

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

**FORM 10-Q**

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

For the Quarterly Period Ended September 30, 2016

OR

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

For the Transition Period From \_\_\_\_\_ to \_\_\_\_\_

Commission File Number: 001-37845

**MICROSOFT CORPORATION**

(Exact name of registrant as specified in its charter)

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

**One Microsoft Way, Redmond, Washington**  
(Address of principal executive offices)

**91-1144442**  
(I.R.S. Employer  
Identification No.)

**98052-6399**  
(Zip Code)

**(425) 882-8080**

(Registrant's telephone number, including area code)

**None**

(Former name, former address and former fiscal year, if changed since last report)

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

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

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

Large accelerated filer

Accelerated filer

Non-accelerated filer  (Do not check if a smaller reporting company)

Smaller reporting company

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

Indicate the number of shares outstanding of each of the issuer's classes of common stock, as of the latest practicable date.

Class

Outstanding at October 14, 2016

Common Stock, \$0.00000625 par value per share

7,775,350,501 shares

**MICROSOFT CORPORATION**  
**FORM 10-Q**  
**For the Quarter Ended September 30, 2016**  
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PART I. FINANCIAL INFORMATION  
ITEM 1. FINANCIAL STATEMENTS  
INCOME STATEMENTS

(In millions, except per share amounts) (Unaudited)

Three Months Ended September 30,	2016	2015
Revenue:		
Product	\$ 13,493	\$ 15,219
Service and other	6,960	5,160
Total revenue	20,453	20,379
Cost of revenue:		
Product	3,581	4,035
Service and other	4,263	3,172
Total cost of revenue	7,844	7,207
Gross margin	12,609	13,172
Research and development	3,106	2,962
Sales and marketing	3,233	3,333
General and administrative	1,045	1,084
Operating income	5,225	5,793
Other income (expense), net	100	(280)
Income before income taxes	5,325	5,513
Provision for income taxes	635	611
Net income	\$ 4,690	\$ 4,902
Earnings per share:		
Basic	\$ 0.60	\$ 0.61
Diluted	\$ 0.60	\$ 0.61
Weighted average shares outstanding:		
Basic	7,789	7,996
Diluted	7,876	8,084
Cash dividends declared per common share	\$ 0.39	\$ 0.36

See accompanying notes.

## COMPREHENSIVE INCOME STATEMENTS

(In millions) (Unaudited)

Three Months Ended September 30,	2016	2015
Net income	<u>\$ 4,690</u>	<u>\$ 4,902</u>
Other comprehensive income (loss):		
Net unrealized gains (losses) on derivatives (net of tax effects of <b>\$(2)</b> and \$23)	<b>(37)</b>	57
Net unrealized gains (losses) on investments (net of tax effects of <b>\$44</b> and \$(308))	<b>83</b>	(571)
Translation adjustments and other (net of tax effects of <b>\$7</b> and \$(12))	<b>98</b>	(270)
Other comprehensive income (loss)	<u>144</u>	<u>(784)</u>
Comprehensive income	<u>\$ 4,834</u>	<u>\$ 4,118</u>

See accompanying notes.

## BALANCE SHEETS

(In millions) (Unaudited)

	September 30, 2016	June 30, 2016
<b>Assets</b>		
Current assets:		
Cash and cash equivalents	\$ 13,928	\$ 6,510
Short-term investments (including securities loaned of \$147 and \$204)	123,004	106,730
<b>Total cash, cash equivalents, and short-term investments</b>	<b>136,932</b>	<b>113,240</b>
Accounts receivable, net of allowance for doubtful accounts of \$284 and \$426	11,129	18,277
Inventories	3,122	2,251
Other	6,726	5,892
<b>Total current assets</b>	<b>157,909</b>	<b>139,660</b>
Property and equipment, net of accumulated depreciation of \$20,885 and \$19,800	19,224	18,356
Equity and other investments	10,486	10,431
Goodwill	17,907	17,872
Intangible assets, net	3,522	3,733
Other long-term assets	3,476	3,416
<b>Total assets</b>	<b>\$ 212,524</b>	<b>\$ 193,468</b>
<b>Liabilities and stockholders' equity</b>		
Current liabilities:		
Accounts payable	\$ 6,296	\$ 6,898
Short-term debt	14,536	12,904
Accrued compensation	3,621	5,264
Income taxes	720	580
Short-term unearned revenue	26,304	27,468
Securities lending payable	210	294
Other	7,123	5,949
<b>Total current liabilities</b>	<b>58,810</b>	<b>59,357</b>
Long-term debt	60,154	40,557
Long-term unearned revenue	7,284	6,441
Deferred income taxes	1,564	1,476
Other long-term liabilities	14,340	13,640
<b>Total liabilities</b>	<b>142,152</b>	<b>121,471</b>
Commitments and contingencies		
Stockholders' equity:		
Common stock and paid-in capital—shares authorized 24,000; outstanding 7,784 and 7,808	67,747	68,178
Retained earnings	944	2,282
Accumulated other comprehensive income	1,681	1,537
<b>Total stockholders' equity</b>	<b>70,372</b>	<b>71,997</b>
<b>Total liabilities and stockholders' equity</b>	<b>\$ 212,524</b>	<b>\$ 193,468</b>

See accompanying notes.

**CASH FLOWS STATEMENTS**

(In millions) (Unaudited)

Three Months Ended September 30,	2016	2015
<b>Operations</b>		
Net income	\$ 4,690	\$ 4,902
Adjustments to reconcile net income to net cash from operations:		
Depreciation, amortization, and other	1,816	1,461
Stock-based compensation expense	703	674
Net recognized losses (gains) on investments and derivatives	(311)	101
Deferred income taxes	15	73
Deferral of unearned revenue	12,583	10,423
Recognition of unearned revenue	(12,904)	(11,355)
Changes in operating assets and liabilities:		
Accounts receivable	7,174	6,376
Inventories	(867)	(937)
Other current assets	(966)	(562)
Other long-term assets	(29)	(5)
Accounts payable	(443)	(135)
Other current liabilities	(361)	(2,024)
Other long-term liabilities	449	(116)
<b>Net cash from operations</b>	<b>11,549</b>	<b>8,876</b>
<b>Financing</b>		
Proceeds from issuance (repayments) of short-term debt, maturities of 90 days or less, net	(3,390)	4,890
Proceeds from issuance of debt	24,977	121
Repayments of debt	(225)	(1,750)
Common stock issued	241	219
Common stock repurchased	(4,362)	(4,757)
Common stock cash dividends paid	(2,800)	(2,475)
Other	(112)	(178)
<b>Net cash from (used in) financing</b>	<b>14,329</b>	<b>(3,930)</b>
<b>Investing</b>		
Additions to property and equipment	(2,163)	(1,356)
Acquisition of companies, net of cash acquired, and purchases of intangible and other assets	(24)	(390)
Purchases of investments	(57,181)	(37,570)
Maturities of investments	8,659	5,686
Sales of investments	32,323	28,502
Securities lending payable	(84)	62
<b>Net cash used in investing</b>	<b>(18,470)</b>	<b>(5,066)</b>
Effect of foreign exchange rates on cash and cash equivalents	10	(44)
<b>Net change in cash and cash equivalents</b>	<b>7,418</b>	<b>(164)</b>
Cash and cash equivalents, beginning of period	6,510	5,595
<b>Cash and cash equivalents, end of period</b>	<b>\$ 13,928</b>	<b>\$ 5,431</b>

See accompanying notes.

## STOCKHOLDERS' EQUITY STATEMENTS

(In millions) (Unaudited)

Three Months Ended September 30,	2016	2015
<b>Common stock and paid-in capital</b>		
Balance, beginning of period	\$ 68,178	\$ 68,465
Common stock issued	241	219
Common stock repurchased	(1,374)	(1,548)
Stock-based compensation expense	703	674
Other, net	(1)	1
Balance, end of period	67,747	67,811
<b>Retained earnings</b>		
Balance, beginning of period	2,282	9,096
Net income	4,690	4,902
Common stock cash dividends	(3,025)	(2,862)
Common stock repurchased	(3,003)	(3,240)
Balance, end of period	944	7,896
<b>Accumulated other comprehensive income</b>		
Balance, beginning of period	1,537	2,522
Other comprehensive income (loss)	144	(784)
Balance, end of period	1,681	1,738
Total stockholders' equity	\$ 70,372	\$ 77,445

See accompanying notes.

**NOTES TO FINANCIAL STATEMENTS**

**(Unaudited)**

**NOTE 1 — ACCOUNTING POLICIES**

**Accounting Principles**

We prepare our unaudited interim consolidated financial statements in accordance with accounting principles generally accepted in the United States of America (“U.S. GAAP”). In the opinion of management, the unaudited interim consolidated financial statements reflect all adjustments of a normal recurring nature that are necessary for a fair presentation of the results for the interim periods presented. Interim results are not necessarily indicative of results for a full year. The information included in this Form 10-Q should be read in conjunction with information included in the Microsoft Corporation 2016 Form 10-K filed with the U.S. Securities and Exchange Commission on July 28, 2016.

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 volume of 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.

**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 Office 365, Microsoft Azure (“Azure”), Microsoft Dynamics (“Dynamics”) CRM Online, and Xbox Live; solution support; and consulting services. Service and other revenue also includes sales from online advertising.



## Recent Accounting Guidance Not Yet Adopted

### *Financial Instruments — Credit Losses*

In June 2016, the Financial Accounting Standards Board (“FASB”) issued a new standard to replace the incurred loss impairment methodology in 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. For trade and other receivables, loans, and other financial instruments, we will be required to use a forward-looking expected loss model rather than the incurred loss model for recognizing credit losses which reflects losses that are probable. 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 new standard will be effective for us beginning July 1, 2020, with early adoption permitted beginning July 1, 2019. Application of the amendments is 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.

### *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 lease assets and lease liabilities on the balance sheet. Most prominent among the amendments is the recognition of assets and liabilities by lessees for those leases classified as operating leases under previous U.S. GAAP. Under the new 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 at the beginning of the earliest period presented using a modified retrospective approach.

The new standard will be effective for us beginning July 1, 2019, with early adoption permitted. We currently anticipate early adoption of the new standard effective July 1, 2017 in conjunction with our adoption of the new revenue standard. Our ability to early adopt is dependent on system readiness, including software procured from third-party providers, and the completion of our analysis of information necessary to restate prior period financial statements.

We anticipate this standard will have a material impact on our consolidated financial statements. While we are continuing to assess all potential impacts of the standard, we currently believe the most significant impact relates to our accounting for office, retail, and datacenter operating leases.

### *Financial Instruments — Recognition, Measurement, Presentation, and Disclosure*

In January 2016, the FASB issued a new standard to amend certain aspects of recognition, measurement, presentation, and disclosure of financial instruments. Most prominent among the amendments is the requirement for changes in the fair value of our equity investments, with certain exceptions, to be recognized through net income rather than other comprehensive income (“OCI”). The new standard will be effective for us beginning July 1, 2018. The application of the amendments will result in a cumulative-effect adjustment to our consolidated balance sheets as of the effective date. We are currently evaluating the impact of this standard on our consolidated financial statements.

### *Revenue from Contracts with Customers*

In May 2014, the FASB issued a new standard related to revenue recognition. Under the new standard, revenue is recognized when a customer obtains control of promised goods or services and is recognized in an amount that reflects the consideration which 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 FASB has recently issued several amendments to the standard, including clarification on accounting for licenses of intellectual property and identifying performance obligations.

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 (the cumulative catch-up transition method). We currently anticipate adopting the standard using the full retrospective method to restate each prior reporting period presented.

The new standard will be effective for us beginning July 1, 2018, and adoption as of the original effective date of July 1, 2017 is permitted. We currently anticipate early adoption of the new standard effective July 1, 2017. Our

ability to early adopt using the full retrospective method is dependent on system readiness, including software procured from third-party providers, and the completion of our analysis of information necessary to restate prior period financial statements.

We anticipate this standard will have a material impact on our consolidated financial statements. While we are continuing to assess all potential impacts of the standard, we currently believe the most significant impact relates to our accounting for software license revenue. We expect revenue related to hardware, cloud offerings, and professional services to remain substantially unchanged. Specifically, under the new standard we expect to recognize Windows 10 revenue predominantly at the time of billing rather than ratably over the life of the related device. We also expect to recognize license revenue at the time of billing rather than over the subscription period from certain multi-year commercial software subscriptions that include both software licenses and Software Assurance. Due to the complexity of certain of our commercial license subscription contracts, the actual revenue recognition treatment required under the standard will be dependent on contract-specific terms, and may vary in some instances from recognition at the time of billing.

We currently believe that the net change in Windows 10 revenue from period to period is indicative of the net change in revenue we expect from the adoption of the new standard.

#### 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 are as follows:

(In millions, except earnings per share)

Three Months Ended September 30,	2016	2015
Net income available for common shareholders (A)	\$ 4,690	\$ 4,902
Weighted average outstanding shares of common stock (B)	7,789	7,996
Dilutive effect of stock-based awards	87	88
Common stock and common stock equivalents (C)	<u>7,876</u>	<u>8,084</u>
<b>Earnings Per Share</b>		
Basic (A/B)	\$ 0.60	\$ 0.61
Diluted (A/C)	\$ 0.60	\$ 0.61

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)

Three Months Ended September 30,	2016	2015
Dividends and interest income	\$ 293	\$ 199
Interest expense	(437)	(249)
Net recognized gains on investments	405	2
Net losses on derivatives	(94)	(103)
Net losses on foreign currency remeasurements	(52)	(36)
Other	(15)	(93)
Total	<u>\$ 100</u>	<u>\$ (280)</u>

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

(In millions)

Three Months Ended September 30,	2016	2015
Other-than-temporary impairments of investments	\$ (18)	\$ (35)
Realized gains from sales of available-for-sale securities	483	107
Realized losses from sales of available-for-sale securities	(60)	(70)
<b>Total</b>	<b>\$ 405</b>	<b>\$ 2</b>

**NOTE 4 — INVESTMENTS**

**Investment Components**

The components of investments, including associated derivatives, but excluding held-to-maturity investments, were as follows:

(In millions)	Cost Basis	Unrealized Gains	Unrealized Losses	Recorded Basis	Cash and Cash Equivalents	Short-term Investments	Equity and Other Investments
<b>September 30, 2016</b>							
Cash	\$ 3,473	\$ 0	\$ 0	\$ 3,473	\$ 3,473	\$ 0	\$ 0
Mutual funds	1,516	0	0	1,516	1,516	0	0
Commercial paper	745	0	0	745	645	100	0
Certificates of deposit	1,304	0	0	1,304	1,128	176	0
U.S. government and agency securities	112,619	116	(34)	112,701	6,916	105,785	0
Foreign government bonds	5,709	9	(18)	5,700	250	5,450	0
Mortgage- and asset-backed securities	4,599	24	(1)	4,622	0	4,622	0
Corporate notes and bonds	6,440	108	(18)	6,530	0	6,530	0
Municipal securities	284	59	0	343	0	343	0
Common and preferred stock	5,395	4,639	(161)	9,873	0	0	9,873
Other investments	585	0	0	585	0	(2)	587
<b>Total</b>	<b>\$ 142,669</b>	<b>\$ 4,955</b>	<b>\$ (232)</b>	<b>\$ 147,392</b>	<b>\$ 13,928</b>	<b>\$ 123,004</b>	<b>\$ 10,460</b>

(In millions)	Cost Basis	Unrealized Gains	Unrealized Losses	Recorded Basis	Cash and Cash Equivalents	Short-term Investments	Equity and Other Investments
<b>June 30, 2016</b>							
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	590	0	0	590	0	(3)	593
<b>Total</b>	<b>\$ 119,053</b>	<b>\$ 4,895</b>	<b>\$ (302)</b>	<b>\$ 123,646</b>	<b>\$ 6,510</b>	<b>\$ 106,730</b>	<b>\$ 10,406</b>

As of September 30, 2016 and June 30, 2016, the recorded bases of common and preferred stock that are restricted for more than one year or are not publicly traded were \$802 million 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.

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. As of September 30, 2016 and June 30, 2016, the collateral received under agreements for loaned securities totaled \$210 million and \$294 million, which is primarily comprised of U.S. government and agency securities.

### 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	Total Unrealized Losses
	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses		
<b>September 30, 2016</b>						
U.S. government and agency securities	\$ 40,654	\$ (26)	\$ 379	\$ (8)	\$ 41,033	\$ (34)
Foreign government bonds	5,081	(1)	38	(17)	5,119	(18)
Mortgage- and asset-backed securities	0	0	214	(1)	214	(1)
Corporate notes and bonds	920	(4)	484	(14)	1,404	(18)
Common and preferred stock	523	(65)	486	(96)	1,009	(161)
<b>Total</b>	<b>\$ 47,178</b>	<b>\$ (96)</b>	<b>\$ 1,601</b>	<b>\$ (136)</b>	<b>\$ 48,779</b>	<b>\$ (232)</b>

(In millions)	Less than 12 Months		12 Months or Greater		Total Fair Value	Total Unrealized Losses
	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses		
<b>June 30, 2016</b>						
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)
<b>Total</b>	<b>\$ 12,188</b>	<b>\$ (165)</b>	<b>\$ 1,967</b>	<b>\$ (137)</b>	<b>\$ 14,155</b>	<b>\$ (302)</b>

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
<b>September 30, 2016</b>		
Due in one year or less	\$ 48,954	\$ 48,970
Due after one year through five years	79,647	79,755
Due after five years through 10 years	1,745	1,788
Due after 10 years	1,354	1,432
<b>Total</b>	<b>\$ 131,700</b>	<b>\$ 131,945</b>

**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 September 30, 2016 and June 30, 2016, the total notional amounts of these foreign exchange contracts sold were \$8.5 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 September 30, 2016 and June 30, 2016, the total notional amounts of these foreign exchange contracts sold were \$5.2 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 September 30, 2016, the total notional amounts of these foreign exchange contracts purchased and sold were \$8.6 billion and \$5.4 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 September 30, 2016, the total notional amounts of equity contracts purchased and sold for managing market price risk were \$1.8 billion and \$2.5 billion, respectively, of which \$737 million and \$986 million, 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 September 30, 2016, the total

notional amounts of fixed-interest rate contracts purchased and sold were \$327 million and \$2.2 billion, 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 September 30, 2016 and June 30, 2016, the total notional derivative amounts of mortgage contracts purchased were \$546 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 September 30, 2016, the total notional amounts of credit contracts purchased and sold were \$384 million and \$271 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 September 30, 2016, the total notional amounts of commodity contracts purchased and sold were \$623 million and \$195 million, respectively. 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 September 30, 2016, 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**

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.

