 2041	1,000	1,000	5.300%	5.361%
November 15, 2042	900	900	3.500%	3.571%
May 1, 2043	500	500	3.750%	3.829%
December 15, 2043	500	500	4.875%	4.918%
February 12, 2045	1,750	1,750	3.750%	3.800%
November 3, 2045	3,000	3,000	4.450%	4.492%
August 8, 2046 (a)	4,500	*	3.700%	3.743%
February 6, 2047 (c)	3,000	*	4.250%	4.287%
February 12, 2055	2,250	2,250	4.000%	4.063%
November 3, 2055	1,000	1,000	4.750%	4.782%
August 8, 2056 (a)	2,250	*	3.950%	4.033%
February 6, 2057 (c)	2,000	*	4.500%	4.528%
Total	$ 77,837	$ 40,949		

(a) *In August 2016, we issued $19.8 billion of debt securities.*

(b) *Remaining notes that were acquired as part of the LinkedIn acquisition. See Note 9 – Business Combinations for further information.*
(c) *In February 2017, we issued $17.0 billion of debt securities.*
(d) *Euro-denominated debt securities.*
* *Not applicable.*

The notes in the table above are senior unsecured obligations and rank equally with our other senior unsecured debt outstanding. Interest on these notes is paid semi-annually, except for the euro-denominated debt securities on which interest is paid annually. Cash paid for interest on our debt for fiscal years 2017, 2016, and 2015 was $1.6 billion, $1.1 billion, and $620 million, respectively. Effective July 1, 2016, we retrospectively adopted accounting guidance that requires debt issuance costs to be recorded as a deduction from the carrying amount of the debt liability, consistent with debt discounts. As of June 30, 2017 and 2016, the aggregate unamortized discount and debt issuance costs associated with our long-term debt, including the current portion, were $715 million and $392 million, respectively.

Maturities of our long-term debt for each of the next five years and thereafter are as follows:

(In millions)

Year Ending June 30,	
2018	$ 1,050
2019	4,000
2020	5,518
2021	3,750
2022	7,996
Thereafter	55,523
Total	$ 77,837

NOTE 13 — INCOME TAXES

The components of the provision for income taxes were as follows:

(In millions)

Year Ended June 30,	**2017**	**2016**	**2015**
Current Taxes			
U.S. federal	**$ 2,739**	$ 545	$ 3,661
U.S. state and local	**30**	136	364
Foreign	**2,472**	1,940	2,065
Current taxes	**5,241**	2,621	6,090
Deferred Taxes			
Deferred taxes	**(3,296)**	332	224
Provision for income taxes	**$ 1,945**	$ 2,953	$ 6,314

In fiscal year 2017, deferred taxes included U.S. and foreign deferred tax benefit of $2.7 billion and $617 million, respectively.

U.S. and foreign components of income (loss) before income taxes were as follows:

(In millions)

Year Ended June 30,	**2017**	**2016**	**2015**
U.S.	**$ 453**	$ (325)	$ 7,363
Foreign	**22,696**	20,076	11,144
Income before income taxes	**$ 23,149**	$ 19,751	$ 18,507

In fiscal year 2017, income before income taxes included the net impact of U.S. and foreign revenue deferrals related to the sales of Windows 10 of $6.4 billion and $317 million, respectively. In fiscal year 2016, income before income taxes included the net impact of U.S. and foreign revenue deferrals related to the sales of Windows 10 of $6.0 billion and $588 million, respectively. In fiscal year 2015, income before income taxes included the net impact of U.S. and foreign impairment, integration, and restructuring expenses relating to our phone business of $1.1 billion and $8.9 billion, respectively.

The items accounting for the difference between income taxes computed at the U.S. federal statutory rate and our effective rate were as follows:

Year Ended June 30,	**2017**	**2016**	**2015**
Federal statutory rate	**35.0%**	35.0%	35.0%
Effect of:			
Foreign earnings taxed at lower rates	**(15.7)%**	(19.4)%	(20.9)%
Phone business losses	**(7.3)%**	1.3%	19.1%
Excess tax benefits relating to stock-based compensation	**(2.7)%**	(2.0)%	0%
Domestic production activities deduction	**(1.4)%**	(0.6)%	(2.4)%
Interest, net	**1.8%**	1.2%	1.5%
Other reconciling items, net	**(1.3)%**	(0.5)%	1.8%
Effective rate	**8.4%**	15.0%	34.1%

The reduction from the federal statutory rate is primarily due to earnings taxed at lower rates in foreign jurisdictions resulting from producing and distributing our products and services through our foreign regional operations centers in Ireland, Singapore, and Puerto Rico. Our foreign regional operating centers, which are taxed at rates lower than the U.S. rate, generated 64%, 69%, and 73% of our foreign income before tax in fiscal years 2017, 2016, and 2015, respectively. Additionally, our effective tax rate in fiscal year 2017 reflects the realization of tax benefits attributable to previous phone business losses. In general, other reconciling items consist primarily of U.S. state income taxes, permanent items, and credits. In fiscal years 2017, 2016, and 2015, there were no individually significant other reconciling items.

The decrease in our effective tax rate for fiscal year 2017 compared to fiscal year 2016 was primarily due to the realization of tax benefits attributable to previous phone business losses, offset in part by changes in the mix of our income before income taxes between the U.S. and foreign countries. The fiscal year 2016 effective tax rate included the impact of nondeductible phone charges and valuation allowances.

