

Notes to Consolidated Financial Statements

International Business Machines Corporation and Subsidiary Companies

The company's segments are as follows:

2018 Segments	Changes (+/-)	2019 Segments
Cognitive Solutions	+ Integration Software + Security Services - Divested Select Software* + Red Hat (post closing)	Cloud & Cognitive Software
Global Business Services	- Divested Mortgage Servicing*	Global Business Services
Technology Services & Cloud Platforms	- Security Services - Integration Software	Global Technology Services
Systems		Systems
Global Financing		Global Financing
Other	+ Divested Mortgage Servicing* + Divested Select Software*	Other**

* IBM completed the sale of its mortgage servicing business on February 28, 2019, and completed the sales of select software products (for all countries) and marketing and platform commerce offerings (in the U.S.) on June 30, 2019. Refer to note E, "Acquisitions & Divestitures," for additional information.

**These divested businesses are reported in Other, as it allows for a better representation of the ongoing performance of the reportable segments.

Segment revenue and pre-tax income include transactions between the segments that are intended to reflect an arm's-length, market-based transfer price. Systems that are used by Global Technology Services in outsourcing arrangements are primarily sourced internally from the Systems segment, and software is primarily sourced internally through the Cloud & Cognitive Software and Systems segments. For providing IT services that are used internally, Global Technology Services and Global Business Services recover cost, as well as a reasonable fee, that is intended to reflect the arm's-length value of providing the services. They enter into arm's-length loans at prices equivalent to market rates with Global Financing to facilitate the acquisition of equipment and software used in services engagements. All internal transaction prices are reviewed annually, and reset if appropriate.

The company utilizes globally integrated support organizations to realize economies of scale and efficient use of resources. As a result, a considerable amount of expense is shared by all of the segments. This shared expense includes sales coverage, certain marketing functions and support functions such as Accounting,

Treasury, Procurement, Legal, Human Resources and Billing and Collections. Where practical, shared expenses are allocated based on measurable drivers of expense, e.g., headcount. When a clear and measurable driver cannot be identified, shared expenses are allocated on a financial basis that is consistent with the company's management system, e.g., advertising expense is allocated based on the gross profits of the segments. A portion of the shared expenses, which are recorded in net income, are not allocated to the segments. These expenses are associated with the elimination of internal transactions and other miscellaneous items.

The following tables reflect the results of continuing operations of the company's segments consistent with the management and measurement system utilized within the company and have been recast for the prior-year periods due to the company's January 2019 segment changes. Performance measurement is based on pre-tax income from continuing operations. These results are used, in part, by the chief operating decision maker, both in evaluating the performance of, and in allocating resources to, each of the segments.