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:

(In millions)	September 30, 2016				June 30, 2016			
	Assets		Liabilities		Assets		Liabilities	
	Short-term Investments	Other Current Assets	Equity and Other Investments	Other Current Liabilities	Short-term Investments	Other Current Assets	Equity and Other Investments	Other Current Liabilities
<b>Non-designated Hedge Derivatives</b>								
Foreign exchange contracts	\$ 12	\$ 134	\$ 0	\$ (68)	\$ 33	\$ 156	\$ 0	\$ (296)
Equity contracts	20	0	0	(3)	23	0	0	(16)
Interest rate contracts	5	0	0	(12)	10	0	0	(25)
Credit contracts	5	0	0	(5)	6	0	0	(5)
Commodity contracts	1	0	0	0	0	0	0	0
<b>Total</b>	<b>\$ 43</b>	<b>\$ 134</b>	<b>\$ 0</b>	<b>\$ (88)</b>	<b>\$ 72</b>	<b>\$ 156</b>	<b>\$ 0</b>	<b>\$ (342)</b>
<b>Designated Hedge Derivatives</b>								
Foreign exchange contracts	\$ 8	\$ 346	\$ 0	\$ (71)	\$ 1	\$ 392	\$ 0	\$ (263)
Equity contracts	0	0	8	(28)	0	0	18	(25)
<b>Total</b>	<b>\$ 8</b>	<b>\$ 346</b>	<b>\$ 8</b>	<b>\$ (99)</b>	<b>\$ 1</b>	<b>\$ 392</b>	<b>\$ 18</b>	<b>\$ (288)</b>
<b>Total gross amounts of derivatives</b>	<b>\$ 51</b>	<b>\$ 480</b>	<b>\$ 8</b>	<b>\$ (187)</b>	<b>\$ 73</b>	<b>\$ 548</b>	<b>\$ 18</b>	<b>\$ (630)</b>
Gross derivatives either offset or subject to an enforceable master netting agreement	\$ 50	\$ 480	\$ 8	\$ (187)	\$ 69	\$ 548	\$ 18	\$ (630)
Gross amounts of derivatives offset on the balance sheet	(54)	(87)	(23)	161	(74)	(302)	(25)	398
Net amounts presented on the balance sheet	(4)	393	(15)	(26)	(5)	246	(7)	(232)
Gross amounts of derivatives not offset on the balance sheet	0	0	0	0	0	0	0	0
Cash collateral received	0	0	0	(245)	0	0	0	(250)
<b>Net amount</b>	<b>\$ (4)</b>	<b>\$ 393</b>	<b>\$ (15)</b>	<b>\$ (271)</b>	<b>\$ (5)</b>	<b>\$ 246</b>	<b>\$ (7)</b>	<b>\$ (482)</b>

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)

Three Months Ended September 30, Foreign Exchange Contracts	2016	2015
Derivatives	\$ (48)	\$ (81)
Hedged items	68	91
<b>Total amount of ineffectiveness</b>	<b>\$ 20</b>	<b>\$ 10</b>
<b>Equity Contracts</b>		
Derivatives	\$ (10)	\$ (33)
Hedged items	10	33
<b>Total amount of ineffectiveness</b>	<b>\$ 0</b>	<b>\$ 0</b>
<b>Amount of equity contracts excluded from effectiveness assessment</b>	<b>\$ (3)</b>	<b>\$ 19</b>

**Cash Flow Hedge Gains (Losses)**

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

(In millions)

Three Months Ended September 30, Effective Portion	2016	2015
Gains recognized in other comprehensive income (net of tax effects of \$1 and \$28)	\$ 35	\$ 161
Gains reclassified from accumulated other comprehensive income into revenue	\$ 75	\$ 109
<b>Amount Excluded from Effectiveness Assessment and Ineffective Portion</b>		
Losses recognized in other income (expense), net	\$ (70)	\$ (82)

We estimate that \$289 million of net derivative gains included in AOCI at September 30, 2016 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 the three months ended September 30, 2016.



**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)

Three Months Ended September 30,	2016	2015
Foreign exchange contracts	\$ (31)	\$ 59
Equity contracts	(17)	34
Interest-rate contracts	4	(1)
Credit contracts	2	(5)
Commodity contracts	(22)	(84)
Total	\$ (64)	\$ 3

**NOTE 6 — 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 traded 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 corporate notes and bonds, common and preferred stock, mortgage- and asset-backed securities, U.S. government and agency securities, and foreign government bonds. 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 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.

**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 <sup>(a)</sup>	Net Fair Value
<b>September 30, 2016</b>						
<b>Assets</b>						
Mutual funds	\$ 1,516	\$ 0	\$ 0	\$ 1,516	\$ 0	\$ 1,516
Commercial paper	0	745	0	745	0	745
Certificates of deposit	0	1,304	0	1,304	0	1,304
U.S. government and agency securities	106,431	6,260	0	112,691	0	112,691
Foreign government bonds	10	5,723	0	5,733	0	5,733
Mortgage- and asset-backed securities	0	4,620	0	4,620	0	4,620
Corporate notes and bonds	0	6,502	1	6,503	0	6,503
Municipal securities	0	343	0	343	0	343
Common and preferred stock	6,696	2,377	18	9,091	0	9,091
Derivatives	6	533	0	539	(164)	375
<b>Total</b>	<b>\$ 114,659</b>	<b>\$ 28,407</b>	<b>\$ 19</b>	<b>\$ 143,085</b>	<b>\$ (164)</b>	<b>\$ 142,921</b>
<b>Liabilities</b>						
Derivatives and other	\$ 3	\$ 184	\$ 0	\$ 187	\$ (161)	\$ 26

(In millions)	Level 1	Level 2	Level 3	Gross Fair Value	Netting <sup>(a)</sup>	Net Fair Value
<b>June 30, 2016</b>						
<b>Assets</b>						
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
<b>Total</b>	<b>\$ 94,438</b>	<b>\$ 24,963</b>	<b>\$ 19</b>	<b>\$ 119,420</b>	<b>\$ (401)</b>	<b>\$ 119,019</b>
<b>Liabilities</b>						
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.

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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)

	September 30, 2016	June 30, 2016
Net fair value of assets measured at fair value on a recurring basis	<b>\$ 142,921</b>	\$ 119,019
Cash	<b>3,473</b>	3,501
Common and preferred stock measured at fair value on a nonrecurring basis	<b>802</b>	767
Other investments measured at fair value on a nonrecurring basis	<b>587</b>	593
Less derivative net assets classified as other current assets	<b>(393)</b>	(246)
Other	<b>2</b>	12
Recorded basis of investment components	<b>\$ 147,392</b>	\$ 123,646

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

During the three months ended September 30, 2016 and 2015, 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)

	September 30, 2016	June 30, 2016
Raw materials	<b>\$ 582</b>	\$ 612
Work in process	<b>110</b>	158
Finished goods	<b>2,430</b>	1,481
Total	<b>\$ 3,122</b>	\$ 2,251

### NOTE 8 — GOODWILL

Changes in the carrying amount of goodwill were as follows:

(In millions)	June 30, 2016	Acquisitions	Other	September 30, 2016
Productivity and Business Processes	\$ 6,678	\$ 2	\$ 22	\$ 6,702
Intelligent Cloud	5,467	0	11	5,478
More Personal Computing	5,727	14	(14)	5,727
Total goodwill	<b>\$ 17,872</b>	<b>\$ 16</b>	<b>\$ 19</b>	<b>\$ 17,907</b>

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.

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**NOTE 9 — 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
			September 30, 2016			June 30, 2016
Technology-based (a)	\$ 6,016	\$ (3,847)	\$ 2,169	\$ 5,970	\$ (3,648)	\$ 2,322
Marketing-related	1,866	(653)	1,213	1,869	(616)	1,253
Contract-based	796	(722)	74	796	(718)	78
Customer-related	470	(404)	66	465	(385)	80
<b>Total</b>	<b>\$ 9,148</b>	<b>\$ (5,626)</b>	<b>\$ 3,522</b>	<b>\$ 9,100</b>	<b>\$ (5,367)</b>	<b>\$ 3,733</b>

(a) *Technology-based intangible assets included \$101 million and \$115 million of net carrying amount of software to be sold, leased, or otherwise marketed as of September 30, 2016 and June 30, 2016, respectively.*

Intangible assets amortization expense was \$214 million and \$242 million for the three months ended September 30, 2016 and 2015, respectively. Amortization of capitalized software was \$14 million and \$18 million for the three months ended September 30, 2016 and 2015, respectively.

The following table outlines the estimated future amortization expense related to intangible assets held as of September 30, 2016:

(In millions)	
<b>Year Ending June 30,</b>	
2017 (excluding the three months ended September 30, 2016)	\$ 563
2018	685
2019	533
2020	456
2021	403
Thereafter	882
<b>Total</b>	<b>\$ 3,522</b>

**NOTE 10 — DEBT**

**Short-term Debt**

As of September 30, 2016, we had \$14.5 billion of commercial paper issued and outstanding, with a weighted-average interest rate of 0.55% and maturities ranging from 47 days to 187 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 November 1, 2016 and November 14, 2018, respectively. These credit facilities serve as a back-up for our commercial paper program. As of September 30, 2016, 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 September 30, 2016, the total carrying value and estimated fair value of our long-term debt were \$60.2 billion and \$64.0 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 and the associated interest rates were as follows as of September 30, 2016 and June 30, 2016:

Due Date	Face Value September 30, 2016	Face Value June 30, 2016	Stated Interest Rate	Effective Interest Rate
	(In millions)			
<b>Notes</b>				
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%
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 (b)	1,967	1,944	2.125%	2.233%
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 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%
December 6, 2028 (b)	1,967	1,944	3.125%	3.218%
May 2, 2033 (b)	617	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%
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 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%
<b>Total</b>	<b>\$ 60,751</b>	<b>\$ 40,949</b>		

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

(b) 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. 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 September 30, 2016 and June 30, 2016, the combined aggregate unamortized discount and debt issuance costs associated with our long-term debt were \$597 million and \$392 million, respectively.

**NOTE 11 — INCOME TAXES**

Our effective tax rate for the three months ended September 30, 2016 and 2015 was 12% and 11%, respectively. Our effective tax rate was lower than the U.S. federal statutory rate 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.

The increase in our current quarter effective tax rate compared to prior year was primarily due to changes in the mix of our income before income taxes between the U.S. and foreign countries, offset by an increase in the tax benefits relating to stock-based compensation.

Tax contingencies and other income tax liabilities were \$12.3 billion and \$11.8 billion as of September 30, 2016 and June 30, 2016, respectively, and are included in other long-term liabilities. This increase relates primarily to current period intercompany transfer pricing.

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. 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 September 30, 2016, 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 also continue to be subject to examination by the IRS for tax years 2010 to 2016.

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 2016, 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 12 — 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 substantially complete as of June 30, 2016, and are expected to be completed by the end of calendar year 2016.

**2016 Restructuring**

We periodically evaluate how to best deploy the company’s resources. In the fourth quarter of 2016, management approved restructuring plans that would result in job eliminations, primarily across our smartphone hardware business and global sales. In addition to the elimination of 1,850 positions that were announced in May 2016, approximately 2,850 roles globally will be reduced during fiscal year 2017 as an extension of the earlier plan. These actions are expected to be completed by the end of the current fiscal year.

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. We do not expect to incur additional charges for these restructuring plans in subsequent years.

Restructuring charges associated with each of these plans were included in impairment, integration, and restructuring expenses on our consolidated income statement, 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 <sup>(a)</sup>	Total
Restructuring liability as of June 30, 2016	\$ 470	\$ 239	\$ 709
Restructuring charges	0	0	0
Cash paid	(161)	(15)	(176)
Restructuring liability as of September 30, 2016	<u>\$ 309</u>	<u>\$ 224</u>	<u>\$ 533</u>

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

**NOTE 13 — UNEARNED REVENUE**

Unearned revenue by segment was as follows:

(In millions)	September 30, 2016	June 30, 2016
Productivity and Business Processes	\$ 11,486	\$ 12,497
Intelligent Cloud	10,322	11,472
More Personal Computing	3,298	3,334
Corporate and Other	8,482	6,606
Total	<u>\$ 33,588</u>	<u>\$ 33,909</u>

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 in the table above. As of September 30, 2016 and June 30, 2016, we deferred a net \$8.5 billion and \$6.6 billion, respectively, in revenue related to Windows 10.

**NOTE 14 — COMMITMENTS AND CONTINGENCIES**

**Capital Lease Commitments**

We have capital leases for datacenters and corporate offices. As of September 30, 2016 and June 30, 2016, assets recorded under capital leases were \$1.1 billion and \$865 million, respectively, and accumulated depreciation associated with capital leases was \$72 million and \$57 million, respectively. For the three months ended September 30, 2016, property and equipment acquired under capital leases was \$267 million. We did not acquire any property and equipment under capital leases for the three months ended September 30, 2015. As of September 30, 2016 and June 30, 2016, capital lease obligations included in other current liabilities were \$32 million and \$25 million, respectively, and capital lease obligations included in other long-term liabilities were \$1.0 billion and \$761 million, respectively.

Future minimum lease payments under non-cancellable capital leases as of September 30, 2016 are as follows:

(In millions)

Year Ending June 30,	
2017 (excluding the three months ended September 30, 2016)	\$ 61
2018	83
2019	85
2020	87
2021	89
Thereafter	1,052
Total (a)	\$ 1,457

(a) As of September 30, 2016, capital leases included imputed interest of \$410 million.

As of September 30, 2016, we had additional purchase obligations for capital leases executed but not yet recorded of \$5.0 billion.

### Other Commitments

On June 11, 2016, we entered into a definitive agreement to acquire LinkedIn Corporation ("LinkedIn") for \$196 per share in an all-cash transaction valued at \$26.2 billion, inclusive of LinkedIn's net cash (the "Merger Agreement"). We will finance the transaction primarily through the issuance of new indebtedness. The Merger Agreement has been unanimously approved by the Boards of Directors of Microsoft and LinkedIn, and has been approved by LinkedIn's shareholders. We expect the acquisition will close in calendar year 2016, subject to satisfaction of certain regulatory approvals and other customary closing conditions. The acquisition is expected to accelerate the growth of LinkedIn, as well as Office 365 and Dynamics.

### 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.

#### *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 have been added to these cases as a defendant. IDT has cases pending against other defendants based on the same patents because most of the patents at issue allegedly relate to 3G and 4G wireless communications standards essential functionality. The cases involving us include three ITC investigations where IDT sought an order excluding importation of 3G and 4G phones into the U.S. and one active case in U.S. District Court in Delaware seeking an injunction and damages. Each of the ITC matters has been 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 appealed this decision to the U.S. Court of Appeals for the Federal Circuit. The Delaware case has been 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. That case is set for trial in September 2018.



*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 2004-2007. In July, 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 vacated the lower court's ruling, and we are awaiting the Supreme Court's full opinion. We expect that the case will be remanded for further proceedings to set an appropriate levy for the 2004-2007 period.

*Other patent and intellectual property claims*

In addition to these cases, there were 58 other patent infringement cases pending against Microsoft as of September 30, 2016.

**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 court granted in part defendants' motion to exclude

plaintiffs' general causation experts. The plaintiffs filed an interlocutory appeal challenging the standard for evaluating expert scientific evidence, which the District of Columbia Court of Appeals agreed to hear *en banc*. Trial court proceedings are stayed pending resolution of the appeal.

#### *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 is not yet active as several defendants remain to be served.

#### **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 September 30, 2016, we accrued aggregate legal liabilities of \$443 million in other current liabilities. While we intend to defend these matters vigorously, adverse outcomes that we estimate could reach approximately \$1.6 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.

#### NOTE 15 — STOCKHOLDERS' EQUITY

#### **Share Repurchases**

On September 16, 2013, our Board of Directors approved a share repurchase program authorizing up to \$40.0 billion in share repurchases. The share repurchase program became effective on October 1, 2013, has no expiration date, and may be suspended or discontinued at any time without notice. As of September 30, 2016, \$3.5 billion remained of our \$40.0 billion share repurchase program. All repurchases were made using cash resources.

On September 20, 2016, our Board of Directors approved a share repurchase program authorizing an additional \$40.0 billion in share repurchases. This share repurchase program will commence following completion of the program approved on September 16, 2013, has no expiration, and may be suspended or discontinued at any time without notice.

We repurchased the following shares of common stock through our share repurchase program approved on September 16, 2013:

(In millions)

Three Months Ended September 30,	2016	2015
Shares of common stock repurchased	63	89
Value of common stock repurchased	\$ 3,550	\$ 4,000

The above table excludes shares repurchased to settle statutory employee tax withholding related to the vesting of stock awards.

**Dividends**

Our Board of Directors declared the following dividends:

Declaration Date	Dividend Per Share	Record Date	Total Amount	Payment Date
			(in millions)	
<b>September 20, 2016</b>	<b>\$ 0.39</b>	<b>November 17, 2016</b>	<b>\$ 3,036</b>	<b>December 8, 2016</b>
September 15, 2015	\$ 0.36	November 19, 2015	\$ 2,868	December 10, 2015

The dividend declared on September 20, 2016 was included in other current liabilities as of September 30, 2016.

**NOTE 16 — ACCUMULATED OTHER COMPREHENSIVE INCOME**

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

(In millions)

Three Months Ended September 30,	2016	2015
<b>Derivatives</b>		
Accumulated other comprehensive income balance, beginning of period	\$ 352	\$ 590
Unrealized gains, net of tax effects of \$1 and \$28	35	161
Reclassification adjustments for gains included in revenue	(75)	(109)
Tax expense included in provision for income taxes	3	5
Amounts reclassified from accumulated other comprehensive income	(72)	(104)
Net current period other comprehensive income (loss)	(37)	57
Accumulated other comprehensive income balance, end of period	\$ 315	\$ 647
<b>Investments</b>		
Accumulated other comprehensive income balance, beginning of period	\$ 2,941	\$ 3,169
Unrealized gains (losses), net of tax effects of \$182 and \$(305)	339	(566)
Reclassification adjustments for gains included in other income (expense), net	(394)	(8)
Tax expense included in provision for income taxes	138	3
Amounts reclassified from accumulated other comprehensive income	(256)	(5)
Net current period other comprehensive income (loss)	83	(571)
Accumulated other comprehensive income balance, end of period	\$ 3,024	\$ 2,598
<b>Translation adjustments and other</b>		
Accumulated other comprehensive loss balance, beginning of period	\$ (1,756)	\$ (1,237)
Translation adjustments and other, net of tax effects of \$7 and \$(12)	98	(270)
Accumulated other comprehensive loss balance, end of period	\$ (1,658)	\$ (1,507)
Accumulated other comprehensive income, end of period	\$ 1,681	\$ 1,738

NOTE 17 — SEGMENT INFORMATION

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.

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 volume licensing and subscriptions to Office 365 commercial for products and services such as Office, Exchange, SharePoint, and Skype for Business, and related Client Access Licenses (“CALs”).
- Office Consumer, including Office sold through retail or through an Office 365 consumer subscription, and Office Consumer Services, including Skype, Outlook.com, and OneDrive.
- Dynamics business solutions, including Dynamics ERP products, Dynamics CRM on-premises, and Dynamics CRM Online.

### **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, as well as 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 screens of all sizes. 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 Embedded; MSN display advertising; and Windows Phone licensing.
- Devices, including Microsoft Surface, phones, and PC accessories.
- 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)

Three Months Ended September 30, Revenue	2016	2015
Productivity and Business Processes	\$ 6,658	\$ 6,306
Intelligent Cloud	6,382	5,892
More Personal Computing	9,294	9,462
Corporate and Other <sup>(a)</sup>	(1,881)	(1,281)
Total revenue	\$ 20,453	\$ 20,379

(In millions)

Three Months Ended September 30, Operating income (loss)	2016	2015
Productivity and Business Processes	\$ 3,120	\$ 3,156
Intelligent Cloud	2,058	2,391
More Personal Computing	1,928	1,527
Corporate and Other <sup>(a)</sup>	(1,881)	(1,281)
Total operating income	\$ 5,225	\$ 5,793

(a) Corporate and Other revenue and operating loss for the three months ended September 30, 2016 and 2015 consisted of net revenue deferrals related to sales of Windows 10.

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, and 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.

**REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM**

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

We have reviewed the accompanying consolidated balance sheet of Microsoft Corporation and subsidiaries (the "Company") as of September 30, 2016, and the related consolidated statements of income, comprehensive income, cash flows, and stockholders' equity for the three-month periods ended September 30, 2016 and 2015. These interim financial statements are the responsibility of the Company's management.

We conducted our reviews in accordance with the standards of the Public Company Accounting Oversight Board (United States). A review of interim financial information consists principally of applying analytical procedures and making inquiries of persons responsible for financial and accounting matters. It is substantially less in scope than an audit conducted in accordance with the standards of the Public Company Accounting Oversight Board (United States), the objective of which is the expression of an opinion regarding the financial statements taken as a whole. Accordingly, we do not express such an opinion.

Based on our reviews, we are not aware of any material modifications that should be made to such consolidated interim financial statements for them to be in conformity with accounting principles generally accepted in the United States of America.

We have previously audited, in accordance with the standards of the Public Company Accounting Oversight Board (United States), the consolidated balance sheet of the Company as of June 30, 2016, and the related consolidated statements of income, comprehensive income, cash flows, and stockholders' equity for the year then ended (not presented herein); and in our report dated July 28, 2016 we expressed an unqualified opinion on those consolidated financial statements. In our opinion, the information set forth in the accompanying consolidated balance sheet as of June 30, 2016 is fairly stated, in all material respects, in relation to the consolidated balance sheet from which it has been derived.