The components of the deferred income tax assets and liabilities were as follows:

(In millions)

June 30,	**2017**	**2016**
Deferred Income Tax Assets		
Stock-based compensation expense	**$ 777**	$ 809
Other expense items	**1,550**	1,609
Restructuring charges	**66**	284
Unearned revenue	**1,889**	494
Impaired investments	**59**	226
Loss carryforwards	**4,809**	4,252
Depreciation and amortization	**53**	115
Other revenue items	**130**	89
Deferred income tax assets	**9,333**	7,878
Less valuation allowance	**(3,310)**	(4,729)
Deferred income tax assets, net of valuation allowance	**$ 6,023**	$ 3,149
Deferred Income Tax Liabilities		
Foreign earnings	**$ (1,107)**	$ (1,242)
Unrealized gain on investments and debt	**(1,384)**	(2,102)
Depreciation and amortization	**(1,630)**	(1,008)
Other	**(21)**	(54)
Deferred income tax liabilities	**(4,142)**	(4,406)
Net deferred income tax assets (liabilities)	**$ 1,881**	$ (1,257)
Reported As		
Other long-term assets	**$ 2,412**	$ 219
Long-term deferred income tax liabilities	**(531)**	(1,476)
Net deferred income tax assets (liabilities)	**$ 1,881**	$ (1,257)

In fiscal year 2017, we corrected the table above to include a $2.5 billion loss carryforward and valuation allowance as of June 30, 2016. We do not consider this correction to be material, and there was no impact to our consolidated financial statements.

As of June 30, 2017, we had net operating loss carryforwards of $13.7 billion, including $11.1 billion of foreign net operating loss carryforwards. The valuation allowance disclosed in the table above relates to the foreign net operating loss carryforwards and other net deferred tax assets that may not be realized.

Deferred income tax balances reflect the effects of temporary differences between the carrying amounts of assets and liabilities and their tax bases and are stated at enacted tax rates expected to be in effect when the taxes are paid or recovered.

As of June 30, 2017, we have not provided deferred U.S. income taxes or foreign withholding taxes on temporary differences of approximately $142 billion resulting from earnings for certain non-U.S. subsidiaries which are permanently reinvested outside the U.S. The unrecognized deferred tax liability associated with these temporary differences was approximately $45 billion as of June 30, 2017.

Income taxes paid, net of refunds, were $2.4 billion, $3.9 billion, and $4.4 billion in fiscal years 2017, 2016, and 2015, respectively.

Tax contingencies and other income tax liabilities were $13.5 billion and $11.8 billion as of June 30, 2017 and 2016, respectively, and are included in other long-term liabilities. This increase relates primarily to current period intercompany transfer pricing and tax credits.

Uncertain Tax Positions

Unrecognized tax benefits as of June 30, 2017, 2016, and 2015, were $11.7 billion, $10.2 billion, and $9.6 billion, respectively. If recognized, these tax benefits would affect our effective tax rates for fiscal years 2017, 2016, and 2015, by $10.2 billion, $8.8 billion, and $7.9 billion, respectively.

As of June 30, 2017, 2016, and 2015, we had accrued interest expense related to uncertain tax positions of $2.3 billion, $1.9 billion, and $1.7 billion, respectively, net of federal income tax benefits. Interest expense on unrecognized tax benefits was $399 million, $163 million, and $237 million in fiscal years 2017, 2016, and 2015, respectively, and was included in provision for income taxes.

The aggregate changes in the balance of unrecognized tax benefits were as follows:

(In millions)

Year Ended June 30,	**2017**	**2016**	**2015**
Balance, beginning of year	**$ 10,164**	$ 9,599	$ 8,714
Decreases related to settlements	**(4)**	(201)	(50)
Increases for tax positions related to the current year	**1,277**	1,086	1,091
Increases for tax positions related to prior years	**397**	115	94
Decreases for tax positions related to prior years	**(49)**	(317)	(144)
Decreases due to lapsed statutes of limitations	**(48)**	(118)	(106)
Balance, end of year	**$ 11,737**	$ 10,164	$ 9,599

While we settled a portion of the Internal Revenue Service (“IRS”) audit for tax years 2004 to 2006 during the third quarter of fiscal year 2011, and settled a portion of the IRS audit for tax years 2007 to 2009 during the first quarter of fiscal year 2016, we remain under audit for those years. We also continue to be subject to examination by the IRS for tax years 2010 to 2016. In February 2012, the IRS withdrew its 2011 Revenue Agents Report for tax years 2004 to 2006 and reopened the audit phase of the examination. As of June 30, 2017, the primary unresolved issue relates to transfer pricing, which could have a significant impact on our consolidated financial statements if not resolved favorably. We believe our allowances for income tax contingencies are adequate. We have not received a proposed assessment for the unresolved issues and do not expect a final resolution of these issues in the next 12 months. Based on the information currently available, we do not anticipate a significant increase or decrease to our tax contingencies for these issues within the next 12 months.

We are subject to income tax in many jurisdictions outside the U.S. Our operations in certain jurisdictions remain subject to examination for tax years 1996 to 2017, some of which are currently under audit by local tax authorities. The resolutions of these audits are not expected to be material to our consolidated financial statements.

NOTE 14 — RESTRUCTURING CHARGES

Phone Hardware Restructuring

In June 2015, management approved a plan to restructure our phone business to better focus and align resources (the “Phone Hardware Restructuring Plan”), under which we eliminated approximately 7,400 positions in fiscal year 2016. In fiscal year 2015, we incurred restructuring charges of $780 million under the Phone Hardware Restructuring Plan, including severance expenses and other reorganization costs. In fiscal year 2016, we reversed $21 million of previously estimated restructuring charges related to contract termination costs. The actions associated with the Phone Hardware Restructuring Plan were completed as of June 30, 2017.

2016 Restructuring

In the fourth quarter of fiscal year 2016, management approved restructuring plans that resulted in approximately 4,700 job eliminations in fiscal year 2017, primarily across our smartphone hardware business and global sales.

In fiscal year 2016, we incurred restructuring charges of $501 million in connection with the 2016 restructuring plans, including severance expenses and other reorganization costs. The actions associated with these restructuring plans were completed as of June 30, 2017.

2017 Restructuring

In June 2017, management approved a sales and marketing restructuring plan. In fiscal year 2017, we recorded employee severance expenses of $306 million primarily related to this sales and marketing restructuring plan. We do not expect to incur additional charges for this restructuring plan in subsequent years. The actions associated with this restructuring plan are expected to be completed by the end of fiscal year 2018.

Restructuring Summary

Restructuring charges associated with each of these plans were included in impairment, integration, and restructuring expenses on our consolidated income statements, and were reflected in Corporate and Other in our table of operating income (loss) by segment.

Changes in the restructuring liability were as follows:

(In millions)	Severance	Other(a)	Total
Balance, as of June 30, 2016	$ 470	$ 239	$ 709
Restructuring charges	306	0	306
Cash paid	(367)	(101)	(468)
Other	(36)	(79)	(115)
Balance, as of June 30, 2017	$ 373	$ 59	$ 432

(a) *Primarily reflects activities associated with the consolidation of our facilities and manufacturing operations, including contract termination costs and asset write-downs.*

NOTE 15 — UNEARNED REVENUE

Unearned revenue by segment was as follows:

(In millions) June 30,	2017	2016
Productivity and Business Processes	$ 14,291	$ 12,497
Intelligent Cloud	13,464	11,472
More Personal Computing	3,420	3,334
Corporate and Other	13,304	6,606
Total	$ 44,479	$ 33,909

Corporate and Other consists of the net revenue deferral from Windows 10. Revenue from Windows 10 is primarily recognized at the time of billing in the More Personal Computing segment, and the deferral and subsequent recognition of revenue is reflected in Corporate and Other.

NOTE 16 — COMMITMENTS

Construction and Operating Leases

We have committed $1.1 billion for constructing new buildings, building improvements, and leasehold improvements as of June 30, 2017.

We have operating leases for most U.S. and international sales and support offices, datacenters, research and development facilities, manufacturing facilities, retail stores, and certain equipment. Rental expense for facilities operating leases was $1.3 billion, $1.0 billion, and $989 million, in fiscal years 2017, 2016, and 2015, respectively.

Future minimum rental commitments under non-cancellable facilities operating leases in place as of June 30, 2017 are as follows:

(In millions)

Year Ending June 30,	
2018	$ 1,292
2019	1,220
2020	1,115
2021	908
2022	749
Thereafter	2,588
Total	$ 7,872

Capital Leases

We have capital leases for datacenters and corporate offices. As of June 30, 2017 and 2016, capital lease obligations included in other current liabilities were $113 million and $25 million, respectively, and capital lease obligations included in other long-term liabilities were $2.4 billion and $761 million, respectively.

Future minimum lease payments under non-cancellable capital leases as of June 30, 2017 were as follows:

(In millions)

Year Ending June 30,	
2018	$ 209
2019	217
2020	222
2021	227
2022	232
Thereafter	2,353
Total (a)	$ 3,460

(a) *Includes imputed interest of $922 million.*

As of June 30, 2017, we had additional purchase obligations for capital leases executed but not yet recorded of $3.2 billion.

NOTE 17 — CONTINGENCIES

Patent and Intellectual Property Claims

IPCom patent litigation

IPCom GmbH & Co. (“IPCom”) is a German company that holds a large portfolio of mobile technology-related patents spanning about 170 patent families and addressing a broad range of cellular technologies. IPCom has asserted 19 of these patents in litigation against Nokia Corporation (“Nokia”) and many of the leading cell phone companies and operators. In November 2014, Microsoft and IPCom entered into a standstill agreement staying all of the pending litigation against Microsoft to permit the parties to pursue settlement discussions, which continue.