/s/ DELOITTE & TOUCHE LLP

Seattle, Washington

October 20, 2016

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

### Note About Forward-Looking Statements

This report includes estimates, projections, statements relating to our business plans, objectives, and expected operating results that are "forward-looking statements" within the meaning of the Private Securities Litigation Reform Act of 1995, Section 27A of the Securities Act of 1933, and Section 21E of the Securities Exchange Act of 1934. Forward-looking statements may appear throughout this report, including the following sections: "Management's Discussion and Analysis of Financial Condition and Results of Operations," and "Risk Factors." These forward-looking statements generally are identified by the words "believe," "project," "expect," "anticipate," "estimate," "intend," "strategy," "future," "opportunity," "plan," "may," "should," "will," "would," "will be," "will continue," "will likely result," and similar expressions. Forward-looking statements are based on current expectations and assumptions that are subject to risks and uncertainties that may cause actual results to differ materially. We describe risks and uncertainties that could cause actual results and events to differ materially in "Risk Factors" (Part II, Item 1A of this Form 10-Q), "Quantitative and Qualitative Disclosures about Market Risk" (Part I, Item 3 of this Form 10-Q), and "Management's Discussion and Analysis of Financial Condition and Results of Operations" (Part I, Item 2 of this Form 10-Q). We undertake no obligation to update or revise publicly any forward-looking statements, whether because of new information, future events, or otherwise.

### OVERVIEW

The following Management's Discussion and Analysis of Financial Condition and Results of Operations ("MD&A") is intended to help the reader understand the results of operations and financial condition of Microsoft Corporation. MD&A is provided as a supplement to, and should be read in conjunction with, our Annual Report on Form 10-K for the year ended June 30, 2016, and our financial statements and the accompanying Notes to Financial Statements (Part 1, Item 1 of this Form 10-Q).

Microsoft is a technology company whose mission is to empower every person and every organization on the planet to achieve more. Our strategy is to build best-in-class platforms and productivity services for a mobile-first, cloud-first world. We develop, license, and support a wide range of software products, services, and devices that deliver new opportunities, greater convenience, and enhanced value to people's lives.

We generate revenue by licensing and supporting an array of software products, by offering a wide range of services, including cloud-based services to consumers and businesses, by designing, manufacturing, and selling devices that integrate with our cloud-based services, and by delivering relevant online advertising to a global audience. Our most significant expenses are related to compensating employees; designing, manufacturing, marketing, and selling our products and services; datacenter costs in support of our cloud-based services; and income taxes.

Highlights from the first quarter of fiscal year 2017 included:

- Commercial cloud annualized revenue run rate\* exceeded \$13 billion.
- Office Commercial revenue grew 5%, driven by Office 365 commercial revenue growth of 51%.
- Office 365 consumer subscribers increased to 24 million.
- Microsoft Dynamics ("Dynamics") revenue grew 11%, driven by Dynamics CRM Online revenue growth.
- Server products and cloud services revenue grew 11%, driven by Microsoft Azure ("Azure") revenue growth.
- Azure revenue grew 116%, with Azure compute usage more than doubling year-over-year.
- Search advertising revenue, excluding traffic acquisition costs, grew 9%, driven by increased revenue per search and search volume.

\* *Commercial cloud annualized revenue run rate is calculated by multiplying revenue for the last month of the quarter by twelve for Office 365 commercial, Azure, Dynamics online, and other cloud properties.*

In June 2016, we entered into a definitive agreement to acquire LinkedIn Corporation ("LinkedIn") for \$196 per share in an all-cash transaction valued at \$26.2 billion, inclusive of LinkedIn's net cash (the "Merger Agreement"). We will finance the transaction primarily through the issuance of new indebtedness. The Merger Agreement has been unanimously approved by the Boards of Directors of Microsoft and LinkedIn, and has been approved by LinkedIn's shareholders. We expect the acquisition will close in calendar year 2016, subject to satisfaction of certain regulatory approvals and other customary closing conditions. The acquisition is expected to accelerate the growth of LinkedIn, as well as Office 365 and Dynamics.



In May 2016, we announced the sale of our entry-level feature phone business for \$350 million. The transaction is expected to close by the end of calendar year 2016, subject to regulatory approvals and other closing conditions.

In July 2015, we announced a plan to restructure our phone business to better focus and align resources. In May 2016, we announced plans to further streamline our smartphone hardware business. These changes in the phone business reinforce our strategy to create a vibrant Windows ecosystem with a single set of experiences across our first-party device family and original equipment manufacturer (“OEM”) offerings. Part of this strategy involves focusing our phone devices on a narrower range of customer categories and differentiating through the combination of hardware and software we are uniquely positioned to offer. As anticipated, our change in phone strategy resulted in a reduction in units sold and associated expenses in fiscal year 2016, and this trend is expected to continue in fiscal year 2017.

### **Industry Trends**

Our industry is dynamic and highly competitive, with frequent changes in both technologies and business models. Each industry shift is an opportunity to conceive new products, new technologies, or new ideas that can further transform the industry and our business. At Microsoft, we push the boundaries of what is possible through a broad range of research and development activities that seek to identify and address the changing demands of customers and users, industry trends, and competitive forces.

### **Economic Conditions, Challenges, and Risks**

The market for software, devices, and cloud-based services is dynamic and highly competitive. Our competitors are developing new software and devices, while also deploying competing cloud-based services for consumers and businesses. The devices and form factors customers prefer evolve rapidly, and influence how users access services in the cloud, and in some cases, the user’s choice of which suite of cloud-based services to use. We must continue to evolve and adapt over an extended time in pace with this changing environment. The investments we are making in devices and infrastructure will continue to increase our operating costs and may decrease our operating margins.

Our success is highly dependent on our ability to attract and retain qualified employees. We hire a mix of university and industry talent worldwide. Microsoft competes for talented individuals globally by offering an exceptional working environment, broad customer reach, scale in resources, the ability to grow one’s career across many different products and businesses, and competitive compensation and benefits. Aggregate demand for our software, services, and devices is correlated to global macroeconomic and geopolitical factors, which remain dynamic.

Our international operations provide a significant portion of our total revenue and expenses. Many of these revenue and expenses are denominated in currencies other than the U.S. dollar. As a result, changes in foreign exchange rates may significantly affect revenue and expenses. The strengthening of the U.S. dollar relative to certain foreign currencies throughout fiscal year 2016, and continuing into fiscal year 2017, negatively impacted reported revenue and reduced reported expenses from our international operations.

See a discussion of these factors and other risks under Risk Factors (Part II, Item 1A of this Form 10-Q).

### **Seasonality**

Our revenue historically has fluctuated quarterly and has generally been highest in the second quarter of our fiscal year due to corporate calendar year-end spending trends in our major markets and holiday season spending by consumers.

### **Reportable Segments**

The segment amounts included in MD&A are presented on a basis consistent with our internal management reporting. Segment information appearing in Note 17–Segment Information of the Notes to Financial Statements (Part I, Item 1 of this Form 10-Q) is also presented on this basis. All differences between our internal management reporting basis and accounting principles generally accepted in the United States (“U.S. GAAP”), along with certain corporate-level and other activity, are included in Corporate and Other.

During the periods presented, we reported our financial performance based on the following segments; Productivity and Business Processes, Intelligent Cloud, and More Personal Computing. We expect to report the financial performance of LinkedIn as part of our Productivity and Business Processes segment.

Additional information on our reportable segments is contained in Note 17—Segment Information of the Notes to Financial Statements (Part I, Item 1 of this Form 10-Q).

### SUMMARY RESULTS OF OPERATIONS

(In millions, except percentages and per share amounts)	Three Months Ended September 30,		Percentage Change
	2016	2015	
Revenue	\$ 20,453	\$ 20,379	0%
Gross margin	\$ 12,609	\$ 13,172	(4)%
Operating income	\$ 5,225	\$ 5,793	(10)%
Diluted earnings per share	\$ 0.60	\$ 0.61	(2)%

Revenue increased \$74 million, driven by growth in Intelligent Cloud and Productivity and Business Processes, offset in part by an increase in the net revenue deferral from Windows 10 and lower revenue from More Personal Computing. Windows 10 revenue 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. Intelligent Cloud revenue increased, primarily due to higher revenue from server products and cloud services. Productivity and Business Processes revenue increased, driven by higher revenue from Office 365. More Personal Computing revenue decreased, mainly due to lower revenue from Devices and Gaming, offset in part by higher revenue from Search advertising. Revenue included an unfavorable foreign currency impact of 2%.

Operating income decreased \$568 million or 10%, primarily due to lower gross margin and an increase in research and development expenses, offset in part by lower sales and marketing expenses. Operating income included an unfavorable foreign currency impact of 5%. Gross margin decreased \$563 million or 4%, driven by higher cost of revenue. Gross margin included an unfavorable foreign currency impact of 2%.

Key changes in expenses were:

- Cost of revenue increased \$637 million or 9%, mainly due to growth in our commercial cloud and Search advertising traffic acquisition costs, offset in part by a reduction in phone sales.
- Research and development expenses increased \$144 million or 5%, primarily due to increased strategic investments and acquisitions to drive cloud engineering, offset in part by a reduction in phone expenses.
- Sales and marketing expenses decreased \$100 million or 3%, primarily due to a reduction in phone expenses and Windows 10 launch-related expenses in the prior year, offset in part by increased investment to drive sales capacity in our commercial cloud.

Diluted earnings per share ("EPS") was \$0.60 for the three months ended September 30, 2016. Current year diluted EPS was negatively impacted by the net revenue deferral from Windows 10, which resulted in a decrease to diluted EPS of \$0.16. Diluted EPS was \$0.61 for the three months ended September 30, 2015. Prior year diluted EPS was negatively impacted by the net revenue deferral from Windows 10, which resulted in a decrease to diluted EPS of \$0.09.

SEGMENT RESULTS OF OPERATIONS

(In millions, except percentages)	Three Months Ended September 30,		Percentage Change
	2016	2015	
<b>Revenue</b>			
Productivity and Business Processes	\$ 6,658	\$ 6,306	6%
Intelligent Cloud	6,382	5,892	8%
More Personal Computing	9,294	9,462	(2)%
Corporate and Other	(1,881)	(1,281)	(47)%
<b>Total revenue</b>	<b>\$ 20,453</b>	<b>\$ 20,379</b>	<b>0%</b>
<b>Operating income (loss)</b>			
Productivity and Business Processes	\$ 3,120	\$ 3,156	(1)%
Intelligent Cloud	2,058	2,391	(14)%
More Personal Computing	1,928	1,527	26%
Corporate and Other	(1,881)	(1,281)	(47)%
<b>Total operating income</b>	<b>\$ 5,225</b>	<b>\$ 5,793</b>	<b>(10)%</b>

**Reportable Segments**Productivity and Business Processes

Revenue increased \$352 million or 6%, primarily due to higher revenue from Office 365. Revenue included an unfavorable foreign currency impact of 2%.

- Office Commercial revenue increased \$264 million or 5%, driven by higher revenue from Office 365 commercial, mainly due to growth in subscribers, offset in part by lower revenue from products licensed on-premises, reflecting a continued shift to Office 365 commercial. Revenue included an unfavorable foreign currency impact of 3%.
- Office Consumer revenue increased \$58 million or 8%, driven by higher revenue from Office 365 consumer, mainly due to growth in subscribers.
- Dynamics revenue increased 11%, mainly due to higher revenue from Dynamics CRM Online, driven by seat growth.

Operating income decreased slightly, primarily due to higher operating expenses. Operating expenses increased \$35 million or 2%, mainly due to higher research and development expenses, driven by investments in cloud engineering. Operating income included an unfavorable foreign currency impact of 3%. Gross margin was flat, reflecting higher cost of revenue, offset by higher revenue. Gross margin included an unfavorable foreign currency impact of 2%. Cost of revenue increased \$353 million or 34%, driven by an increased mix of cloud offerings.

Intelligent Cloud

Revenue increased \$490 million or 8%, due to higher revenue from server products and cloud services. Revenue included an unfavorable foreign currency impact of 2%.

- Server products and cloud services revenue grew \$486 million or 11%, driven by Azure revenue growth of 116%, as well as growth in revenue from our server products licensed on-premises.
- Enterprise Services revenue increased 1%, driven by growth in revenue from Premier Support Services and Microsoft Consulting Services, offset in part by a decline in revenue from custom support agreements.

Operating income decreased \$333 million or 14%, primarily due to higher operating expenses. Operating expenses increased \$408 million or 21%, mainly due to higher research and development expenses and sales and marketing expenses. Research and development expenses increased \$196 million or 26% and sales and marketing expenses

increased \$191 million or 22%, driven by strategic investments and acquisitions to drive cloud engineering, sales capacity, and developer engagement. Operating income included an unfavorable foreign currency impact of 3%. Gross margin increased \$75 million or 2%, mainly due to higher revenue, offset in part by higher cost of revenue. Gross margin included an unfavorable foreign currency impact of 2%. Cost of revenue increased \$415 million or 27%, driven by an increased mix of cloud offerings.

More Personal Computing

Revenue decreased \$168 million or 2%, mainly due to lower revenue from Devices and Gaming, offset in part by higher revenue from Search advertising.

- Devices revenue decreased \$493 million or 27%, mainly due to lower revenue from phones, offset in part by higher Microsoft Surface (“Surface”) revenue. Phone revenue decreased \$799 million or 72%, driven by a reduction in volume of phones sold. Surface revenue increased \$253 million or 38%, primarily driven by a higher mix of premium devices sold.
- Gaming revenue decreased \$110 million or 5%, primarily due to lower Xbox hardware revenue, offset in part by higher revenue from Xbox software and services. Xbox hardware revenue decreased 26%, mainly due to lower prices of consoles sold and a decline in volume of consoles sold. Xbox software and services revenue increased 6%, driven by a higher volume of Xbox Live transactions and revenue per transaction.
- Search advertising revenue increased \$409 million or 40%. Search advertising revenue, excluding traffic acquisition costs, increased 9%, primarily driven by growth in Bing, due to higher revenue per search and search volume.
- Windows revenue increased slightly, mainly due to higher revenue from patent licensing. Windows OEM licensing (“Windows OEM”) revenue was flat, slightly ahead of the PC market. Windows OEM Pro revenue grew 1%, generally in line with the commercial PC market, and Windows OEM non-Pro revenue declined 1%, slightly outperforming the consumer PC market.

Operating income increased \$401 million or 26%, primarily due to lower operating expenses. Operating expenses decreased \$438 million or 13%, mainly due to lower sales and marketing expenses and research and development expenses. Sales and marketing expenses decreased \$245 million or 18% and research and development expenses decreased \$139 million or 9%, driven by a reduction in phone expenses. The decrease in sales and marketing expenses also reflects Windows 10 launch-related expenses in the prior year. Operating income included an unfavorable foreign currency impact of 5%. Gross margin decreased slightly, reflecting lower revenue, offset in part by a reduction in cost of revenue. Cost of revenue decreased \$131 million or 3%, driven by a reduction in phone sales, offset in part by an increase in Search advertising traffic acquisition costs and Surface cost of revenue. Surface cost of revenue increased, primarily driven by a higher mix of premium devices sold. Gross margin included an unfavorable foreign currency impact of 2%.

**Corporate and Other**

Corporate and Other revenue is comprised of revenue deferrals related to Windows 10. Corporate and Other operating income (loss) is comprised of Windows 10 revenue deferrals and corporate-level activity not specifically allocated to a segment, including impairment, integration, and restructuring expenses.

Revenue decreased and operating loss increased, due to a \$600 million increase in net revenue deferrals from Windows 10. During the three months ended September 30, 2016 and 2015, we deferred net revenue from Windows 10 of \$1.9 billion and \$1.3 billion, respectively.

OPERATING EXPENSES

**Research and Development**

(In millions, except percentages)	Three Months Ended September 30,		Percentage Change
	2016	2015	
Research and development	\$ 3,106	\$ 2,962	5%
As a percent of revenue	15%	15%	Oppt

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.

Research and development expenses increased \$144 million or 5%, primarily due to increased strategic investments and acquisitions to drive cloud engineering, offset in part by a reduction in phone expenses.

### Sales and Marketing

(In millions, except percentages)	Three Months Ended September 30,		Percentage Change
	2016	2015	
Sales and marketing	\$ 3,233	\$ 3,333	(3)%
As a percent of revenue	16%	16%	Oppt

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.

Sales and marketing expenses decreased \$100 million or 3%, primarily due to a reduction in phone expenses and Windows 10 launch-related expenses in the prior year, offset in part by increased investments to drive sales capacity in our commercial cloud.

### General and Administrative

(In millions, except percentages)	Three Months Ended September 30,		Percentage Change
	2016	2015	
General and administrative	\$ 1,045	\$ 1,084	(4)%
As a percent of revenue	5%	5%	Oppt

General and administrative expenses include payroll, employee benefits, stock-based compensation expense, severance expense, and other headcount-related expenses associated with finance, legal, facilities, certain human resources and other administrative personnel, certain taxes, and legal and other administrative fees.

General and administrative expenses decreased \$39 million or 4%, primarily due to a reduction in phone expenses and lower employee-related expenses.

### OTHER INCOME (EXPENSE), NET

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

(In millions)	Three Months Ended September 30,	
	2016	2015
Dividends and interest income	\$ 293	\$ 199
Interest expense	(437)	(249)
Net recognized gains on investments	405	2
Net losses on derivatives	(94)	(103)
Net losses on foreign currency remeasurements	(52)	(36)
Other	(15)	(93)
<b>Total</b>	<b>\$ 100</b>	<b>\$ (280)</b>

We use derivative instruments to: manage risks related to foreign currencies, equity prices, interest rates, and credit; enhance investment returns; and facilitate portfolio diversification. Gains and losses from changes in fair values of derivatives that are not designated as hedges 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 and gains (losses) on certain balance sheet amounts from foreign exchange rate changes.

Dividends and interest income increased due to higher portfolio balances and yields on fixed-income securities. Interest expense increased due to higher outstanding long-term debt. Net recognized gains on investments increased primarily due to higher gains on sales of equity securities. Net losses on derivatives decreased slightly due to lower losses on commodity and foreign currency derivatives compared to the prior year and gains on interest rate derivatives as compared to losses in the prior year, offset in part by losses on equity contracts as compared to gains in the prior year. Other reflects losses recognized from certain joint ventures for both periods presented, and prior year includes losses from divestitures.

#### INCOME TAXES

Our effective tax rate for the three months ended September 30, 2016 and 2015 was 12% and 11%, respectively. Our effective tax rate was lower than the U.S. federal statutory rate 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.

The increase in our current quarter effective tax rate compared to prior year was primarily due to changes in the mix of our income before income taxes between the U.S. and foreign countries, offset by an increase in the tax benefits relating to stock-based compensation.

Tax contingencies and other income tax liabilities were \$12.3 billion and \$11.8 billion as of September 30, 2016 and June 30, 2016, respectively, and are included in other long-term liabilities. This increase relates primarily to current period intercompany transfer pricing.

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. 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 September 30, 2016, 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 also continue to be subject to examination by the IRS for tax years 2010 to 2016.

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 2016, 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.

#### FINANCIAL CONDITION

##### **Cash, Cash Equivalents, and Investments**

Cash, cash equivalents, and short-term investments totaled \$136.9 billion as of September 30, 2016, compared with \$113.2 billion as of June 30, 2016. Equity and other investments were \$10.5 billion as of September 30, 2016, compared with \$10.4 billion as of June 30, 2016. Our short-term investments are primarily intended to facilitate liquidity and for capital preservation. They consist predominantly of highly liquid investment-grade fixed-income securities, diversified among industries and individual issuers. The investments are predominantly U.S. dollar-denominated securities, but also include foreign currency-denominated securities in order to diversify risk. Our fixed-income investments are exposed to interest rate risk and credit risk. The credit risk and average maturity of our fixed-income portfolio are managed to achieve economic returns that correlate to certain fixed-income indices. The settlement risk related to these investments is insignificant given that the short-term investments held are primarily highly liquid investment-grade fixed-income securities.

Of the cash, cash equivalents, and short-term investments as of September 30, 2016, \$111.1 billion was held by our foreign subsidiaries and would be subject to material repatriation tax effects. The amount of cash, cash equivalents, and short-term investments held by foreign subsidiaries subject to other restrictions on the free flow of funds (primarily currency and other local regulatory) was \$2.4 billion. As of September 30, 2016, approximately 83% of the

cash equivalents and short-term investments held by our foreign subsidiaries were invested in U.S. government and agency securities, approximately 4% were invested in corporate notes and bonds of U.S. companies, and approximately 4% were invested in U.S. mortgage- and asset-backed securities, all of which are denominated in U.S. dollars. The remaining cash equivalents and short-term investments held by our foreign subsidiaries were invested in foreign securities.

#### *Securities lending*

We lend certain fixed-income and equity securities to increase investment returns. 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. Collateral received is recorded as an asset with a corresponding liability. Our securities lending payable balance was \$210 million as of September 30, 2016. Our average and maximum securities lending payable balances for the three months ended September 30, 2016 were \$514 million and \$1.2 billion, respectively. Intra-year variances in the amount of securities loaned are mainly due to fluctuations in the demand for the securities.

#### *Valuation*

In general, and where applicable, we use quoted prices in active markets for identical assets or liabilities to determine the fair value of our financial instruments. This pricing methodology applies to our Level 1 investments, such as exchange-traded mutual funds, domestic and international equities, and U.S. government securities. If quoted prices in active markets for identical assets or liabilities are not available to determine fair value, then we use quoted prices for similar assets and liabilities or inputs other than the quoted prices that are observable either directly or indirectly. This pricing methodology applies to our Level 2 investments such as corporate notes and bonds, common and preferred stock, foreign government bonds, mortgage- and asset-backed securities, U.S. government and agency securities, and certificates of deposit. Level 3 investments are valued using internally developed models with unobservable inputs. Assets and liabilities measured at fair value on a recurring basis using unobservable inputs are an immaterial portion of our portfolio.

A majority of our investments are priced by pricing vendors and are generally Level 1 or Level 2 investments as these vendors either provide a quoted market price in an active market or use observable inputs for their pricing without applying significant adjustments. Broker pricing is used mainly when a quoted price is not available, the investment is not priced by our pricing vendors, or when a broker price is more reflective of fair values in the market in which the investment trades. Our broker-priced investments are generally classified as Level 2 investments because the broker prices these investments based on similar assets without applying significant adjustments. In addition, all of our broker-priced investments have a sufficient level of trading volume to demonstrate that the fair values used are appropriate for these investments. Our fair value processes include controls that are designed to ensure appropriate fair values are recorded. These controls include model validation, review of key model inputs, analysis of period-over-period fluctuations, and independent recalculation of prices where appropriate.

#### **Cash Flows**

Cash flows from operations increased \$2.7 billion to \$11.5 billion for the three months ended September 30, 2016, mainly due to an increase in cash received from customers and unsettled cash equivalent investments in government securities as of quarter end. Cash from financing increased \$18.3 billion to \$14.3 billion, mainly due to an \$18.1 billion increase in proceeds from issuances of debt, net of repayments, and a \$395 million decrease in cash used for common stock repurchases, offset in part by a \$325 million increase in dividends paid. Cash used in investing increased \$13.4 billion to \$18.5 billion, mainly due to a \$12.8 billion increase in cash used for net investment purchases, sales, and maturities, and an \$807 million increase in cash used for additions to property and equipment, offset in part by a \$366 million decrease in cash used for acquisitions of companies, net of cash acquired, and purchases of intangibles and other assets.

#### **Debt**

We issued debt to take advantage of favorable pricing and liquidity in the debt markets, reflecting our credit rating and the low interest rate environment. The proceeds of these issuances were or will be used for general corporate purposes, which may include, among other things, funding for working capital, capital expenditures, repurchases of capital stock, acquisitions, and repayment of existing debt. See Note 10 – Debt of the Notes to Financial Statements (Part 1, Item 1 of this Form 10-Q) for further discussion.

## Unearned Revenue

Unearned revenue as of September 30, 2016 was comprised mainly of unearned revenue from volume licensing programs. Unearned revenue from volume licensing programs represents customer billings for multi-year licensing arrangements paid for either at inception of the agreement or annually at the beginning of each coverage period and accounted for as subscriptions with revenue recognized ratably over the coverage period. Unearned revenue as of September 30, 2016 also included payments for: Windows 10 licenses; post-delivery support and consulting services to be performed in the future; Office 365 subscriptions; Xbox Live subscriptions; Dynamics business solutions products; Skype prepaid credits and subscriptions; bundled products and services; and other offerings for which we have been paid in advance and earn the revenue when we provide the service or software, or otherwise meet the revenue recognition criteria.

The following table outlines the expected future recognition of unearned revenue as of September 30, 2016:

(In millions)

### Three Months Ending,

December 31, 2016	\$ 11,138
March 31, 2017	8,020
June 30, 2017	5,130
September 30, 2017	2,016
Thereafter	7,284
Total	<u>\$ 33,588</u>

If our customers choose to license cloud-based versions of our products and services rather than licensing transaction-based products and services, the associated revenue will shift from being recognized at the time of the transaction to being recognized over the subscription period or upon consumption, as applicable.

## Share Repurchases

On September 16, 2013, our Board of Directors approved a share repurchase program authorizing up to \$40.0 billion in share repurchases. The share repurchase program became effective on October 1, 2013, has no expiration date, and may be suspended or discontinued at any time without notice. As of September 30, 2016, \$3.5 billion remained of our \$40.0 billion share repurchase program. While the program has no expiration date, we intend to complete it by December 31, 2016.

On September 20, 2016, our Board of Directors approved a share repurchase program authorizing an additional \$40.0 billion in share repurchases. This share repurchase program will commence following completion of the program approved on September 16, 2013, has no expiration, and may be suspended or discontinued at any time without notice.

During the three months ended September 30, 2016, we repurchased 63 million shares of Microsoft common stock for \$3.6 billion under the share repurchase program approved on September 16, 2013. All repurchases were made using cash resources.

## Dividends

See Note 15 – Stockholders' Equity of the Notes to Financial Statements (Part 1, Item 1 of this Form 10-Q) for further discussion.

## Off-Balance Sheet Arrangements

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. In evaluating estimated losses on these indemnifications, we consider factors such as the degree of probability of an unfavorable outcome and our ability to make a reasonable estimate of the amount of loss. These obligations did not have a material impact on our consolidated financial statements during the periods presented.



## **Other Planned Uses of Capital**

In June 2016, we entered into a definitive agreement to acquire LinkedIn in an all-cash transaction valued at \$26.2 billion, inclusive of LinkedIn's net cash. We expect the acquisition will close in calendar year 2016, and we will finance the transaction primarily through the issuance of new debt.

We will continue to invest in sales, marketing, product support infrastructure, and existing and advanced areas of technology, as well as continue making acquisitions that align with our business strategy. Additions to property and equipment will continue, including new facilities, datacenters, and computer systems for research and development, sales and marketing, support, and administrative staff. We expect capital expenditures to increase in coming years in support of growth in our cloud offerings. We have operating leases for most U.S. and international sales and support offices and certain equipment. We have not engaged in any related party transactions or arrangements with unconsolidated entities or other persons that are reasonably likely to materially affect liquidity or the availability of capital resources.

## **Liquidity**

We earn a significant amount of our operating income outside the U.S., which is deemed to be permanently reinvested in foreign jurisdictions. As a result, as discussed above under Cash, Cash Equivalents, and Investments, the majority of our cash, cash equivalents, and short-term investments are held by foreign subsidiaries. We currently do not intend nor foresee a need to repatriate these funds. We expect existing domestic cash, cash equivalents, short-term investments, cash flows from operations, and access to capital markets to continue to be sufficient to fund our domestic operating activities and cash commitments for investing and financing activities, such as regular quarterly dividends, debt maturities, and material capital expenditures, for at least the next 12 months and thereafter for the foreseeable future. In addition, we expect existing foreign cash, cash equivalents, short-term investments, and cash flows from operations to continue to be sufficient to fund our foreign operating activities and cash commitments for investing activities, such as material capital expenditures, for at least the next 12 months and thereafter for the foreseeable future.

Should we require more capital in the U.S. than is generated by our operations domestically, for example to fund significant discretionary activities, such as business acquisitions and share repurchases, we could elect to repatriate future earnings from foreign jurisdictions or raise capital in the U.S. through debt or equity issuances. These alternatives could result in higher effective tax rates, increased interest expense, or dilution of our earnings. We have borrowed funds domestically and continue to believe we have the ability to do so at reasonable interest rates.

### RECENT ACCOUNTING GUIDANCE

See Note 1 – Accounting Policies of the Notes to Financial Statements (Part 1, Item 1 of this Form 10-Q) for further discussion.

### APPLICATION OF CRITICAL ACCOUNTING POLICIES

Our consolidated financial statements and accompanying notes are prepared in accordance with U.S. GAAP. Preparing consolidated financial statements requires management to make estimates and assumptions that affect the reported amounts of assets, liabilities, revenue, and expenses. These estimates and assumptions are affected by management's application of accounting policies. Critical accounting policies for us include revenue recognition, impairment of investment securities, goodwill, research and development costs, contingencies, income taxes, and inventories.

## **Revenue Recognition**

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.

Judgment is also required to assess whether future releases of certain software represent new products or upgrades and enhancements to existing products. Certain volume licensing arrangements include a perpetual license for

current products combined with rights to receive unspecified future versions of software products and are accounted for as subscriptions, with billings recorded as unearned revenue and recognized as revenue ratably over the coverage period.

Software updates are evaluated on a case-by-case basis to determine whether they meet the definition of an upgrade, which may require revenue to be deferred and recognized when the upgrade is delivered. If it is determined that implied post-contract customer support ("PCS") is being provided, revenue from the arrangement is deferred and recognized over the implied PCS term. If updates are determined to not meet the definition of an upgrade, revenue is generally recognized as products are shipped or made available.

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.

In January 2015, we announced Windows 10 would be free to all qualified existing users of Windows 7 and Windows 8.1. This offer differs from historical offers preceding the launch of new versions of Windows as it is being made available for free to existing users in addition to new customers after the offer announcement. We evaluated the nature and accounting treatment of the Windows 10 offer and determined that it represents a marketing and promotional activity, in part because the offer is being made available for free to existing users. As this is a marketing and promotional activity, revenue recognition of new sales of Windows 8 will continue to be recognized as delivered.

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. 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.

We currently are evaluating the impact of the new standard related to revenue recognition, which we anticipate will have a material impact on our consolidated financial statements. See Note 1 – Accounting Policies of the Notes to Financial Statements (Part I, Item 1 of this Form 10-Q) for further discussion.

### **Impairment of Investment Securities**

We review investments quarterly for indicators of other-than-temporary impairment. This determination requires significant judgment. In making this judgment, we employ a systematic methodology quarterly 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. If market, industry, and/or investee conditions deteriorate, we may incur future impairments.

### **Goodwill**

We allocate goodwill to reporting units based on the reporting unit expected to benefit from the business combination. We evaluate our reporting units on an annual basis and, if necessary, reassign goodwill using a relative fair value allocation approach. 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. These events or circumstances could include a significant change in the business climate, legal factors, operating performance indicators, competition, or sale or disposition of a significant portion of a reporting unit.

Application of the goodwill impairment test requires judgment, including the identification of reporting units, assignment of assets and liabilities to reporting units, assignment of goodwill to reporting units, and determination of the fair value of each reporting unit. The fair value of each reporting unit is estimated primarily through the use of a discounted cash flow methodology. This analysis requires significant judgments, including estimation of future cash flows, which is dependent on internal forecasts, estimation of the long-term rate of growth for our business, estimation of the useful life over which cash flows will occur, and determination of our weighted average cost of capital.

The estimates used to calculate the fair value of a reporting unit change from year to year based on operating results, market conditions, and other factors. Changes in these estimates and assumptions could materially affect the determination of fair value and goodwill impairment for each reporting unit.

### **Research and Development Costs**

Costs incurred internally in researching and developing a computer software product are charged to expense until technological feasibility has been established for the product. Once technological feasibility is established, all software costs are capitalized until the product is available for general release to customers. Judgment is required in determining when technological feasibility of a product is established. We have determined that technological feasibility for our software products is reached after all high-risk development issues have been resolved through coding and testing. Generally, this occurs shortly before the products are released to manufacturing. The amortization of these costs is included in cost of revenue over the estimated life of the products.

### **Legal and Other Contingencies**

The outcomes of legal proceedings and claims brought against us are subject to significant uncertainty. An estimated loss from a loss contingency such as a legal proceeding or claim is accrued by a charge to income if it is probable that an asset has been impaired or a liability has been incurred and the amount of the loss can be reasonably estimated. In determining whether a loss should be accrued we evaluate, among other factors, the degree of probability of an unfavorable outcome and the ability to make a reasonable estimate of the amount of loss. Changes in these factors could materially impact our consolidated financial statements.

### **Income Taxes**

The objectives of accounting for income taxes are to recognize the amount of taxes payable or refundable for the current year and deferred tax liabilities and assets for the future tax consequences of events that have been recognized in an entity's financial statements or tax returns. We recognize the tax benefit from an uncertain tax position only if it is more likely than not that the tax position will be sustained on examination by the taxing authorities, based on the technical merits of the position. The tax benefits recognized in the financial statements from such a position are measured based on the largest benefit that has a greater than 50% likelihood of being realized upon ultimate settlement. Accounting literature also provides guidance on derecognition of income tax assets and liabilities, classification of deferred income tax assets and liabilities, accounting for interest and penalties associated with tax positions, and income tax disclosures. Judgment is required in assessing the future tax consequences of events that have been recognized on our consolidated financial statements or tax returns. Variations in the actual outcome of these future tax consequences could materially impact our consolidated financial statements.

### **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. These reviews include analysis of demand forecasts, product life cycle status, product development plans, current sales levels, pricing strategy, and component cost trends. 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.

## ITEM 3. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

### RISKS

We are exposed to economic risk from foreign exchange rates, interest rates, credit risk, equity prices, and commodity prices. A portion of these risks is hedged, but they may impact our consolidated financial statements.

#### **Foreign Currency**

Certain forecasted transactions, assets, and liabilities are exposed to foreign currency risk. We monitor our foreign currency exposures daily and use hedges where practicable to offset the risks and maximize the economic effectiveness of our foreign currency positions. Principal currencies hedged include the euro, Japanese yen, British pound, Canadian dollar, and Australian dollar.

#### **Interest Rate**

Our fixed-income portfolio is diversified across credit sectors and maturities, consisting primarily of investment-grade securities. The credit risk and average maturity of the fixed-income portfolio is managed to achieve economic returns that correlate to certain global and domestic fixed-income indices. In addition, we use "To Be Announced" forward purchase commitments of mortgage-backed assets to gain exposure to agency mortgage-backed securities.

#### **Equity**

Our equity portfolio consists of global, developed, and emerging market securities that are subject to market price risk. We manage the securities relative to certain global and domestic indices and expect their economic risk and return to correlate with these indices.

#### **Commodity**

We use broad-based commodity exposures to enhance portfolio returns and facilitate portfolio diversification. Our investment portfolio has exposure to a variety of commodities, including precious metals, energy, and grain. We manage these exposures relative to global commodity indices and expect their economic risk and return to correlate with these indices.

### VALUE-AT-RISK

We use a value-at-risk ("VaR") model to estimate and quantify our market risks. VaR is the expected loss, for a given confidence level, in the fair value of our portfolio due to adverse market movements over a defined time horizon. The VaR model is not intended to represent actual losses in fair value, including determinations of other-than-temporary losses in fair value in accordance with U.S. GAAP, but is used as a risk estimation and management tool. The distribution of the potential changes in total market value of all holdings is computed based on the historical volatilities and correlations among foreign exchange rates, interest rates, equity prices, and commodity prices, assuming normal market conditions.

The VaR is calculated as the total loss that will not be exceeded at the 97.5 percentile confidence level or, alternatively stated, the losses could exceed the VaR in 25 out of 1,000 cases. Several risk factors are not captured in the model, including liquidity risk, operational risk, and legal risk.

The following table sets forth the one-day VaR for substantially all of our positions as of September 30, 2016 and June 30, 2016 and for the three months ended September 30, 2016:

(In millions)

Risk Categories	September 30, 2016	June 30, 2016	Three Months Ended September 30, 2016		
			Average	High	Low
Foreign currency	\$ 230	\$ 92	\$ 183	\$ 303	\$ 88
Interest rate	\$ 84	\$ 58	\$ 70	\$ 84	\$ 57
Equity	\$ 152	\$ 157	\$ 160	\$ 165	\$ 151
Commodity	\$ 11	\$ 12	\$ 11	\$ 12	\$ 9

Total one-day VaR for the combined risk categories was \$325 million as of September 30, 2016 and \$225 million as of June 30, 2016. The total VaR is 32% and 29% less as of September 30, 2016 and June 30, 2016, respectively, than the sum of the separate risk categories in the table above due to the diversification benefit of the combination of risks.

#### ITEM 4. CONTROLS AND PROCEDURES

Under the supervision and with the participation of our management, including the Chief Executive Officer and Chief Financial Officer, we have evaluated the effectiveness of our disclosure controls and procedures as required by Exchange Act Rule 13a-15(b) as of the end of the period covered by this report. Based on that evaluation, the Chief Executive Officer and Chief Financial Officer have concluded that these disclosure controls and procedures are effective. There were no changes in our internal control over financial reporting during the quarter ended September 30, 2016 that have materially affected, or are reasonably likely to materially affect, our internal control over financial reporting.

## PART II. OTHER INFORMATION

### ITEM 1. LEGAL PROCEEDINGS

See Note 14 – Commitments and Contingencies of the Notes to Financial Statements (Part I, Item 1 of this Form 10-Q) for information regarding legal proceedings in which we are involved.

### ITEM 1A. RISK FACTORS

Our operations and financial results are subject to various risks and uncertainties, including those described below, that could adversely affect our business, financial condition, results of operations, cash flows, and the trading price of our common stock.

**We face intense competition across all markets for our products and services, which may lead to lower revenue or operating margins.**

#### *Competition in the technology sector*

Our competitors range in size from diversified global companies with significant research and development resources to small, specialized firms whose narrower product lines may let them be more effective in deploying technical, marketing, and financial resources. Barriers to entry in many of our businesses are low and many of the areas in which we compete evolve rapidly with changing and disruptive technologies, shifting user needs, and frequent introductions of new products and services. Our ability to remain competitive depends on our success in making innovative products, devices, and services that appeal to businesses and consumers.

#### *Competition among platforms, ecosystems, and devices*

An important element of our business model has been to create platform-based ecosystems on which many participants can build diverse solutions. A well-established ecosystem creates beneficial network effects among users, application developers, and the platform provider that can accelerate growth. Establishing significant scale in the marketplace is necessary to achieve and maintain attractive margins. We face significant competition from firms that provide competing platforms, applications, and services.

- A competing vertically-integrated model, in which a single firm controls the software and hardware elements of a product and related services, has succeeded with some consumer products such as personal computers, tablets, phones, gaming consoles, and wearables. Competitors pursuing this model also earn revenue from services integrated with the hardware and software platform. We also offer some vertically-integrated hardware and software products and services. To the extent we shift a portion of our business to a vertically integrated model we increase our cost of revenue and reduce our operating margins.
- We derive substantial revenue from licenses of Windows operating systems on personal computers. We face significant competition from competing platforms developed for new devices and form factors such as smartphones and tablet computers. These devices compete on multiple bases including price and the perceived utility of the device and its platform. Users are increasingly turning to these devices to perform functions that in the past were performed by personal computers. Even if many users view these devices as complementary to a personal computer, the prevalence of these devices may make it more difficult to attract application developers to our PC operating system platforms. Competing with operating systems licensed at low or no cost may decrease our PC operating system margins. In addition, some of our devices compete with products made by our OEM partners, which may affect their commitment to our platform.
- Competing platforms have content and application marketplaces (sometimes referred to as “stores”) with scale and significant installed bases. The variety and utility of content and applications available on a platform are important to device purchasing decisions. Users sometimes incur costs to move data and buy new content and applications when switching platforms. To compete, we must successfully enlist developers to write applications for our marketplace and ensure that these applications have high quality, customer appeal, and value. Efforts to compete with competitors’ content and application marketplaces may increase our cost of revenue and lower our operating margins.

*Business model competition*

Companies compete with us based on a growing variety of business models.

- Even as we transition to a mobile-first and cloud-first strategy, the license-based proprietary software model generates most of our software revenue. We bear the costs of converting original ideas into software products through investments in research and development, offsetting these costs with the revenue received from licensing our products. Many of our competitors also develop and sell software to businesses and consumers under this model.
- Other competitors develop and offer free applications, online services and content, and make money by selling third-party advertising. Advertising revenue funds development of products and services these competitors provide to users at no or little cost, competing directly with our revenue-generating products.
- Some companies compete with us using an open source business model by modifying and then distributing open source software at nominal cost to end-users, and earning revenue on advertising or complementary services and products. These firms do not bear the full costs of research and development for the software. Some open source software vendors develop software that mimics the features and functionality of our products.