InterDigital patent litigation

InterDigital Technology Corporation and InterDigital Communications Corporation (collectively, “IDT”) filed four patent infringement cases against Nokia in the International Trade Commission (“ITC”) and in U.S. District Court for the District of Delaware between 2007 and 2013. We were added to these cases as a defendant after we acquired the Nokia phone business. Each of the ITC matters was resolved in our favor. In September 2015, in an *inter partes* review the United States Patent Trial and Appeal Board issued a final written decision that deemed unpatentable all asserted claims of the patent remaining at issue in the Delaware case. IDT’s appeal of this decision was heard by the U.S. Court of Appeals for the Federal Circuit on April 7, 2017 and the Delaware case was stayed pending final completion of the *inter partes* review (including appeals and any subsequent proceedings in the Patent Office). We filed an antitrust complaint against IDT in the District of Delaware in August 2015 asserting violations of Section 2 of the Sherman Act, alleging unlawful exploitation of standard essential patents. Microsoft and IDT settled these cases in May 2017 and they have been dismissed.

European copyright levies

We assumed from Nokia all potential liability due to Nokia’s alleged failure to pay “private copyright levies” in various European countries based upon sale of memory cards and mobile phones that incorporate blank memory. The levies are based upon a 2001 European Union (“EU”) Directive establishing a right for end users to make copies of copyrighted works for personal or private use, but also allowing the collection of levies based upon sales of blank media or recording devices to compensate copyright holders for private copying. Various collecting societies in EU countries initiated litigation against Nokia, stating it must pay levies not only based upon sales of blank memory cards, but also phones that include blank memory for data storage on the phones, regardless of actual usage of that memory. The most significant cases against Nokia were pending in Germany and Austria, due to both the high volume of sales and high levy amounts sought in these countries. We reached a settlement of the Austrian case in August 2016. In Germany, the only period for which settlement has not been reached is 2004 through 2007. In July 2016, the German Supreme Court heard our appeal contesting the legality of the levy assessed on phones with music players and over five megabytes of memory. The Supreme Court issued a ruling in December 2016, finding that the levy may not be appropriate for phones that have the ability to receive music files only via Bluetooth or infrared inputs, and remanded for further proceedings. A new case schedule has not been set, and we have reached a tentative settlement.

Other patent and intellectual property claims

In addition to the IPCom cases, there were 41 other patent infringement cases pending against Microsoft as of June 30, 2017.

Antitrust, Unfair Competition, and Overcharge Class Actions

Antitrust and unfair competition class action lawsuits were filed against us in British Columbia, Ontario, and Quebec, Canada. All three have been certified on behalf of Canadian indirect purchasers who acquired licenses for Microsoft operating system software and/or productivity application software between 1998 and 2010.

The trial of the British Columbia action commenced in May 2016. The plaintiffs filed their case in chief in August 2016, setting out claims made, authorities, and evidence in support of their claims. A six-month oral hearing is scheduled to commence in September 2017, consisting of cross examination on witness affidavits. The Ontario and Quebec cases are inactive.

Other Antitrust Litigation and Claims

China State Administration for Industry and Commerce investigation

In 2014, Microsoft was informed that China's State Administration for Industry and Commerce ("SAIC") had begun a formal investigation relating to China's Anti-Monopoly Law, and the SAIC conducted onsite inspections of Microsoft offices in Beijing, Shanghai, Guangzhou, and Chengdu. SAIC has stated the investigation relates to compatibility, bundle sales, file verification issues related to Windows and Office software, and potentially other issues.

Product-Related Litigation

U.S. cell phone litigation

Nokia, along with other handset manufacturers and network operators, is a defendant in 19 lawsuits filed in the Superior Court for the District of Columbia by individual plaintiffs who allege that radio emissions from cellular handsets caused their brain tumors and other adverse health effects. We assumed responsibility for these claims as part of our acquisition of Nokia's Devices and Services business and have been substituted for the Nokia defendants. Nine of these cases were filed in 2002 and are consolidated for certain pre-trial proceedings; the remaining 10 cases are stayed. In a separate 2009 decision, the Court of Appeals for the District of Columbia held that adverse health effect claims arising from the use of cellular handsets that operate within the U.S. Federal Communications Commission radio frequency emission guidelines ("FCC Guidelines") are pre-empted by federal law. The plaintiffs allege that their handsets either operated outside the FCC Guidelines or were manufactured before the FCC Guidelines went into effect. The lawsuits also allege an industry-wide conspiracy to manipulate the science and testing around emission guidelines.

In 2013, defendants in the consolidated cases moved to exclude plaintiffs' expert evidence of general causation on the basis of flawed scientific methodologies. In 2014, the trial court granted in part and denied in part defendants' motion to exclude plaintiffs' general causation experts. The defendants filed an interlocutory appeal challenging the standard for evaluating expert scientific evidence, which the District of Columbia Court of Appeals heard *en banc*. In October 2016, the Court of Appeals issued its decision adopting the standard advocated by defendants and remanding the cases to the trial court for further proceedings under that standard. Plaintiffs have filed a motion to reopen discovery and file additional expert evidence.

Canadian cell phone class action

Nokia, along with other handset manufacturers and network operators, is a defendant in a 2013 class action lawsuit filed in the Supreme Court of British Columbia by a purported class of Canadians who have used cellular phones for at least 1,600 hours, including a subclass of users with brain tumors. Microsoft was served with the complaint in June 2014 and has been substituted for the Nokia defendants. The litigation has been dormant for more than two years.

Other Contingencies

We also are subject to a variety of other claims and suits that arise from time to time in the ordinary course of our business. Although management currently believes that resolving claims against us, individually or in aggregate, will not have a material adverse impact on our consolidated financial statements, these matters are subject to inherent uncertainties and management's view of these matters may change in the future.