The competitive pressures described above may cause decreased sales volumes, price reductions, and/or increased operating costs, such as for research and development, marketing, and sales incentives. This may lead to lower revenue, gross margins, and operating income.

**Our increasing focus on services presents execution and competitive risks.** A growing part of our business involves cloud-based services available across the spectrum of computing devices. Our strategic vision is to compete and grow as a productivity and platform company for the mobile-first and cloud-first world. At the same time, our competitors are rapidly developing and deploying cloud-based services for consumers and business customers. Pricing and delivery models are evolving. Devices and form factors influence how users access services in the cloud and sometimes the user's choice of which suite of cloud-based services to use. We are devoting significant resources to develop and deploy our cloud-based strategies. The Windows ecosystem must continue to evolve with this changing environment. We are undertaking cultural and organizational changes to drive accountability and eliminate obstacles to innovation. The Company's investment in gaining insights from data is becoming central to the value of the services we deliver to customers, to our operational efficiency and key opportunities in monetization, customer perceptions of quality, and operational efficiency. Besides software development costs, we are incurring costs to build and maintain infrastructure to support cloud computing services. These costs will reduce the operating margins we have previously achieved. Whether we succeed in cloud-based services depends on our execution in several areas, including:

- Continuing to bring to market compelling cloud-based experiences that generate increasing traffic and market share.
- Maintaining the utility, compatibility, and performance of our cloud-based services on the growing array of computing devices, including PCs, smartphones, tablets, gaming consoles, and other television-related devices.
- Continuing to enhance the attractiveness of our cloud platforms to third-party developers.
- Ensuring our cloud-based services meet the reliability expectations of our customers and maintain the security of their data.
- Making our suite of cloud-based services platform-agnostic, available on a wide range of devices and ecosystems, including those of our competitors.

It is uncertain whether our strategies will attract the users or generate the revenue required to succeed. If we are not effective in executing organizational and technical changes to increase efficiency and accelerate innovation, or if we fail to generate sufficient usage of our new products and services, we may not grow revenue in line with the infrastructure and development investments described above. This may negatively impact gross margins and operating income.

**We make significant investments in new products and services that may not achieve expected returns.** We will continue to make significant investments in research, development, and marketing for existing products, services, and technologies, including the Windows operating system, the Microsoft Office system, Bing, Windows Phone, Windows Server, the Windows Store, the Microsoft Azure Services platform, Office 365, other cloud-based offerings,

and the Xbox entertainment platform. We also invest in the development and acquisition of a variety of hardware for productivity, communication, and entertainment including PCs, tablets, phones, and gaming devices. Investments in new technology are speculative. Commercial success depends on many factors, including innovativeness, developer support, and effective distribution and marketing. If customers do not perceive our latest offerings as providing significant new functionality or other value, they may reduce their purchases of new software and hardware products or upgrades, unfavorably affecting revenue. We may not achieve significant revenue from new product, service, and distribution channel investments for several years, if at all. New products and services may not be profitable, and even if they are profitable, operating margins for some new products and businesses will not be as high as the margins we have experienced historically.

The launch of Windows 10, with free upgrades to existing users of Windows 7 and 8.1, has been the most ambitious update effort we have ever undertaken. We did extensive preparation and ongoing compatibility testing for applications and devices to help ensure a positive experience for our users installing Windows 10. We also consistently promoted the update to Windows 7 and 8.1 users. However, negative upgrade experiences could adversely affect the reception of Windows 10 in the marketplace and may lead to litigation or regulatory actions by customers and government agencies. In addition, we anticipate that Windows 10 will enable new post-license monetization opportunities beyond initial license revenues. Our inability to realize these opportunities to the extent we expect could have an adverse impact on our revenues. Finally, our practices around data collection, use, and management in Windows 10 are subject to regulatory review, and may result in decisions directing us to change these practices and imposing fines. If so, we could face negative public reaction, degraded user experiences, and reduced flexibility in product design.

Developing new technologies is complex. It can require long development and testing periods. Significant delays in new releases or significant problems in creating new products or services could adversely affect our revenue.

**Acquisitions, joint ventures, and strategic alliances may have an adverse effect on our business.** We expect to continue making acquisitions and entering into joint ventures and strategic alliances as part of our long-term business strategy. In June 2016, we announced our acquisition of LinkedIn for approximately \$26.2 billion. The LinkedIn acquisition and other transactions and arrangements involve significant challenges and risks, including that they do not advance our business strategy, that we get an unsatisfactory return on our investment, that we have difficulty integrating new employees, business systems, and technology, or that they distract management from our other businesses. If an arrangement fails to adequately anticipate changing circumstances and interests of a party, it may result in early termination or renegotiation of the arrangement. The success of these transactions and arrangements will depend in part on our ability to leverage them to enhance our existing products and services or develop compelling new ones. It may take longer than expected to realize the full benefits from these transactions and arrangements, such as increased revenue, enhanced efficiencies, or increased market share, or the benefits may ultimately be smaller than we expected. These events could adversely affect our operating results or financial condition.

**If our goodwill or amortizable intangible assets become impaired, we may be required to record a significant charge to earnings.** We acquire other companies and intangible assets and may not realize all the economic benefit from those acquisitions, which could cause an impairment of goodwill or intangibles. We review our amortizable intangible assets for impairment when events or changes in circumstances indicate the carrying value may not be recoverable. We test goodwill for impairment at least annually. Factors that may be a change in circumstances, indicating that the carrying value of our goodwill or amortizable intangible assets may not be recoverable, include a decline in our stock price and market capitalization, reduced future cash flow estimates, and slower growth rates in industry segments in which we participate. We may be required to record a significant charge on our consolidated financial statements during the period in which any impairment of our goodwill or amortizable intangible assets is determined, negatively affecting our results of operations. For example, in the fourth quarter of fiscal year 2015, we recorded a \$5.1 billion charge for the impairment of goodwill and a \$2.2 billion charge for the impairment of intangible assets, and in the fourth quarter of fiscal year 2016 we recorded a \$480 million charge for the impairment of intangible assets. The impairment charges for both periods related to our phone business. Our acquisition of LinkedIn will result in a significant increase in our goodwill and intangible asset balances.

**We may not earn the revenues we expect from our intellectual property rights.**

*We may not be able to adequately protect our intellectual property rights*

Protecting our intellectual property rights and combating unlicensed copying and use of our software and other intellectual property on a global basis is difficult. While piracy adversely affects U.S. revenue, the impact on revenue



from outside the U.S. is more significant, particularly in countries where laws are less protective of intellectual property rights. Our revenue in these markets may grow slower than the underlying device market. Similarly, the absence of harmonized patent laws makes it more difficult to ensure consistent respect for patent rights. Throughout the world, we educate users about the benefits of licensing genuine products and obtaining indemnification benefits for intellectual property risks, and we educate lawmakers about the advantages of a business climate where intellectual property rights are protected. Reductions in the legal protection for software intellectual property rights could adversely affect revenue.

*We may not receive expected royalties from our patent licenses*

We expend significant resources to patent the intellectual property we create with the expectation that we will generate revenues by incorporating that intellectual property in our products or services or, in some instances, by licensing our patents to others in return for a royalty. Changes in the law may weaken our ability to prevent the use of patented technology or collect revenue for licensing our patents. These include legislative changes and regulatory actions that make it more difficult to obtain injunctions, and the increasing use of legal process to challenge issued patents. Similarly, licensees of our patents may fail to satisfy their obligations to pay us royalties, or may contest the scope and extent of their obligations. Finally, the royalties we can obtain to monetize our intellectual property may decline because of the evolution of technology, selling price changes in products using licensed patents, or the difficulty of discovering infringements.

**Third parties may claim we infringe their intellectual property rights.** From time to time, others claim we infringe their intellectual property rights. The number of these claims may grow because of constant technological change in the markets in which we compete, the extensive patent coverage of existing technologies, the rapid rate of issuance of new patents, and our offering of first-party devices, such as Surface and Lumia phones. To resolve these claims, we may enter into royalty and licensing agreements on terms that are less favorable than currently available, stop selling or redesign affected products or services, or pay damages to satisfy indemnification commitments with our customers. These outcomes may cause operating margins to decline. Besides money damages, in some jurisdictions plaintiffs can seek injunctive relief that may limit or prevent importing, marketing, and selling our products or services that have infringing technologies. In some countries, such as Germany, an injunction can be issued before the parties have fully litigated the validity of the underlying patents. We have paid significant amounts to settle claims related to the use of technology and intellectual property rights and to procure intellectual property rights as part of our strategy to manage this risk, and may continue to do so.

**We may not be able to protect our source code from copying if there is an unauthorized disclosure of source code.** Source code, the detailed program commands for our operating systems and other software programs, is critical to our business. Although we license portions of our application and operating system source code to several licensees, we take significant measures to protect the secrecy of large portions of our source code. If a significant portion of our source code leaks, we might lose future trade secret protection for that source code. It may become easier for third parties to compete with our products by copying functionality, which could adversely affect our revenue and operating margins. Unauthorized disclosure of source code also could increase the security risks described in the next paragraph.

**Cyber-attacks and security vulnerabilities could lead to reduced revenue, increased costs, liability claims, or harm to our competitive position.**

*Security of Microsoft's information technology*

Threats to IT security can take a variety of forms. Individual and groups of hackers, and sophisticated organizations including state-sponsored organizations or nation-states themselves, may take steps that pose threats to our customers and our IT. These actors may use a wide variety of methods, which may include developing and deploying malicious software to attack our products and services and gain access to our networks and datacenters, using social engineering techniques, or acting in a coordinated manner to launch distributed denial of service or other coordinated attacks. Cyber threats are constantly evolving, thereby increasing the difficulty of detecting and successfully defending against them. Cyber threats can have cascading impacts that unfold with increasing speed across our internal networks and systems and those of our partners and customers. Breaches of our network or data security could disrupt the security of our internal systems and business applications, impair our ability to provide services to our customers and protect the privacy of their data, result in product development delays, compromise confidential or technical business information harming our competitive position, result in theft or misuse of our intellectual property or other assets, require us to allocate more resources to improved technologies, or otherwise adversely affect our business.

In addition, our internal IT environment continues to evolve. Often, we are early adopters of new devices and technologies. We embrace new ways of sharing data and communicating internally and with partners and customers using methods such as social networking and other consumer-oriented technologies. Our business policies and internal security controls may not keep pace with these changes as new threats emerge.

*Security of our products, services, devices, and customers' data*

Security threats are a particular challenge to companies like us whose business is technology products and services. Threats to our own IT infrastructure can also affect our customers. Customers using our cloud-based services rely on the security of our infrastructure to ensure the reliability of our services and the protection of their data. Hackers tend to focus their efforts on the most popular operating systems, programs, and services, including many of ours, and we expect that to continue. The security of our products and services is important in our customers' purchasing decisions.

To defend against security threats, both to our internal IT systems and those of our customers, we must continuously engineer more secure products and services, enhance security and reliability features, improve the deployment of software updates to address security vulnerabilities, develop mitigation technologies that help to secure customers from attacks even when software updates are not deployed, maintain the digital security infrastructure that protects the integrity of our network, products, and services, and provide customers security tools such as firewalls and anti-virus software.

The cost of these steps could reduce our operating margins. If we fail to do these things well, actual or perceived security vulnerabilities in our products and services could harm our reputation and lead customers to reduce or delay future purchases of products or subscriptions to services, or to use competing products or services. Customers may also spend more on protecting their existing computer systems from attack, which could delay adoption of additional products or services. Customers may fail to update their systems, continue to run software or operating systems we no longer support, or may fail timely to install security patches. Any of these actions by customers could adversely affect our revenue. Actual or perceived vulnerabilities may lead to claims against us. Although our license agreements typically contain provisions that eliminate or limit our exposure to liability, there is no assurance these provisions will withstand legal challenges. Legislative or regulatory action in these areas may increase the costs to develop, implement, or secure our products and services.

**Disclosure of personal data could result in liability and harm our reputation.** As we continue to grow the number and scale of our cloud-based offerings, we store and process increasingly large amounts of personally identifiable information of our customers. The continued occurrence of high-profile data breaches provides evidence of an external environment increasingly hostile to information security. Despite our efforts to improve the security controls across our business groups and geographies, it is possible our security controls over personal data, our training of employees and vendors on data security, and other practices we follow may not prevent the improper disclosure of customer data we or our vendors store and manage. Improper disclosure could harm our reputation, lead to legal exposure to customers, or subject us to liability under laws that protect personal data, resulting in increased costs or loss of revenue. Our software products and services also enable our customers to store and process personal data on-premises or, increasingly, in a cloud-based environment we host. Government authorities can sometimes require us to produce customer data in response to valid legal orders. In the U.S. and elsewhere, we advocate for transparency concerning these requests and appropriate limitations on government authority to compel disclosure. Despite our efforts to protect customer data, perceptions that the collection, use and retention of personal information is not satisfactorily protected could inhibit sales of our products or services, and could limit adoption of our cloud-based solutions by consumers, businesses, and government entities. Additional security measures we may take to address customer concerns, or constraints on our flexibility to determine where and how to operate datacenters in response to customer expectations or governmental rules or actions, may cause higher operating expenses.

**We may have outages, data losses, and disruptions of our online services if we fail to maintain an adequate operations infrastructure.** Our increasing user traffic, growth in services, and the complexity of our products and services demand more computing power. We spend substantial amounts to build, purchase, or lease datacenters and equipment and to upgrade our technology and network infrastructure to handle more traffic on our websites and in our datacenters. These demands continue to increase as we introduce new products and services and support the growth of existing services such as Bing, Exchange Online, Microsoft Azure, Microsoft Account services, Office 365, OneDrive, SharePoint Online, Skype, Xbox Live, Outlook.com, and Windows Stores. We are rapidly growing our business of providing a platform and back-end hosting for services provided by third parties to their end users. Maintaining, securing, and expanding this infrastructure is expensive and complex. It requires that we maintain an

Internet connectivity infrastructure that is robust and reliable within competitive and regulatory constraints that continue to evolve. Inefficiencies or operational failures, including temporary or permanent loss of customer data or insufficient Internet connectivity, could diminish the quality of our products, services, and user experience resulting in contractual liability, claims by customers and other third parties, regulatory actions, damage to our reputation, and loss of current and potential users, subscribers, and advertisers, each of which may harm our operating results and financial condition.

**Government litigation and regulatory activity relating to competition rules may limit how we design and market our products.** As a leading global software and device maker, we are closely scrutinized by government agencies under U.S. and foreign competition laws. An increasing number of governments are regulating competition law activities and this includes increased scrutiny in potentially large markets such as the European Union (“EU”), the U.S., and China. Some jurisdictions also allow competitors or consumers to assert claims of anti-competitive conduct. U.S. federal and state antitrust authorities have previously brought enforcement actions and continue to scrutinize our business.

The European Commission (“the Commission”) closely scrutinizes the design of high-volume Microsoft products and the terms on which we make certain technologies used in these products, such as file formats, programming interfaces, and protocols, available to other companies. Flagship product releases such as Windows 10 can receive significant scrutiny under competition laws. For example, in 2004, the Commission ordered us to create new versions of our Windows operating system that do not include certain multimedia technologies and to provide our competitors with specifications for how to implement certain proprietary Windows communications protocols in their own products. In 2009, the Commission accepted a set of commitments offered by Microsoft to address the Commission’s concerns relating to competition in web browsing software, including an undertaking to address Commission concerns relating to interoperability. The web browsing commitments expired in 2014. The remaining obligations may limit our ability to innovate in Windows or other products in the future, diminish the developer appeal of the Windows platform, and increase our product development costs. The availability of licenses related to protocols and file formats may enable competitors to develop software products that better mimic the functionality of our products, which could hamper sales of our products.

Our portfolio of first-party devices continues to grow; at the same time our OEM partners offer a large variety of devices on our platforms. As a result, increasingly we both cooperate and compete with our OEM partners, creating a risk that we fail to do so in compliance with competition rules. Regulatory scrutiny in this area may increase. Certain foreign governments, particularly in China and other countries in Asia, have advanced arguments under their competition laws that exert downward pressure on royalties for our intellectual property. Because these jurisdictions only recently implemented competition laws, their enforcement activities are unpredictable.

Government regulatory actions and court decisions such as these may hinder our ability to provide the benefits of our software to consumers and businesses, reducing the attractiveness of our products and the revenue that come from them. New competition law actions could be initiated. The outcome of such actions, or steps taken to avoid them, could adversely affect us in a variety of ways, including:

- We may have to choose between withdrawing products from certain geographies to avoid fines or designing and developing alternative versions of those products to comply with government rulings, which may entail a delay in a product release and removing functionality that customers want or on which developers rely.
- We may be required to make available licenses to our proprietary technologies on terms that do not reflect their fair market value or do not protect our associated intellectual property.
- The rulings described above may be precedent in other competition law proceedings.
- We are subject to a variety of ongoing commitments because of court or administrative orders, consent decrees, or other voluntary actions we have taken. If we fail to comply with these commitments, we may incur litigation costs and be subject to substantial fines or other remedial actions.
- Our ability to realize anticipated Windows 10 post-sale monetization opportunities may be limited.

**Our global operations subject us to potential liability under anti-corruption, trade protection, and other laws and regulations.** The Foreign Corrupt Practices Act and other anti-corruption laws and regulations (“Anti-Corruption Laws”) prohibit corrupt payments by our employees, vendors, or agents. From time to time, we receive inquiries from authorities in the U.S. and elsewhere and reports from employees and others about our business activities outside the U.S. and our compliance with Anti-Corruption Laws. Specifically, we have been cooperating with authorities in the U.S. in connection with reports concerning our compliance with the Foreign Corrupt Practices Act in various countries. While we devote substantial resources to our global compliance programs and have implemented policies,

training, and internal controls designed to reduce the risk of corrupt payments, our employees, vendors, or agents may violate our policies. Our failure to comply with Anti-Corruption Laws could result in significant fines and penalties, criminal sanctions against us, our officers, or our employees, prohibitions on the conduct of our business, and damage to our reputation. Geopolitical instability may lead to sanctions and impact our ability to do business in some geographies. Operations outside the U.S. may be affected by changes in trade protection laws, policies, and measures, sanctions, and other regulatory requirements affecting trade and investment. We may be subject to legal liability and reputational damage if we sell goods or services in violation of U.S. trade sanctions on countries such as Iran, North Korea, Cuba, Sudan, and Syria.

Other regulatory areas that may apply to our products and online services offerings include user privacy, telecommunications, data storage and protection, and online content. For example, regulators may take the position that our offerings such as Skype are covered by laws regulating telecommunications services. Data protection authorities may assert that our collection, use, and management of customer data is inconsistent with their laws and regulations. Applying these laws and regulations to our business is often unclear, subject to change over time, and sometimes may conflict from jurisdiction to jurisdiction. Additionally, these laws and governments' approach to their enforcement, and our products and services, are continuing to evolve. Compliance with these types of regulation may involve significant costs or require changes in products or business practices that result in reduced revenue. Noncompliance could result in the imposition of penalties or orders we stop the alleged noncompliant activity.

**Laws and regulations relating to the handling of personal data may impede the adoption of our services or result in increased costs, legal claims, or fines against us.** The growth of our internet- and cloud-based services internationally relies increasingly on the movement of data across national boundaries. Legal requirements relating to the collection, storage, handling, and transfer of personal data continue to evolve. For example, the EU and the U.S. formally entered into a new framework in July 2016 that provides a mechanism for companies to transfer data from EU member states to the U.S. This new framework, called the Privacy Shield, is intended to address shortcomings identified by the European Court of Justice in a predecessor mechanism. The Privacy Shield and other mechanisms are likely to be reviewed by the European courts, which may lead to uncertainty about the legal basis for data transfers across the Atlantic. Ongoing legal reviews may result in burdensome or inconsistent requirements affecting the location and movement of our customer and internal employee data as well as the management of that data. Compliance may require changes in services, business practices, or internal systems that result in increased costs, lower revenue, reduced efficiency, or greater difficulty in competing with foreign-based firms. Failure to comply with existing or new rules may result in significant penalties or orders to stop the alleged noncompliant activity.