As of June 30, 2017, we accrued aggregate legal liabilities of $352 million. While we intend to defend these matters vigorously, adverse outcomes that we estimate could reach approximately $1.0 billion in aggregate beyond recorded amounts are reasonably possible. Were unfavorable final outcomes to occur, there exists the possibility of a material adverse impact on our consolidated financial statements for the period in which the effects become reasonably estimable.

Indemnifications

We provide indemnifications of varying scope and size to certain customers against claims of intellectual property infringement made by third parties arising from the use of our products and certain other matters. Additionally, we have agreed to cover damages resulting from breaches of certain security and privacy commitments in our cloud business. We evaluate estimated losses for these indemnifications, and we consider such factors as the degree of probability of an unfavorable outcome and the ability to make a reasonable estimate of the amount of loss. To date, we have not encountered significant costs as a result of these obligations and have not accrued any liabilities related to these indemnifications on our consolidated financial statements.

NOTE 18 — STOCKHOLDERS' EQUITY

Shares Outstanding

Shares of common stock outstanding were as follows:

(In millions)

Year Ended June 30,	2017	2016	2015
Balance, beginning of year	**7,808**	8,027	8,239
Issued	**70**	75	83
Repurchased	**(170)**	(294)	(295)
Balance, end of year	**7,708**	7,808	8,027

Share Repurchases

On September 16, 2013, our Board of Directors approved a share repurchase program authorizing up to $40.0 billion in share repurchases. This share repurchase program became effective on October 1, 2013, and was completed on December 22, 2016.

On September 20, 2016, our Board of Directors approved a share repurchase program authorizing up to an additional $40.0 billion in share repurchases. This share repurchase program commenced on December 22, 2016 following completion of the prior program approved on September 16, 2013, has no expiration date, and may be suspended or discontinued at any time without notice. As of June 30, 2017, $36.8 billion remained of this $40.0 billion share repurchase program.

We repurchased the following shares of common stock under the share repurchase programs:

(In millions)	Shares	Amount	Shares	Amount	Shares	Amount
Year Ended June 30,		2017		2016		2015
First Quarter	**63**	**$ 3,550**	89	$ 4,000	43	$ 2,000
Second Quarter	**59**	**3,533**	66	3,600	43	2,000
Third Quarter	**25**	**1,600**	69	3,600	116	5,000
Fourth Quarter	**23**	**1,600**	70	3,600	93	4,209
Total	**170**	**$ 10,283**	294	$ 14,800	295	$ 13,209

Shares repurchased during the third and fourth quarter of fiscal year 2017 were under the share repurchase program approved September 20, 2016. All other shares repurchased were under the share repurchase program approved September 16, 2013. The above table excludes shares repurchased to settle statutory employee tax withholding related to the vesting of stock awards. All repurchases were made using cash resources.

Dividends

In fiscal year 2017, our Board of Directors declared the following dividends:

Declaration Date	Dividend Per Share	Record Date	Total Amount	Payment Date
			(In millions)	
September 20, 2016	**$ 0.39**	**November 17, 2016**	**$ 3,024**	**December 8, 2016**
November 30, 2016	**0.39**	**February 16, 2017**	**3,012**	**March 9, 2017**
March 14, 2017	**0.39**	**May 18, 2017**	**3,009**	**June 8, 2017**
June 13, 2017	**0.39**	**August 17, 2017**	**3,006**	**September 14, 2017**

The dividend declared on June 13, 2017 will be paid after the filing date of the 2017 Form 10-K and was included in other current liabilities as of June 30, 2017.

In fiscal year 2016, our Board of Directors declared the following dividends:

Declaration Date	Dividend Per Share	Record Date	Total Amount	Payment Date
			(In millions)	
September 15, 2015	$ 0.36	November 19, 2015	$ 2,868	December 10, 2015
December 2, 2015	0.36	February 18, 2016	2,842	March 10, 2016
March 15, 2016	0.36	May 19, 2016	2,821	June 9, 2016
June 14, 2016	0.36	August 18, 2016	2,800	September 8, 2016

The dividend declared on June 14, 2016 was included in other current liabilities as of June 30, 2016.

NOTE 19 — ACCUMULATED OTHER COMPREHENSIVE INCOME

The following table summarizes the changes in accumulated other comprehensive income by component:

(In millions)

Year Ended June 30,	**2017**	**2016**	**2015**
Derivatives			
Balance, beginning of period	**$ 352**	$ 590	$ 31
Unrealized gains, net of tax effects of **$4**, $24 and $35	**328**	351	1,152
Reclassification adjustments for gains included in revenue	**(555)**	(625)	(608)
Tax expense included in provision for income taxes	**9**	36	15
Amounts reclassified from accumulated other comprehensive income	**(546)**	(589)	(593)
Net current period other comprehensive income (loss)	**(218)**	(238)	559
Balance, end of period	**$ 134**	$ 352	$ 590
Investments			
Balance, beginning of period	**$ 2,941**	$ 3,169	$ 3,531
Unrealized gains, net of tax effects of **$267**, $120 and $59	**517**	219	110
Reclassification adjustments for gains included in other income (expense), net	**(2,513)**	(688)	(728)
Tax expense included in provision for income taxes	**880**	241	256
Amounts reclassified from accumulated other comprehensive income	**(1,633)**	(447)	(472)
Net current period other comprehensive loss	**(1,116)**	(228)	(362)
Balance, end of period	**$ 1,825**	$ 2,941	$ 3,169
Translation Adjustments and Other			
Balance, beginning of period	**$ (1,756)**	$ (1,237)	$ 146
Translation adjustments and other, net of tax effects of **$9**, $(33) and $16	**228**	(519)	(1,383)
Balance, end of period	**$ (1,528)**	$ (1,756)	$ (1,237)
Accumulated other comprehensive income, end of period	**$ 431**	$ 1,537	$ 2,522