**Our business depends on our ability to attract and retain talented employees.** Our business is based on successfully attracting and retaining talented employees. The market for highly skilled workers and leaders in our industry is extremely competitive. We are limited in our ability to recruit internationally by restrictive domestic immigration laws. If we are less successful in our recruiting efforts, or if we cannot retain key employees, our ability to develop and deliver successful products and services may be adversely affected. Effective succession planning is also important to our long-term success. Failure to ensure effective transfer of knowledge and smooth transitions involving key employees could hinder our strategic planning and execution. How employment-related laws are interpreted and applied to our workforce practices may result in increased operating costs and less flexibility in how we meet our workforce needs.

**We have claims and lawsuits against us that may result in adverse outcomes.** We are subject to a variety of claims and lawsuits. These claims may arise from a wide variety of business practices and initiatives, including major new product releases such as Windows 10, significant business transactions, warranty or product claims, and employment practices. Adverse outcomes in some or all of these claims may result in significant monetary damages or injunctive relief that could adversely affect our ability to conduct our business. The litigation and other claims are subject to inherent uncertainties and management's view of these matters may change in the future. A material adverse impact on our consolidated financial statements could occur for the period in which the effect of an unfavorable final outcome becomes probable and reasonably estimable.

**We may have additional tax liabilities.** We are subject to income taxes in the U.S. and many foreign jurisdictions. Significant judgment is required in determining our worldwide provision for income taxes. In the ordinary course of our business, there are many transactions and calculations where the ultimate tax determination is uncertain. We regularly are under audit by tax authorities in different jurisdictions. Economic and political pressures to increase tax revenue in various jurisdictions may make resolving tax disputes favorably more difficult. Although we believe our tax estimates are reasonable, the final determination of tax audits and any related litigation in the jurisdictions where we are subject to taxation could be materially different from our historical income tax provisions and accruals. The results of an audit or litigation could have a material effect on our consolidated financial statements in the period or periods in which that determination is made.

We earn a significant amount of our operating income from outside the U.S., and any repatriation of funds currently held in foreign jurisdictions to the U.S. may result in higher effective tax rates for the company. In addition, there have been proposals from Congress to change U.S. tax laws that would significantly impact how U.S. multinational corporations are taxed on foreign earnings. Although we cannot predict whether or in what form any proposed legislation may pass, if enacted, it could have a material adverse impact on our tax expense and cash flows.

**Our hardware and software products may experience quality or supply problems.** Our vertically-integrated hardware products such as Xbox consoles, Surface devices, phones, and other devices we design, manufacture, and market are highly complex and can have defects in design, manufacture, or associated software. We could incur significant expenses, lost revenue, and reputational harm as a result of recalls, safety alerts, or product liability claims if we fail to prevent, detect, or address such issues through design, testing, or warranty repairs. We acquire some device components from sole suppliers. Our competitors use some of the same suppliers and their demand for hardware components can affect the capacity available to us. If a component from a sole-source supplier is delayed or becomes unavailable, whether because of supplier capacity constraint or industry shortages, we may not obtain timely replacement supplies, resulting in reduced sales. Component shortages, excess or obsolete inventory, or price reductions resulting in inventory adjustments may increase our cost of revenue. Xbox consoles, Surface devices, phones, and other hardware are assembled in Asia and other geographies that may be subject to disruptions in the supply chain, resulting in shortages that would affect our revenue and operating margins. These same risks would apply to any other vertically-integrated hardware and software products we may offer.

Our software products also may experience quality or reliability problems. The highly sophisticated software products we develop may contain bugs and other defects that interfere with their intended operation. Any defects we do not detect and fix in pre-release testing could cause reduced sales and revenue, damage to our reputation, repair or remediation costs, delays in the release of new products or versions, or legal liability. Although our license agreements typically contain provisions that eliminate or limit our exposure to liability, there is no assurance these provisions will withstand legal challenge.

We strive to empower all people and organizations to achieve more, and accessibility of our products is an important aspect of this goal. There is increasing pressure from advocacy groups, regulators, competitors, and customers to make technology more accessible. If our products do not meet customer expectations or emerging global accessibility requirements, we could lose sales opportunities or face regulatory actions.

**Our global business exposes us to operational and economic risks.** Our customers are located in over 200 countries and a significant part of our revenue comes from international sales. The global nature of our business creates operational and economic risks. Emerging markets are a significant focus of our international growth strategy. The developing nature of these markets presents several risks, including deterioration of social, political, labor, or economic conditions in a country or region, and difficulties in staffing and managing foreign operations. Although we hedge a portion of our international currency exposure, significant fluctuations in foreign exchange rates between the U.S. dollar and foreign currencies may adversely affect our revenue. Competitive or regulatory pressure to make our pricing structure uniform might require that we reduce the sales price of our software in the U.S. and other countries.

**Catastrophic events or geopolitical conditions may disrupt our business.** A disruption or failure of our systems or operations because of a major earthquake, weather event, cyber-attack, terrorist attack, or other catastrophic event could cause delays in completing sales, providing services, or performing other critical functions. Our corporate headquarters, a significant portion of our research and development activities, and certain other essential business operations are in the Seattle, Washington area, and we have other business operations in the Silicon Valley area of California, both of which are seismically active regions. A catastrophic event that results in the destruction or disruption of any of our critical business or IT systems could harm our ability to conduct normal business operations. Providing our customers with more services and solutions in the cloud puts a premium on the resilience of our systems and strength of our business continuity management plans, and magnifies the potential impact of prolonged service outages on our operating results.

Abrupt political change, terrorist activity, and armed conflict pose a risk of general economic disruption in affected countries, which may increase our operating costs. These conditions also may add uncertainty to the timing and budget for technology investment decisions by our customers, and may cause supply chain disruptions for hardware manufacturers, either of which may adversely affect our revenue. The long-term effects of climate change on the global economy or the IT industry in particular are unclear. Environmental regulations or changes in the supply,

demand or available sources of energy or other natural resources may affect the availability or cost of goods and services, including natural resources, necessary to run our business. Changes in weather where we operate may increase the costs of powering and cooling computer hardware we use to develop software and provide cloud-based services.

**Adverse economic or market conditions may harm our business.** Worsening economic conditions, including inflation, recession, or other changes in economic conditions, may cause lower IT spending and adversely affect our revenue. If demand for PCs, servers, and other computing devices declines, or consumer or business spending for those products declines, our revenue will be adversely affected. Substantial revenue comes from our U.S. government contracts. An extended federal government shutdown resulting from failing to pass budget appropriations, adopt continuing funding resolutions or raise the debt ceiling, and other budgetary decisions limiting or delaying federal government spending, could reduce government IT spending on our products and services and adversely affect our revenue.

Our product distribution system relies on an extensive partner and retail network. OEMs building devices that run our software have also been a significant means of distribution. The impact of economic conditions on our partners, such as the bankruptcy of a major distributor, OEM, or retailer, could cause sales channel disruption.

Challenging economic conditions also may impair the ability of our customers to pay for products and services they have purchased. As a result, allowances for doubtful accounts and write-offs of accounts receivable may increase.

We maintain an investment portfolio of various holdings, types, and maturities. These investments are subject to general credit, liquidity, market, and interest rate risks, which may be exacerbated by unusual events that affect global financial markets. A significant part of our investment portfolio comprises U.S. government securities. If global credit and equity markets decline for long periods, or if there is a downgrade of the U.S. government credit rating due to an actual or threatened default on government debt, our investment portfolio may be adversely affected and we could determine that more of our investments have experienced an other-than-temporary decline in fair value, requiring impairment charges that could adversely affect our financial results.

**ITEM 2. UNREGISTERED SALES OF EQUITY SECURITIES AND USE OF PROCEEDS**

Items 2(a) and (b) are not applicable.

**(c) STOCK REPURCHASES**

Period	Total Number of Shares Purchased	Average Price Paid per Share	Total Number of Shares Purchased as Part of Publicly Announced Plans or Programs	Approximate Dollar Value of Shares that May Yet be Purchased under the Plans or Programs
				(in millions)
July 1, 2016 – July 31, 2016	20,206,697	\$ 54.04	20,206,697	\$ 5,991
August 1, 2016 – August 31, 2016	22,667,078	\$ 57.71	22,667,078	\$ 4,683
September 1, 2016 – September 30, 2016	20,076,491	\$ 57.28	20,076,491	\$ 3,533
	62,950,266		62,950,266	

During the three months ended September 30, 2016, we repurchased 63 million shares of our common stock for \$3.6 billion under a \$40.0 billion share repurchase plan approved by our Board of Directors on September 16, 2013. The share repurchase program became effective on October 1, 2013, has no expiration date, and may be suspended or discontinued at any time without notice. While the program has no expiration date, we intend to complete it by December 31, 2016. As of September 30, 2016, \$3.5 billion remained of the \$40.0 billion share repurchase program. All repurchases were made using cash resources.

On September 20, 2016, our Board of Directors approved a share repurchase program authorizing an additional \$40.0 billion in share repurchases. This share repurchase program will commence following completion of the program approved on September 16, 2013, has no expiration, and may be suspended or discontinued at any time without notice.

Our stock repurchases may occur through open market purchases or pursuant to a Rule 10b5-1 trading plan.

Excluded from this disclosure are shares repurchased to settle statutory employee tax withholding related to the vesting of stock awards.

## ITEM 6. EXHIBITS

3.2	Bylaws of Microsoft Corporation (incorporated by reference to Current Report on Form 8-K filed September 22, 2016)
4.14	Eleventh Supplemental Indenture for 1.100% Notes due 2019, 1.550% Notes due 2021, 2.000% Notes due 2023, 2.400% Notes due 2026, 3.450% Notes due 2036, 3.700% Notes due 2046, and 3.950% Notes due 2056, dated as of August 8, 2016, between Microsoft Corporation and U.S. Bank, National Association, as trustee, to the Indenture, dated as of May 18, 2009, between Microsoft Corporation and The Bank of New York Mellon Trust Company, N.A., as trustee (incorporated by reference to Current Report on Form 8-K filed August 5, 2016)
10.1*	Microsoft Corporation 2001 Stock Plan
10.12	Amended and Restated Officers' Indemnification Trust Agreement between Microsoft Corporation and The Bank of New York Mellon Trust Company, as trustee
10.13	Amended and Restated Directors' Indemnification Trust Agreement between Microsoft Corporation and The Bank of New York Mellon Trust Company, as trustee
10.17*	Executive Incentive Plan
10.18*	Form of Executive Incentive Plan Stock Award Agreement under the Microsoft Corporation 2001 Stock Plan
10.22*	Senior Executive Severance Benefit Plan
10.25*	Form of Executive Incentive Plan Performance Stock Award Agreement under the Microsoft Corporation 2001 Stock Plan
15	Letter regarding unaudited interim financial information
31.1	Certifications of Chief Executive Officer Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002
31.2	Certifications of Chief Financial Officer Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002
32.1**	Certification of Chief Executive Officer Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002
32.2**	Certification of Chief Financial Officer Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002
101.INS	XBRL Instance Document
101.SCH	XBRL Taxonomy Extension Schema
101.CAL	XBRL Taxonomy Extension Calculation Linkbase
101.DEF	XBRL Taxonomy Extension Definition Linkbase
101.LAB	XBRL Taxonomy Extension Label Linkbase
101.PRE	XBRL Taxonomy Extension Presentation Linkbase

\* *Indicates a management contract or compensatory plan or arrangement*

\*\* *Furnished, not filed*

**Items 3, 4, and 5 are not applicable and have been omitted.**



**SIGNATURE**

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

MICROSOFT CORPORATION

/s/ FRANK H. BROD

Frank H. Brod  
Corporate Vice President, Finance and Administration;  
Chief Accounting Officer (Duly Authorized Officer)

October 20, 2016

**MICROSOFT CORPORATION  
2001 STOCK PLAN**

**(as amended effective as of July 26, 2016)**

1. Purpose of the Plan. The purposes of this Stock Plan are to attract and retain the best available individuals for positions of substantial responsibility, to provide additional incentive to such individuals, and to promote the success of the Company's business by aligning the financial interests of Employees and Consultants providing personal services to the Company or to any Parent or Subsidiary of the Company with long-term shareholder value.

Awards granted hereunder may be Incentive Stock Options, Nonqualified Stock Options, Stock Awards, or SARs, at the discretion of the Board and as reflected in the terms of the Award Agreement.

2. Definitions. As used herein, the following definitions shall apply:

(a) "Award" shall mean any award or benefits granted under the Plan, including Options, Stock Awards, and SARs.

(b) "Award Agreement" shall mean a written or electronic agreement between the Company and the Awardee setting forth the terms of the Award.

(c) "Awardee" shall mean the holder of an outstanding Award.

(d) "Board" shall mean (i) the Board of Directors of the Company or (ii) both the Board and the Committee, if a Committee has been appointed in accordance with Section 4(a) of the Plan.

(e) "Code" shall mean the Internal Revenue Code of 1986, as amended.

(f) "Committee" shall mean the Compensation Committee appointed by the Board of Directors in accordance with Section 4(a) of the Plan, if one is appointed; provided, however, if the Board of Directors appoints more than one Committee pursuant to Section 4(a), then "Committee" shall refer to the appropriate Committee, as indicated by the context of the reference.

(g) "Common Shares" shall mean the common shares of Microsoft Corporation.

(h) "Company" shall mean Microsoft Corporation, a Washington corporation and any successor thereto.

(i) "Consultant" shall mean any person, except an Employee, engaged by the Company or any Parent or Subsidiary of the Company, to render personal services to such entity, including as an advisor.

(j) "Continuous Status as a Participant" shall mean (1) for Employees, the absence of any interruption or termination of service as an Employee, and (2) for Consultants, the absence of any interruption, expiration, or termination of such person's consulting or advisory relationship with the Company or the occurrence of any termination event as set forth in such person's Award Agreement. Continuous Status as a Participant shall not be considered interrupted (i) for an Employee in the case of sick leave, maternity leave, infant care leave, medical emergency leave, military leave, or any other leave of absence for which Continuous Status is not considered interrupted in accordance with the Company's policies on such matters, and (ii) for a Consultant, in the case of any temporary interruption in such person's availability to provide services to the Company which has been authorized in writing by a Vice President of the Company prior to its commencement.

(k) "Conversion Options" shall mean the Options described in Section 6(c) of the Plan.

(l) "Employee" shall mean any person, including an officer, who is a common law employee of, receives remuneration for personal services to, is reflected on the official human resources database as an employee of, and is on the payroll of the Company or any Parent or Subsidiary of the Company. A person

is on the payroll if he or she is paid from the payroll department of the Company, or any Parent or Subsidiary of the Company. Persons providing services to the Company, or to any Parent or Subsidiary of the Company, pursuant to an agreement with a staff leasing organization, temporary workers engaged through or employed by temporary or leasing agencies, and workers who hold themselves out to the Company, Parent, or Subsidiary to which they are providing services as being independent contractors, or as being employed by or engaged through another company while providing the services are not Employees for purposes of this Plan, whether or not such persons are, or may be reclassified by the courts, the Internal Revenue Service, the U. S. Department of Labor, or other person or entity as, common law employees of the Company, Parent, or Subsidiary, either solely or jointly with another person or entity.

- (m) "Effective Date" shall mean January 1, 2001.
- (n) "Exchange Act" shall mean the Securities Exchange Act of 1934, as amended.
- (o) "Incentive Stock Option" shall mean any Option intended to qualify as an incentive stock option within the meaning of Section 422 of the Code.
- (p) "Maximum Annual Participant Award" shall have the meaning set forth in Section 5(b).
- (q) "Nonqualified Stock Option" shall mean an Option not intended to qualify as an Incentive Stock Option.
- (r) "Option" shall mean a stock option granted pursuant to Section 6 of the Plan.
- (s) "Parent" shall mean a "parent corporation," whether now or hereafter existing, as defined in Section 424(e) of the Code.
- (t) "Participant" shall mean an Employee or Consultant.
- (u) "Plan" shall mean this 2001 Stock Plan, including any amendments thereto.
- (v) "Share" shall mean one Common Share, as adjusted in accordance with Section 14 of the Plan.
- (w) "SAR" shall mean a stock appreciation right awarded pursuant to Section 8 of the Plan.
- (x) "Stock Award" shall mean a grant of Shares or of a right to receive Shares or their cash equivalent (or both) pursuant to Section 7 of the Plan.
- (y) "Subsidiary" shall mean (i) in the case of an Incentive Stock Option a "subsidiary corporation," whether now or hereafter existing, as defined in Section 424(f) of the Code, and (ii) in the case of a Nonqualified Stock Option, a Stock Award or an SAR, with the approval of the Board, Committee or other person authorized to administer the Plan in accordance with Section 4 of the Plan, a limited liability company, partnership or other entity in which the Company controls 50 percent or more of the voting power or equity interests.

3. Shares Subject to the Plan. Subject to the provisions of Sections 14 and 16 of the Plan, the maximum aggregate number of Shares (increased, proportionately, in the event of any stock split, stock dividend or similar event with respect to the Shares) which may be awarded and delivered under the Plan shall not exceed the sum of (a) any Shares available for future awards, as of the Effective Date, under the Microsoft Corporation 1991 Stock Option Plan, as amended ("1991 Stock Plan") and (b) any Shares that are represented by awards under the 1991 Stock Plan which, after the Effective Date, are forfeited, expire, are cancelled without delivery of Shares, or otherwise result in the return of Shares to the Company, minus (c) 100,000,000 Shares (unadjusted for any stock split or stock dividend with respect to the Shares). The Shares may be authorized, but unissued, or reacquired Common Shares.

Subject to the provisions of the following sentence, if an Award should expire or become unexercisable for any reason without having been exercised in full, the undelivered Shares which were subject thereto shall, unless the Plan shall have been terminated, become available for future Awards under the Plan. Notwithstanding anything to the contrary contained herein, any Awards of Options that are transferred to a third party pursuant to a program under which the holder of certain Options may transfer such Options to such third party in exchange for cash or other consideration, shall be removed from the Plan and the Shares subject to such Awards shall not be available for regrant under the Plan regardless of whether the transferred Options are exercised or expire without exercise.

#### 4. Administration of the Plan.

(a) Procedure. The Plan shall be administered by the Board of Directors of the Company.

(i) The Board of Directors may appoint one or more Committees each consisting of not less than two members of the Board of Directors to administer the Plan on behalf of the Board of Directors, subject to such terms and conditions as the Board of Directors may prescribe. Once appointed, such Committees shall continue to serve until otherwise directed by the Board of Directors.

(ii) From time to time the Board of Directors may increase the size of the Committee(s) and appoint additional members thereof, remove members (with or without cause) and appoint new members in substitution therefor, or fill vacancies however caused.

(iii) The Committee(s) appointed to administer the Plan on behalf of the Board of Directors may delegate its authority to administer the Plan to the extent provided in the charter for the Committee(s) or a resolution of the Board.

(b) Powers of the Board. Subject to the provisions of the Plan, the Board shall have the authority, in its discretion: (i) to grant Incentive Stock Options, Nonqualified Stock Options, Stock Awards, and SARs; (ii) to determine, in accordance with Section 11(b) of the Plan, the fair market value of the Shares; (iii) to determine, in accordance with Section 11(a) of the Plan, the exercise price per share of Awards to be granted; (iv) to determine the Participants to whom, and the time or times at which, Awards shall be granted and the number of Shares to be represented by each Award; (v) to interpret the Plan and the terms of Awards; (vi) to prescribe, amend, and rescind rules and regulations relating to the Plan; including the form of Award Agreement, and manner of acceptance of an Award, (vii) to determine the terms and provisions of each Award to be granted (which need not be identical) and, with the consent of the Awardee, modify or amend any Award; (viii) to authorize conversion or substitution under the Plan of any or all Conversion Options; (ix) to accelerate or defer (with the consent of the Awardee) the vesting or exercise date of any Award; (x) to authorize any person to execute on behalf of the Company any instrument required to effectuate the grant of an Award previously granted by the Board; and (xi) to make all other determinations deemed necessary or advisable for the administration of the Plan; *provided that*, no consent of an Awardee is necessary under clauses (vii) or (ix) if the modification, amendment, acceleration, or deferral, in the reasonable judgment of the Board confers a benefit on the Awardee, or is made pursuant to an adjustment in accordance with Section 14.