NOTE 20 — EMPLOYEE STOCK AND SAVINGS PLANS

We grant stock-based compensation to employees and directors. As of June 30, 2017, an aggregate of 127 million shares were authorized for future grant under our stock plans. Awards that expire or are canceled without delivery of shares generally become available for issuance under the plans. We issue new shares of Microsoft common stock to satisfy vesting of awards granted under our stock plans. We also have an ESPP for all eligible employees.

Stock-based compensation expense and related income tax benefits were as follows:

(In millions)

Year Ended June 30,	**2017**	**2016**	**2015**
Stock-based compensation expense	**$ 3,266**	$ 2,668	$ 2,574
Income tax benefits related to stock-based compensation	**1,066**	882	868

Stock Plans

Stock awards entitle the holder to receive shares of Microsoft common stock as the award vests. Stock awards generally vest over a four or five-year service period.

Executive Incentive Plan

Under the Executive Incentive Plan, the Compensation Committee approves stock awards to executive officers and certain senior executives. RSUs generally vest ratably over a four-year service period. PSUs generally vest over a three-year performance period. The number of shares the PSU holder receives is based on the extent to which the corresponding performance goals have been achieved.

Activity for all stock plans

The fair value of stock awards was estimated on the date of grant using the following assumptions:

Year Ended June 30,	2017	2016	2015
Dividends per share (quarterly amounts)	**$ 0.36 - $ 0.39**	$ 0.31 - $ 0.36	$ 0.28 - $ 0.31
Interest rates	**1.2% - 2.2%**	1.1% - 1.8%	1.2% - 1.9%

During fiscal year 2017, the following activity occurred under our stock plans:

	Shares	Weighted Average Grant-Date Fair Value
	(In millions)	
Stock Awards		
Nonvested balance, beginning of year	**194**	**$ 36.92**
Granted (a)	**84**	**55.64**
Assumed in acquisitions (b)	**23**	**59.09**
Vested	**(80)**	**37.36**
Forfeited	**(20)**	**43.71**
Nonvested balance, end of year	**201**	**46.32**

(a) *Includes 2 million PSUs granted during fiscal year 2017. During both fiscal year 2016 and 2015 we granted 1 million PSUs.*
(b) *Substantially all awards assumed were related to LinkedIn. See Note 9 – Business Combinations for further information.*

As of June 30, 2017, there was approximately $6.5 billion of total unrecognized compensation costs related to stock awards. These costs are expected to be recognized over a weighted average period of 3 years. The weighted average grant-date fair value of stock awards granted was $55.64, $41.51, and $42.36 for fiscal years 2017, 2016, and 2015, respectively. The fair value of stock awards vested was $4.8 billion, $3.9 billion, and $4.2 billion, for fiscal years 2017, 2016, and 2015, respectively.

Employee Stock Purchase Plan

We have an ESPP for all eligible employees. Shares of our common stock may be purchased by employees at three-month intervals at 90% of the fair market value on the last trading day of each three-month period. Employees may purchase shares having a value not exceeding 15% of their gross compensation during an offering period. Employees purchased the following shares during the periods presented:

(Shares in millions)

Year Ended June 30,	2017	2016	2015
Shares purchased	**13**	15	16
Average price per share	**$ 56.36**	$ 44.83	$ 39.87

As of June 30, 2017, 129 million shares of our common stock were reserved for future issuance through the ESPP.

Savings Plan

We have a savings plan in the U.S. that qualifies under Section 401(k) of the Internal Revenue Code, and a number of savings plans in international locations. Participating U.S. employees may contribute a portion of their salary, subject to certain limitations. Beginning January 2016, we contribute fifty cents for each dollar a participant contributes in this plan, with a maximum employer contribution of 50% of the IRS contribution limit for the calendar year. Prior to January 2016, we contributed fifty cents for each dollar of the first 6% a participant contributed in this plan, with a maximum contribution of the lesser of 3% of a participant's earnings or 3% of the IRS compensation limit for the calendar year. Matching contributions for all plans were $734 million, $549 million, and $454 million in fiscal years 2017, 2016, and 2015, respectively, and were expensed as contributed.

NOTE 21 — SEGMENT INFORMATION AND GEOGRAPHIC DATA

In its operation of the business, management, including our chief operating decision maker, who is also our Chief Executive Officer, reviews certain financial information, including segmented internal profit and loss statements prepared on a basis not consistent with U.S. GAAP. During the periods presented, we reported our financial performance based on the following segments: Productivity and Business Processes, Intelligent Cloud, and More Personal Computing.

In December 2016, we completed our acquisition of LinkedIn Corporation. LinkedIn is reported as part of our Productivity and Business Processes segment.