The Board may, but need not, determine that an award shall vest or be granted subject to the satisfaction of one or more performance goals. Performance goals for awards will be determined by the Compensation Committee of the Board and will be designed to support the business strategy, and align executives' interests with customer and shareholder interests. For awards that are intended to qualify as performance-based compensation under Section 162(m), performance goals will be based on one or more of the following business criteria: sales or licensing volume, revenues, customer satisfaction, expenses, organizational health/productivity, earnings (which includes similar measurements such as net profits, operating profits and net income, and which may be calculated before or after taxes, interest, depreciation, amortization or taxes), margins, cash flow, shareholder return, return on equity, return on assets or return on investments, working capital, product shipments or releases, brand or product recognition or acceptance and/or stock price. These criteria may be measured: individually, alternatively or in any combination; with respect to the Company, a subsidiary, division, business unit, product line, product or any combination of the foregoing; on an absolute basis, or relative to a target, to a designated comparison group, to results in other periods or to other external measures; and including or excluding items that could affect the measurement, such as extraordinary or unusual and nonrecurring gains or

losses, litigation or claim judgments or settlements, material changes in tax laws, acquisitions or divestitures, the cumulative effect of accounting changes, asset write-downs, restructuring charges, or the results of discontinued operations.

(c) Effect of Board's Decision. All decisions, determinations, and interpretations of the Board shall be final and binding on all Participants and Awardees.

#### 5. Eligibility.

(a) Awards may be granted to Participants and to persons to whom offers of employment as an Employee have been extended; provided that Incentive Stock Options may only be granted to Employees. For avoidance of doubt, directors are not eligible to participate in the Plan unless they are Employees or Consultants.

(b) The maximum number of Shares with respect to which an Award or Awards may be granted to any Participant in any one taxable year of the Company (the "Maximum Annual Participant Award") shall not exceed 20,000,000 Common Shares for Options or SARs, or 5,000,000 shares for Stock Awards (increased, in both cases proportionately, in the event of any stock split, stock dividend or similar event with respect to the Shares). If an Option is in tandem with an SAR, such that the exercise of the Option or SAR with respect to a Share cancels the tandem SAR or Option right, respectively, with respect to each Share, the tandem Option and SAR rights with respect to each Share shall be counted as covering but one Share for purposes of the Maximum Annual Participant Award.

#### 6. Options.

(a) Each Option shall be designated in the written or electronic option agreement as either an Incentive Stock Option or a Nonqualified Stock Option. However, notwithstanding such designations, to the extent that the aggregate fair market value of the Shares with respect to which Options designated as Incentive Stock Options are exercisable for the first time by any Employee during any calendar year (under all plans of the Company) exceeds \$100,000, such Options shall be treated as Nonqualified Stock Options.

(b) For purposes of Section 6(a), Options shall be taken into account in the order in which they were granted, and the fair market value of the Shares shall be determined as of the time the Option with respect to such Shares is granted.

(c) Options converted or substituted under the Plan for any or all outstanding stock options and stock appreciation rights held by employees, consultants, advisors or other option holders granted by entities subsequently acquired by the Company or a subsidiary or affiliate of the Company ("Conversion Options") shall be effective as of the close of the respective mergers into, or acquisitions of such entities by, the Company or a subsidiary or affiliate of the Company; provided that such Conversion Options may not be exercised during any periods that may be specified by the Company immediately following the close of the merger or acquisition necessary to ensure compliance with applicable law. The Conversion Options may be Incentive Stock Options or Nonqualified Stock Options, as determined by the Committee; provided, however, that stock appreciation rights in the acquired entity shall only be converted to or substituted with Nonqualified Stock Options. The Conversion Options shall be options to purchase the number of Common Shares determined by multiplying the number of shares of the acquired entity's common stock underlying each such stock option or stock appreciation right immediately prior to the closing of such merger or acquisition by the number specified in the applicable merger or acquisition agreement for conversion of each share of such entity's common stock to a Common Share (the "Merger Ratio"), rounded down to the closest whole share. Such Conversion Options shall be exercisable at an exercise price per Common Share (increased to the nearest whole cent) equal to the exercise price per share of the acquired entity's common stock under each such stock option or stock appreciation right immediately prior to closing divided by the Merger Ratio. No fractional Common Shares will be issued upon exercise of Conversion Options. In lieu of such issuance, the Common Shares issued pursuant to each such exercise shall be rounded to the closest whole Share. Conversion Options may be granted and exercised without the issuance of an Award Agreement.

#### 7. Stock Awards.

(a) Stock Awards may be granted either alone, in addition to, or in tandem with other Awards granted under the Plan. After the Committee determines that it will offer a Stock Award, it will advise the Awardee in writing or electronically, by means of an Award Agreement, of the terms, conditions and restrictions,

including vesting, if any, related to the offer, including the number of Shares that the Awardee shall be entitled to receive or purchase, the price to be paid, if any, and, if applicable, the time within which the Awardee must accept the offer. The offer shall be accepted by execution of an Award Agreement in the manner determined by the Committee; provided that Shares may be issued to an Awardee under a fully vested Stock Award without the issuance of an Award Agreement.

(b) Unless the Committee determines otherwise, the Award Agreement shall provide for the forfeiture of the non-vested Common Shares underlying such Stock Award upon the Awardee ceasing to be a Participant. To the extent that the Awardee purchased the Shares granted under such Stock Award and any such Shares remain non-vested at the time the Awardee ceases to be a Participant, the cessation of Participant status shall cause an immediate sale of such non-vested Shares to the Company at the original price per Common Share paid by the Awardee.

#### 8. SARs.

(a) The Committee shall have the full power and authority, exercisable in its sole discretion, to grant SARs to selected Awardees. The Committee is authorized to grant both tandem stock appreciation rights ("Tandem SARs") and stand-alone stock appreciation rights ("Stand-Alone SARs") as described below.

#### (b) Tandem SARs.

(i) Awardees may be granted a Tandem SAR, exercisable upon such terms and conditions as the Committee shall establish, to elect between the exercise of the underlying Section 6 Option for Common Shares or the surrender of the Option in exchange for a distribution from the Company in an amount equal to the excess of (A) the fair market value (on the Option surrender date) of the number of Shares in which the Awardee is at the time vested under the surrendered Option (or surrendered portion thereof) over (B) the aggregate exercise price payable for such vested Shares.

(ii) No such Option surrender shall be effective unless it is approved by the Committee, either at the time of the actual Option surrender or at any earlier time. If the surrender is so approved, then the distributions to which the Awardee shall become entitled under this Section 8(b) may be made in Common Shares valued at fair market value on the Option surrender date, in cash, or partly in Shares and partly in cash, as the Committee shall deem appropriate.

(iii) If the surrender of an Option is not approved by the Committee, then the Awardee shall retain whatever rights he or she had under the surrendered Option (or surrendered portion thereof) on the Option surrender date and may exercise such rights at any time prior to the later of (A) five (5) business days after the receipt of the rejection notice or (B) the last day on which the Option is otherwise exercisable in accordance with the terms of the instrument evidencing such Option, but in no event may such rights be exercised more than ten (10) years after the date of the Option grant.

#### (c) Stand-Alone SARs.

(i) An Awardee may be granted a Stand-Alone SAR not tied to any underlying Option under Section 6 of the Plan. The Stand-Alone SAR shall cover a specified number of Common Shares and shall be exercisable upon such terms and conditions as the Committee shall establish. Upon exercise of the Stand-Alone SAR, the holder shall be entitled to receive a distribution from the Company in an amount equal to the excess of (A) the aggregate fair market value (on the exercise date) of the Common Shares underlying the exercised right over (B) the aggregate base price in effect for those Shares.

(ii) The number of Common Shares underlying each Stand-Alone SAR and the base price in effect for those Shares shall be determined by the Committee at the time the Stand-Alone SAR is granted. In no event, however, may the base price per Share be less than the fair market value per underlying Common Share on the grant date.

(iii) The distribution with respect to an exercised Stand-Alone SAR may be made in Common Shares valued at fair market value on the exercise date, in cash, or partly in Shares and partly in cash, as the Committee shall deem appropriate.

(d) The Common Shares underlying any SARs exercised under this Section 8 shall not be available for subsequent issuance under the Plan.

9. Term of Plan. The Plan shall become effective as of the Effective Date. It shall continue in effect until terminated under Section 17 of the Plan.

10. Term of Award; Limitations on Vesting and Repricing.

(a) The term of each Award shall be no more than ten (10) years from the date of grant. However, in the case of an Incentive Stock Option granted to a Participant who, at the time the Option is granted, owns Shares representing more than ten percent (10%) of the voting power of all classes of shares of the Company or any Parent or Subsidiary, the term of the Option shall be no more than five (5) years from the date of grant.

(b) Each Award shall vest over a period of not less than three (3) years from the date of grant, provided that Awards covering up to 50,000,000 shares (increased, proportionately, in the event of any stock split, stock dividend or similar event) may be granted without regard to the 3-year vesting restriction; provided further, that Conversion Options and awards that are granted or vest based on performance goals or that vest in less than three (3) years based on death, disability, or retirement shall not count toward the limit of this Section 10(b).

(c) Without approval of the shareholders of the Company, no Option or SAR may be repriced, replaced, regranted through cancellation, repurchased for cash or other consideration, or modified (except in connection with an adjustment pursuant to Section 14), in each case if the effect would be to reduce the exercise price for the Shares underlying the Option or SAR.

11. Exercise Price and Consideration.

(a) The per Share exercise price under each Award shall be such price as is determined by the Board, subject to the following:

(i) In the case of an Incentive Stock Option

(A) granted to an Employee who, at the time of the grant of such Incentive Stock Option, owns shares representing more than ten percent (10%) of the voting power of all classes of shares of the Company or any Parent or Subsidiary, the per Share exercise price shall be no less than 110% of the fair market value per Share on the date of grant.

(B) granted to any other Employee, the per Share exercise price shall be no less than 100% of the fair market value per Share on the date of grant.

(ii) Except for Conversion Options under Section 6(c), the per Share exercise price under a Nonqualified Stock Option or SAR shall be no less than seventy-five percent (75%) of the fair market value per Share on the date of grant. Notwithstanding the foregoing (or any other provision of the Plan), Options and SARs that are granted to Employees who are non-exempt for purposes of the FLSA, shall satisfy the requirements for exclusion from regular rate of pay for purposes of the FLSA and shall have an exercise price that is at least eighty-five percent (85%) of the fair market value of the underlying Shares at the time of grant; furthermore, such Options or SARs shall not be exercisable within the six (6) month period immediately following the date of grant, except, if so provided in the Award Agreement, in the event of the Awardee's death, disability, or retirement, upon a change in corporate control of the Company, or under such other circumstances as are permitted under the FLSA or rules and regulations thereunder.

(iii) The maximum aggregate number of Shares underlying all Nonqualified Stock Options and SARs with a per Share exercise price of less than fair market value on any grant date that may be granted under this Plan is 50,000,000 Shares (increased, proportionately, in the event of any stock split, or stock dividend or similar event with respect to the Shares); provided that Conversion Options shall not count against the limit of this Section 11(a)(iii).

(b) The fair market value per Share shall be the closing price per share of the Common Share on the Nasdaq Stock Market ("Nasdaq") on the date of grant. If the Shares cease to be listed on Nasdaq, the Board shall designate an alternative method of determining the fair market value of the Shares.

(c) The consideration to be paid for the Shares to be issued upon exercise of an Award, including the method of payment, shall be determined by the Board at the time of grant and may consist of cash and/or check. Payment may also be made by delivering a properly executed exercise notice together with irrevocable instructions to a broker to promptly deliver to the Company the amount of sale proceeds

necessary to pay the exercise price. If the Awardee is an officer of the Company within the meaning of Section 16 of the Exchange Act, the officer may, in addition, be allowed to pay all or part of the purchase price with Shares which, as of the exercise date, the officer has owned for six (6) months or more. If the Awardee is a participant in the 1998 Microsoft Corporation Stock Option Gain And Bonus Deferral Program, he may in addition be allowed to pay all or part of the purchase price of any deferred Option with Shares. Shares used by officers to pay the exercise price shall be valued at their fair market value on the exercise date.

(d) Prior to issuance of the Shares upon exercise of an Award, the Awardee shall pay any federal, state, and local income and employment tax withholding obligations applicable to such Award. If an Awardee is an officer of the Company within the meaning of Section 16 of the Exchange Act, he may elect to pay such withholding tax obligations by having the Company withhold Shares having a value equal to the amount required to be withheld, and any Award under the Plan may permit or require that such withholding tax obligations be paid by having the Company withhold Shares having a value equal to the amount required to be withheld. The value of the Shares to be withheld shall equal the fair market value of the Shares on the day the Award is exercised. The right of an officer to dispose of Shares to the Company in satisfaction of withholding tax obligations shall be deemed to be approved as part of the initial grant of an Award, unless thereafter rescinded, and shall otherwise be made in compliance with Rule 16b-3 and other applicable regulations, and any Award under the Plan may permit or require that such withholding tax obligations be paid by having the Company withhold Shares having a value equal to the amount required to be withheld.

## 12. Exercise of Award.

(a) Procedure for Exercise; Rights as a Shareholder. Any Award granted hereunder shall be exercisable at such times and under such conditions as determined by the Board at the time of grant, and as shall be permissible under the terms of the Plan.

An Award may not be exercised for a fraction of a Share.

An Award shall be deemed to be exercised when written or electronic notice of such exercise has been given to the Company in accordance with the terms of the Award by the person entitled to exercise the Award and full payment for the Shares with respect to which the Award is exercised has been received by the Company. Full payment may, as authorized by the Board, consist of any consideration and method of payment allowable under Section 11(c) of the Plan. Until the issuance (as evidenced by the appropriate entry on the books of the Company or of a duly authorized transfer agent of the Company) of the share certificate evidencing such Shares, no right to vote or receive dividends or any other rights as a shareholder shall exist with respect to the Shares subject to the Award, notwithstanding the exercise of the Award. The Company shall issue (or cause to be issued) such share certificate promptly upon exercise of the Award. In the event that the exercise of an Award is treated in part as the exercise of an Incentive Stock Option and in part as the exercise of a Nonqualified Stock Option pursuant to Section 6(a), the Company shall issue a share certificate evidencing the Shares treated as acquired upon the exercise of an Incentive Stock Option and a separate share certificate evidencing the Shares treated as acquired upon the exercise of a Nonqualified Stock Option, and shall identify each such certificate accordingly in its share transfer records. No adjustment will be made for a dividend or other right for which the record date is prior to the date the share certificate is issued, except as provided in Section 14 of the Plan.

Exercise of an Award in any manner and delivery of the Shares subject to such Award shall result in a decrease in the number of Shares which thereafter may be available, both for purposes of the Plan and for sale under the Award, by the number of Shares as to which the Award is exercised.

(b) Termination of Status as a Participant. In the event of termination of an Awardee's Continuous Status as a Participant, such Awardee may exercise his or her rights under any outstanding Awards to the extent exercisable on the date of termination (but in no event later than the date of expiration of the term of such Award as set forth in the Award Agreement). To the extent that the Awardee was not entitled to exercise his or her rights under such Awards at the date of such termination, or does not exercise such rights within the time specified in the individual Award Agreements, the Awards shall terminate, except as otherwise may be provided in the Award Agreement.



(c) Disability of Awardee. Notwithstanding the provisions of Section 12(b) above, in the event of termination of an Awardee's Continuous Status as a Participant as a result of total and permanent disability (i.e., by reason of any medically determinable physical or mental impairment which can be expected to result in death or which has lasted or can be expected to last for a continuous period of twelve (12) months) (i) the Awardee is unable to engage in any substantial gainful activity, or (ii) the Awardee has received income replacement benefits for at least three months under an accident and health plan covering Company employees):

(i) Any outstanding but unvested Stock Award shall become immediately vested (unless otherwise provided in the Award Agreement); and

(ii) Any outstanding Option or SAR shall vest, but only to the extent of the vesting that would have occurred had the Awardee remained in Continuous Status as a Participant for a period of twelve (12) months after the date on which the Participant ceased performing services as a result of the total and permanent disability. An Option or SAR that is vested pursuant to this Section 12(c) must be exercised within eighteen (18) months (or such shorter time as is specified in the grant) from the date on which the Participant ceased performing services as a result of the total and permanent disability (but in no event later than the date of expiration of the term of such Option or SAR as set forth in the Award Agreement). To the extent that the Awardee was not entitled to exercise such Option or SAR within the time specified herein, the Award shall terminate. This Section 12(c) shall only apply to a Conversion Option to the extent provided in the Award Agreement for the Conversion Option.

(d) Death of Awardee. Notwithstanding the provisions of Section 12(b) above, in the event of the death of an Awardee:

(i) who is at the time of death a Participant with an outstanding Stock Award, all unvested shares under any outstanding Awards shall become immediately vested (unless otherwise provided in the Award Agreement). Such shares may be claimed by the Awardee's estate or by a person who acquired the right to the shares by bequest or inheritance within twelve (12) months following the date of death. Any right to shares not claimed within twelve (12) months from the date of death shall be canceled.

(ii) who is at the time of death a Participant with an outstanding Option or SAR, the Option or SAR will vest, but only to the extent of the vesting that would have occurred had the Awardee continued living and remained in Continuous Status as a Participant twelve (12) months following the date of death. An Option or SAR that is vested pursuant to this Section 12(d)(i) may be exercised, at any time within twelve (12) months following the date of death, by the Awardee's estate or by a person who acquired the right to exercise the Award by bequest or inheritance; or

(iii) whose Option or SAR has not yet expired but whose Continuous Status as a Participant terminated prior to the date of death, the Option or SAR may be exercised, at any time within twelve (12) months following the date of death, by the Awardee's estate or by a person who acquired the right to exercise the Option or SAR by bequest or inheritance, but only to the extent of the right to exercise that had vested at the date of termination.

This Section 12(d) shall only apply to a Conversion Option to the extent provided in the Award Agreement for the Conversion Option.

(e) Notwithstanding subsections (b), (c), and (d) of this Section 12, the Board shall have the authority to extend the expiration date of any outstanding Option in circumstances in which it deems such action to be appropriate (provided that no such extension shall extend the term of an Award beyond the date on which the Award would have expired if no termination of the Employee's Continuous Status as a Participant had occurred).

13. Non-Transferability of Awards. An Award may not be sold, pledged, assigned, hypothecated, transferred, or disposed of in any manner other than by will or by the laws of descent or distribution and may be exercised, during the lifetime of the Awardee, only by the Awardee; provided that the Board may permit further transferability, on a general or specific basis, and may impose conditions and limitations on any permitted transferability.

14. Adjustments to Shares Subject to the Plan. If any change is made to the Shares by reason of any stock split, stock dividend, recapitalization, combination of shares, exchange of shares or other change affecting the outstanding Shares as a class without the Company's receipt of consideration, appropriate

adjustments shall be made to (i) the maximum number and/or class of securities issuable under the Plan, (ii) the number and/or class of securities and/or the price per Share covered by outstanding Awards under the Plan, (iii) the Maximum Annual Participant Award, (iv) the maximum aggregate number of Shares underlying all Nonqualified Stock Options and SARs with a per Share exercise price of less than fair market value on any grant date that may be granted under the Plan, and (v) the maximum aggregate number of Shares underlying all Awards with a vesting period of less than three years. The Board may also make adjustments described in (i)-(v) of the previous sentence in the event of any distribution of assets to shareholders other than a normal cash dividend. In determining adjustments to be made under this Section 14, the Board may take into account such factors as it deems appropriate, including (i) the restrictions of applicable law, (ii) the potential tax consequences of an adjustment and (iii) the possibility that some Awardees might receive an adjustment and a distribution or other unintended benefit, and in light of such factors or circumstances may make adjustments that are not uniform or proportionate among outstanding Awards, modify vesting dates, defer the delivery of stock certificates or make other equitable adjustments. Any such adjustments to outstanding Awards will be effected in a manner that precludes the enlargement of rights and benefits under such Awards. Adjustments, if any, and any determinations or interpretations, including any determination of whether a distribution is other than a normal cash dividend, made by the Board shall be final, binding and conclusive. For purposes of this Section 14, conversion of any convertible securities of the Company shall not be deemed to have been effected without receipt of consideration. Except as expressly provided herein, no issuance by the Company of shares of any class, or securities convertible into shares of any class, shall affect, and no adjustment by reason thereof shall be made with respect to, the number or price of Shares subject to an Award.