Our reportable segments are described below.

Productivity and Business Processes

Our Productivity and Business Processes segment consists of products and services in our portfolio of productivity, communication, and information services, spanning a variety of devices and platforms. This segment primarily comprises:

- Office Commercial, including Office 365 subscriptions and Office licensed on-premises, comprising Office, Exchange, SharePoint, Skype for Business, and Microsoft Teams, and related Client Access Licenses ("CALs").
- Office Consumer, including Office 365 subscriptions and Office licensed on-premises, and Office Consumer Services, including Skype, Outlook.com, and OneDrive.
- LinkedIn, including Talent Solutions, Marketing Solutions, and Premium Subscriptions.
- Dynamics business solutions, including Dynamics ERP on-premises, Dynamics CRM on-premises, and Dynamics 365, a set of cloud-based applications across ERP and CRM.

Intelligent Cloud

Our Intelligent Cloud segment consists of our public, private, and hybrid server products and cloud services that can power modern business. This segment primarily comprises:

- Server products and cloud services, including Microsoft SQL Server, Windows Server, Visual Studio, System Center, and related CALs, and Azure.
- Enterprise Services, including Premier Support Services and Microsoft Consulting Services.

More Personal Computing

Our More Personal Computing segment consists of products and services geared towards harmonizing the interests of end users, developers, and IT professionals across all devices. This segment primarily comprises:

- Windows, including Windows original equipment manufacturer licensing and other non-volume licensing of the Windows operating system; Windows Commercial, comprising volume licensing of the Windows operating system, Windows cloud services, and other Windows commercial offerings; patent licensing; Windows Internet of Things ("IoT"); and MSN display advertising.
- Devices, including Microsoft Surface, PC accessories, and other intelligent devices.
- Gaming, including Xbox hardware and Xbox software and services, comprising Xbox Live transactions, subscriptions, and advertising ("Xbox Live"), video games, and third-party video game royalties.
- Search advertising.

Corporate and Other includes adjustments to conform our internal accounting policies to U.S. GAAP, and impairment, integration, and restructuring expenses. Significant internal accounting policies that differ from U.S. GAAP relate to Windows 10 revenue recognition.

Revenue and costs are generally directly attributed to our segments. However, due to the integrated structure of our business, certain revenue recognized and costs incurred by one segment may benefit other segments. Revenue on certain contracts is allocated among the segments based on the relative value of the underlying products and services, which can include allocation based on actual prices charged, prices when sold separately, or estimated costs plus a profit margin. Cost of revenue is allocated in certain cases based on a relative revenue methodology. Operating expenses that are allocated primarily include those relating to marketing of products and services from which multiple segments benefit, and are generally allocated based on relative gross margin.

In addition, certain costs incurred at a corporate level that are identifiable and that benefit our segments are allocated to them. These allocated costs include costs of: legal, including settlements, and fines; information technology; human resources; finance; excise taxes; field selling; shared facilities services; and customer service and support. Each allocation is measured differently based on the specific facts and circumstances of the costs being allocated. Certain corporate-level activity is not allocated to our segments, including impairment, integration, and restructuring expenses.

Segment revenue and operating income (loss) were as follows during the periods presented:

(In millions)

Year Ended June 30,	**2017**	**2016**	**2015**
Revenue			
Productivity and Business Processes	**$ 30,444**	$ 26,487	$ 26,430
Intelligent Cloud	**27,440**	25,042	23,715
More Personal Computing	**38,773**	40,434	43,435
Corporate and Other	**(6,707)**	(6,643)	0
Total	**$ 89,950**	$ 85,320	$ 93,580

(In millions)			
Year Ended June 30,	2017	2016	2015
Operating income (loss)			
Productivity and Business Processes	**$ 11,913**	$ 12,418	$ 13,274
Intelligent Cloud	**9,138**	9,315	9,803
More Personal Computing	**8,288**	6,202	5,095
Corporate and Other	**(7,013)**	(7,753)	(10,011)
Total	**$ 22,326**	$ 20,182	$ 18,161

Corporate and Other operating loss activity was as follows during the periods presented:

(In millions)			
Year Ended June 30,	2017	2016	2015
Net revenue deferral from Windows 10	**$ (6,707)**	$ (6,643)	$ 0
Impairment, integration, and restructuring expenses	**(306)**	(1,110)	(10,011)
Total Corporate and Other	**$ (7,013)**	$ (7,753)	$ (10,011)

No sales to an individual customer or country other than the United States accounted for more than 10% of fiscal year 2017, 2016, or 2015 revenue. Revenue, classified by the major geographic areas in which our customers are located, was as follows:

(In millions)			
Year Ended June 30,	2017	2016	2015
United States (a)	**$ 45,248**	$ 40,578	$ 42,941
Other countries	**44,702**	44,742	50,639
Total	**$ 89,950**	$ 85,320	$ 93,580

(a) *Includes billings to OEMs and certain multinational organizations because of the nature of these businesses and the impracticability of determining the geographic source of the revenue.*

Revenue from external customers, classified by significant product and service offerings, were as follows:

(In millions)			
Year Ended June 30,	2017	2016	2015
Microsoft Office system	**$ 25,389**	$ 23,588	$ 23,538
Server products and tools	**21,758**	19,177	18,612
Xbox	**9,256**	9,395	9,121
Windows PC operating system	**8,625(a)**	8,104(a)	14,826
Advertising	**6,971**	6,098	4,557
Consulting and product support services	**5,588**	5,641	5,090
Devices	**4,557**	7,466	11,602
LinkedIn	**2,268(b)**	0	0
Other	**5,538**	5,851	6,234
Total	**$ 89,950**	$ 85,320	$ 93,580

(a) *Includes the net revenue deferral from Windows 10.*
(b) *Includes advertising revenue*.

Our total commercial cloud revenue, which primarily comprises Office 365 commercial, Azure, Dynamics 365, and other cloud properties, was $14.9 billion, $9.5 billion, and $5.8 billion in fiscal years 2017, 2016, and 2015, respectively. These amounts are included in their respective product categories in the table above.

Assets are not allocated to segments for internal reporting presentations. A portion of amortization and depreciation is included with various other costs in an overhead allocation to each segment; it is impracticable for us to separately identify the amount of amortization and depreciation by segment that is included in the measure of segment profit or loss.

Long-lived assets, excluding financial instruments and tax assets, classified by the location of the controlling statutory company and with countries over 10% of the total shown separately, were as follows:

(In millions)

June 30,	**2017**	**2016**	**2015**
United States	**$ 39,118**	$ 22,819	$ 19,562
Ireland	**12,876**	2,078	1,595
Luxembourg	**6,845**	6,854	6,879
Other countries	**10,123**	8,210	8,469
Total	**$ 68,962**	$ 39,961	$ 36,505

NOTE 22 — QUARTERLY INFORMATION (UNAUDITED)

(In millions, except per share amounts)

Quarter Ended	**September 30**	**December 31**	**March 31**	**June 30**	**Total**
Fiscal Year 2017 (a)					
Revenue (b)	**$ 20,453**	**$ 24,090**	**$ 22,090**	**$ 23,317**	**$ 89,950**
Gross margin	**12,609**	**14,189**	**14,030**	**14,861**	**55,689**
Operating income	**5,225**	**6,177**	**5,594**	**5,330**	**22,326**
Net income	**4,690**	**5,200**	**4,801**	**6,513**(c)	**21,204**(c)
Basic earnings per share	**0.60**	**0.67**	**0.62**	**0.84**	**2.74**
Diluted earnings per share	**0.60**	**0.66**	**0.61**	**0.83**(c)	**2.71**(c)
Fiscal Year 2016					
Revenue (d)	$ 20,379	$ 23,796	$ 20,531	$ 20,614	$ 85,320
Gross margin	13,172	13,924	12,809	12,635	52,540
Operating income	5,793	6,026	5,283	3,080	20,182
Net income	4,902	5,018	3,756	3,122(e)	16,798(e)
Basic earnings per share	0.61	0.63	0.48	0.40	2.12
Diluted earnings per share	0.61	0.62	0.47	0.39(e)	2.10(e)

(a) *On December 8, 2016, we acquired LinkedIn Corporation. LinkedIn has been included in our consolidated results of operations starting on the acquisition date.*

(b) *Reflects the impact of the net revenue deferral from Windows 10 of $1.9 billion, $2.0 billion, $1.5 billion, and $1.4 billion, for the first, second, third, and fourth quarter of fiscal year 2017, respectively, and $6.7 billion for fiscal year 2017.*

(c) *Includes $306 million of employee severance expenses primarily related to our sales and marketing restructuring plan, which decreased operating income, net income, and diluted EPS by $306 million, $243 million, and $0.03, respectively.*

(d) *Reflects the impact of the net revenue deferral from Windows 10 of $1.3 billion, $1.7 billion, $1.6 billion, and $2.0 billion, for the first, second, third, and fourth quarter of fiscal year 2016, respectively, and $6.6 billion for fiscal year 2016.*

(e) *Includes $630 million of asset impairment charges related to our phone business, and $480 million of restructuring charges associated with our 2016 restructuring plans, which together decreased operating income, net income, and diluted EPS by $1.1 billion, $895 million, and $0.11, respectively.*

REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM

To the Board of Directors and Stockholders of Microsoft Corporation
Redmond, Washington

We have audited the accompanying consolidated balance sheets of Microsoft Corporation and subsidiaries (the “Company”) as of June 30, 2017 and 2016, and the related consolidated statements of income, comprehensive income, cash flows, and stockholders’ equity for each of the three years in the period ended June 30, 2017. These financial statements are the responsibility of the Company’s management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, such consolidated financial statements present fairly, in all material respects, the financial position of Microsoft Corporation and subsidiaries as of June 30, 2017 and 2016, and the results of their operations and their cash flows for each of the three years in the period ended June 30, 2017, in conformity with accounting principles generally accepted in the United States of America.

We have also audited, in accordance with the standards of the Public Company Accounting Oversight Board (United States), the Company’s internal control over financial reporting as of June 30, 2017, based on the criteria established in *Internal Control – Integrated Framework (2013)* issued by the Committee of Sponsoring Organizations of the Treadway Commission and our report dated August 2, 2017 expressed an unqualified opinion on the Company’s internal control over financial reporting.

/s/ DELOITTE & TOUCHE LLP

Seattle, Washington
August 2, 2017