In the event of the proposed dissolution or liquidation of the Company, the Award will terminate immediately prior to the consummation of such proposed action, unless otherwise provided by the Board. The Board may, in the exercise of its sole discretion in such instances, declare that any Award shall terminate as of a date fixed by the Board and give each Awardee the right to exercise an Award as to all or any part of the Shares subject to an Award, including Shares as to which the Award would not otherwise be exercisable. In the event of a proposed sale of all or substantially all of the assets of the Company, or the merger of the Company with or into another corporation, each Award shall be assumed or an equivalent award shall be substituted by such successor corporation or a parent or subsidiary of such successor corporation, unless such successor corporation does not agree to assume the Award or to substitute an equivalent award, in which case the Board shall, in lieu of such assumption or substitution, provide for the Awardee to have the right to exercise the Award as to all of the Shares subject to Awards, including Shares as to which the Award would not otherwise be exercisable. If the Board makes an Award fully exercisable in lieu of assumption or substitution in the event of a merger or sale of assets, the Board shall notify the Awardee that the Award shall be fully exercisable for a period of fifteen (15) days from the date of such notice, and the Award will terminate upon the expiration of such period.

15. Time of Granting Awards. The date of grant of an Award shall, for all purposes, be the date on which the Company completes the corporate action relating to the grant of such Award and all conditions to the grant have been satisfied, provided that conditions to the grant, exercise or vesting of an Award shall not defer the date of grant. Notice of a grant shall be given to each Participant to whom an Award is so granted within a reasonable time after the determination has been made.

16. Substitutions and Assumptions. The Board shall have the right to substitute or assume Awards in connection with mergers, reorganizations, separations, or other transactions to which Section 424(a) of the Code applies, provided such substitutions and assumptions are permitted by Section 424 of the Code and the regulations promulgated thereunder. The number of Shares reserved pursuant to Section 3 may be increased by the corresponding number of Awards assumed and, in the case of a substitution, by the net increase in the number of Shares subject to Awards before and after the substitution.

17. Amendment and Termination of the Plan.

(a) Amendment and Termination. The Board may amend or terminate the Plan from time to time in such respects as the Board may deem advisable (including, but not limited to amendments which the Board deems appropriate to enhance the Company's ability to claim deductions related to stock option exercises); provided that any increase in the number of Shares subject to the Plan, other than in connection with an adjustment under Section 14 of the Plan, and any amendment described in Section 10(c) of the Plan, shall require approval of or ratification by the shareholders of the Company.

(b) Participants in Foreign Countries. The Board shall have the authority to adopt such modifications, procedures, and subplans as may be necessary or desirable to comply with provisions of the laws of foreign countries in which the Company or its Subsidiaries may operate to assure the viability of the benefits from Awards granted to Participants performing services in such countries and to meet the objectives of the Plan.

(c) Effect of Amendment or Termination. Except as otherwise provided in Sections 4 and 14, any such amendment or termination of the Plan shall not affect Awards already granted and such Awards shall remain in full force and effect as if this Plan had not been amended or terminated, unless mutually agreed otherwise between the Awardee and the Board, which agreement must be in writing and signed by the Awardee and the Company.

18. Conditions Upon Issuance of Shares. Shares shall not be issued pursuant to the exercise of an Award unless the exercise of such Award and the issuance and delivery of such Shares pursuant thereto shall comply with all relevant provisions of law, including, without limitation, the Securities Act of 1933, as amended, the Exchange Act, the rules and regulations promulgated thereunder, and the requirements of any stock exchange upon which the Shares may then be listed, and shall be further subject to the approval of counsel for the Company with respect to such compliance.

19. Reservation of Shares. The Company, during the term of this Plan, will at all times reserve and keep available such number of Shares as shall be sufficient to satisfy the requirements of the Plan.

20. No Employment/Service Rights. Nothing in the Plan shall confer upon any Participant the right to an Award or to continue in service as an Employee or Consultant for any period of specific duration, or interfere with or otherwise restrict in any way the rights of the Company (or any Parent or Subsidiary employing or retaining such person), or of any Participant or Awardee, which rights are hereby expressly reserved by each, to terminate such person's services at any time for any reason, with or without cause.

\* All share numbers in the Plan reflect the 2-for-1 stock split effected February 2003.

**AMENDED AND RESTATED  
OFFICERS' INDEMNIFICATION TRUST AGREEMENT**

This AMENDED AND RESTATED OFFICERS' INDEMNIFICATION TRUST AGREEMENT (this "**Trust**" or this "**Agreement**") is amended and restated effective as of June 30, 2016 (the "**Effective Date**"), between MICROSOFT CORPORATION, a Washington corporation ("**Grantor**"), and The Bank of New York Mellon Trust Company, N.A. (the "**Trustee**"), whose address is 400 South Hope Street, Suite 500, Los Angeles, California 90071, and, as an additional party, Charles H. Noski (the "**Beneficiaries' Representative**").

**RECITALS**

A. Grantor established this Trust and its predecessors to be a source of indemnification for Grantor's Officers who are eligible for indemnification as stated in this Trust as it is in effect from time to time.

B. Grantor has determined, after due diligence, that it has and will continue to derive substantial economic benefits from this Trust, including from economic terms that are more favorable to Grantor than obtaining protection for its Officers through the current director and officer insurance market.

C. Grantor's Articles of Incorporation (the "**Articles**") provide for mandatory indemnification of Grantor's Officers (as defined in the Articles) to the maximum extent provided by law, and as such, this Trust is not an exclusive source of indemnification for the Officers as covered in this Agreement.

D. Grantor has determined that the Trust continues to be necessary in order for Grantor to attract and retain the most qualified Officers. Grantor has also determined to increase the Minimum Balance to reflect current market conditions.

E. This Agreement amends, restates and replaces the 2009 Officers' Indemnification Trust Agreement dated June 28, 2009 established by Grantor, with The Bank of New York Mellon Trust Company, N.A., as Trustee therein and Charles H. Noski as Beneficiaries' Representative therein (the "**2009 Trust**"). Grantor's Board of Directors has acted by resolution adopted March 15, 2016 to amend and restate the 2009 Trust effective as of the Effective Date.

F. The 2009 Trust replaced the Trust Agreement dated June 1, 1993 established by Grantor, with The Bank of New York Mellon Trust Company, N.A., successor in interest to BNY Western Trust Company, as Trustee therein and Charles Noski as Beneficiaries' Representative therein (the "**1993 Trust**").

G. This Trust also is designed to provide continuing coverage for the "executive officers" as such term is used in the 1993 Trust as such coverage was effective upon execution of the 2009 Trust, with such coverage to overlap with the 1993 Trust for certain officers of Grantor prior to termination of the 1993 Trust.

H. Except as otherwise noted, the capitalized terms have the meaning ascribed to them in the body of this Agreement.

## AGREEMENT

NOW, THEREFORE, Grantor will transfer to the Trustee funds as provided on **Exhibit A** of this Agreement and the Trustee acknowledges the Minimum Balance on June 30, 2016, accepts the trust created hereby and agrees that it will hold all property which it may receive hereunder, as custodian IN TRUST, for the purposes and upon the terms and conditions hereinafter stated, and Grantor, the Trustee and the Beneficiaries' Representative agree as follows:

### ARTICLE 1 DEFINITIONS

**"1993 Trust"** is defined in Section F of the Recitals.

**"2009 Trust"** is defined in Section E of the Recitals.

**"Act"** means the Washington Business Corporation Act RCW 23B or succession legislation.

**"Additional Contributions"** is defined in Section 4.4.

**"Adverse Determination"** is defined in Section 4.11.

**"Agreement"** is defined in the Preamble.

**"Articles"** is defined in Section C of the Recitals.

**"Beneficiary"** and **"Beneficiaries"** are defined in Section 3.1.

**"Beneficiaries' Representative"** is defined in the Preamble.

**"Board of Directors"** means the board of directors of Microsoft Corporation as constituted from time to time.

**"Business Day"** means any day, excluding Saturday, Sunday and any day on which banking institutions located in Seattle, Washington or Los Angeles, CA are authorized by applicable law to be closed.

**"Cash"** means (a) currency of the United States, and (b) certificates of deposit or time deposits having, in each case, a tenor of not more than six (6) months, issued by any U.S. commercial bank or any branch or agency of a non-U.S. bank licensed to conduct business in the U.S. having combined capital and surplus of not less than \$250,000,000 (including the Trustee and its affiliates).

“**Change of Control**” is defined in Section 3.1.

“**Claim**” or “**Claims**” includes, without limitation, any threatened, pending, or completed action, suit, or proceeding, whether civil, derivative, criminal, administrative, investigative, or otherwise, initiated by a person other than the Beneficiary (including any Claims by or in the right of Grantor), unless the Claim was initiated by the Beneficiary in good faith to establish or enforce a right to indemnification under the Articles, this Trust or applicable statute.

“**Collateral**” is defined in Section 4.11.

“**Covered Act**” means any act or omission (including, without limitation, any alleged breach of duty, neglect, error, misstatement, misleading statement, or otherwise, or appearing as or preparing to be a witness) by a Beneficiary, and any Claim against such Beneficiary, by reason of the fact that Beneficiary (a) is or was an Officer of Grantor, (b) is or was an executive officer “Beneficiary” under the 1993 Trust, or (c) is or was an Officer of Grantor or executive officer “Beneficiary” under the 1993 Trust and is or was serving at the request of Grantor as a director, officer, partner, trustee, fiduciary, employee or agent of another corporation, partnership, joint venture, trust, employee benefit plan or other enterprise.

“**Corporate Securities**” means US dollar denominated senior debt obligations that are obligations (whether direct or by virtue of guarantees) of corporations organized in the United States whose long-term, unsecured, unsubordinated debt securities are rated at least “A” (or its equivalent successor rating) in the case of Standard & Poor’s Ratings Group or “A2” (or its equivalent successor rating) in the case of Moody’s Investors Service, Inc.

“**Demand**” is defined in Section 4.7.1.

“**Director**” means a current, past or future member of the Board of Directors.

“**Effective Date**” is defined in the Preamble.

“**Eligible Securities**” means Cash, Treasury Securities, Government Securities, Municipal Securities, Corporate Securities, Money Market Funds and Other Eligible Securities. All Eligible Securities must be in a form suitable for delivery and retransfer, and must be capable of being priced by recognized third-party dealers.

“**Excluded Claim**” means any payment for Losses or Expenses in connection with any Claim the payment of which is Ultimately Determined to be prohibited by the Act, public policy, or other applicable law (including binding regulations and orders of, and undertakings or other commitments with, any governmental entity or agency) as the same exists or may hereafter be amended (but, in the case of any such amendment, only to the extent that such amendment permits Grantor to provide broader indemnification rights than said law permitted Grantor to provide prior to such amendment). For the avoidance of doubt, a “**knowing violation of law**” means a conscious, intentional and deliberate act or failure to act (a) that is a material breach of applicable law, (b) that is done with actual knowledge that such act or failure to act is a material breach of applicable law, (c) that is done with the intent that such act or failure to act will be a material

breach of applicable law, (d) that is done with actual knowledge that such act or failure to act will inflict material harm on Grantor, (e) that is done with the intent that such act or failure to act will inflict material harm on Grantor, and (f) that such act or failure to act does inflict such material harm on Grantor. For the avoidance of doubt, "**intentional misconduct**" means a conscious, intentional and deliberate act or failure to act (a) that is done with actual knowledge that such misconduct will inflict material harm on Grantor, (b) that is done with the intent to inflict material harm on Grantor, and (c) that such misconduct does inflict such material harm on Grantor.

"**Executive Officers**" means those employees of the Grantor designated as executive officers by the Grantor's Board of Directors from time to time.

"**Expenses**" means any reasonable expenses incurred by Beneficiary as a result of a Claim or Claims made against him or her for Covered Acts including, without limitation, counsel fees and costs of investigative, judicial, or administrative proceedings and any appeals.

"**Fines**" shall include any fine, penalty or, with respect to an employee benefit plan, any excise tax, or penalty assessed with respect thereto.

"**Government Securities**" means bonds, notes, debentures, obligations or other evidence of indebtedness issued and/or guaranteed by the Federal National Mortgage Association, the Federal Home Loan Mortgage Corporation or the Government National Mortgage Association, including mortgage participation certificates, mortgage pass-through certificates and other mortgage-backed securities, but excluding collateralized mortgage obligations and mortgage-related securities representing payments of interest only or principal only and REMIC securities and CMBS (commercial mortgage backed securities).

"**Grantor**" is defined in the Preamble.

"**Loss**" means any amount which a Beneficiary is legally obligated to pay as a result of any Claim or Claims made against him or her for Covered Acts including, without limitation, Fines, damages, judgments, costs of defense of any Claims and sums paid in settlement of any Claim or Claims, specifically including fees of plaintiff's counsel.

"**Minimum Balance**" is defined in Section 4.2.

"**Money Market Funds**" means money market funds rated "AAAm" or "AAAm-G" by Standard & Poor's Rating Service or having a rating in the highest investment category granted thereby from Moody's Investors Service, including, without limitation, any mutual fund for which the Trustee or an affiliate of the Trustee serves as investment manager, administrator, shareholder servicing agent and/or custodian or subcustodian, notwithstanding that (a) the Trustee or an affiliate of the Trustee receives fees from funds for services rendered, (b) the Trustee collects fees for services rendered pursuant to this Agreement, which fees are separate from the fees received from such funds, and (c) services performed for such funds and pursuant to this Agreement may at times duplicate those provided to such funds by the Trustee or an affiliate of the Trustee.

**"Municipal Securities"** means senior and unsubordinated debt obligations that are obligations (whether direct or by virtue of guarantees) of U.S. state or municipal issuers whose long-term, unsecured, unsubordinated, debt securities are rated at least "A" (or its equivalent successor rating) in the case of Standard & Poor's Ratings Group or "A2" (or its equivalent successor rating) in the case of Moody's Investors Service, Inc., excluding "A" or "A2" rated debt securities of housing and hospital issuers and municipal funds and partnerships where the rating is not based upon the rating of a third-party credit enhancer of such securities.

**"Officer"** means any employee of Grantor elected, designated or appointed by the Board of Directors as an officer at a level "corporate vice president" or higher as of July 1, 2009 and from time to time thereafter.

**"Other Eligible Securities"** means securities other than Cash, Corporate Securities, Treasury Securities, Government Securities, Money Market Funds and Municipal Securities mutually agreed upon in writing by the Beneficiaries' Representative and Grantor.

**"Treasury Securities"** means securities issued or guaranteed by the United States government, including United States Department of the Treasury obligations and any other obligations the timely payment of principal and interest of which is fully and unconditionally guaranteed by the United States government.

**"Trust"** is defined in the Preamble.

**"Trust Fund"** is defined in Section 4.1.

**"Trustee"** is defined in the Preamble.

**"UCC"** is defined in Section 4.11.3.

**"Ultimate Determination"** means a final order from which there is no further right of appeal in any action in which a Beneficiary seeks indemnification. Such an order shall constitute the Ultimate Determination of the Beneficiary's right to indemnification from Grantor. **"Ultimately Determined"** shall have a correlative meaning.

## **ARTICLE 2 PRIOR COVERED ACTS AND CLAIMS**

**2.1 Indemnification for Covered Acts.** The Beneficiaries under this Trust shall be indemnified for any Losses, Expenses or Fines that result from a Claim based on a Covered Act asserted while this Trust is in effect without regard to whether the Covered Act occurred on, before or after the establishment of this Trust. Rights to coverage as a Beneficiary under this Agreement shall be deemed to vest with and upon such person's appointment as an Officer. If a Beneficiary of this Trust was also a "Beneficiary" of the 1993 Trust prior to its termination and the 2009 Trust, such person shall be covered by this Trust as a Beneficiary hereunder for Covered Acts as defined herein and also as to "Covered Acts" under such prior trust agreements that occurred prior to the Effective Date.



**2.2 Nonexclusive Remedy.** The rights of Beneficiaries to indemnification from this Trust are limited to the assets of the Trust, but this does not limit any Beneficiary's rights, if any, to indemnification (without duplication) from Grantor, or other Grantor arrangements or obligations, including but not limited to any applicable insurance coverage.

**ARTICLE 3  
THE BENEFICIARIES AND THE  
BENEFICIARIES' REPRESENTATIVE**

**3.1 The Beneficiaries.** All present and future Officers as well as any executive officers of Grantor who were "Beneficiaries" of the 1993 Trust (for Covered Acts as defined herein during their employment as an executive officer of Grantor as provided in the 1993 Trust) shall be "**Beneficiaries**" of this Trust (and each a "**Beneficiary**"), *provided, however*, that if there is a Change in Control of Grantor, no Officers appointed after or in connection with such Change in Control shall be entitled to be Beneficiaries who were not Beneficiaries under this Agreement, the 2009 Trust or the 1993 Trust prior to such Change in Control. For purposes of this Agreement, "**Change of Control**" shall mean (a) a tender offer or exchange offer in which the purpose of such offer is to take over and control Grantor and such offer is accepted by owners of securities of Grantor representing 50% or more of the combined voting power of Grantor's then outstanding voting securities, (b) Grantor is merged or consolidated with another corporation and as a result of such merger or consolidation less than 50% of the outstanding voting securities of the surviving or resulting corporation shall then be owned in the aggregate by the former shareholders of Grantor, (c) Grantor transfers substantially all of its assets to another corporation which is not a wholly-owned subsidiary of Grantor, or (d) during any period of twelve (12) consecutive months, individuals who at the beginning of such twelve (12) month period were directors of Grantor cease for any reason to constitute at least a majority of Grantor's Board of Directors. The Beneficiaries' Representative shall promptly notify the Trustee in writing of a Change in Control. Any Beneficiary shall remain a Beneficiary despite his or her resignation, removal, or other failure to continue to be an Officer during the term of this Agreement as to Covered Acts during such Beneficiary's service as an Officer or as an executive officer under the 1993 Trust. A person whose conduct gives rise to a right of indemnification both as a member of the Board of Directors and as an Officer of Grantor, shall be a Beneficiary hereunder as to all such conduct without being required to separate his or her activities between the role of Director and the role of Officer.

**3.2 New Beneficiaries.** If prior to a Change in Control an individual is appointed as an Officer by Grantor's Board of Directors, Grantor agrees to notify the Trustee and the Beneficiaries' Representative promptly of such appointment; *provided, however*, Grantor's failure to so notify the Trustee and the Beneficiaries' Representative shall not affect in any way an individual Officer's rights as a Beneficiary under this Trust. The Trustee and the Beneficiaries' Representative shall have the right to rely on the accuracy and completeness of any statement provided to it by Grantor's Secretary, Assistant Secretary or Chief Executive Officer as to the Beneficiary status of any individual.

**3.3 Beneficiaries' Representative.** Except as expressly provided elsewhere in this Agreement, all communications or demands made by and among the Trustee and the Beneficiaries

are to be made through the individual then designated as the Beneficiaries' Representative. The Beneficiaries' Representative shall have the exclusive right to convey Demands from time to time on the Trustee to direct payment to one or more of the Beneficiaries.

**3.4 Identity of Beneficiaries' Representative.** The Beneficiaries' Representative shall be a person who is a present or past nonemployee Director of Grantor, designated in writing to the Trustee and Grantor from time to time by a majority of the nonemployee Directors on the Board of Directors. For this purpose, a Director who has not been employed by Grantor during the current calendar year and the preceding three (3) years shall be regarded as a nonemployee Director. The Trustee, Grantor and Beneficiaries shall be entitled to rely on the original appointment of that individual as the Beneficiaries' Representative unless notified in writing of a change in the Beneficiaries' Representative by a writing signed by the former Beneficiaries' Representative. A Beneficiary shall be deemed to have consented to such change in Beneficiaries' Representative if such Beneficiary is provided with notice of such change in accordance with Section 8.6 and does not provide written notice of objection to the change within ten (10) days. The Trustee shall be entitled to rely on such subsequent appointment as of the date such writing is received by the Trustee. The Trustee shall be entitled to rely on the accuracy and completeness of a written list delivered to the Trustee by Grantor, and certified by the Secretary of Grantor to be accurate and to have been prepared in good faith, identifying the individuals who constitute the then current nonemployee Directors. In the absence of an effective appointment of a Beneficiaries' Representative, the Trustee or any Beneficiary may, after ten (10) days' written notice to all Beneficiaries and Grantor, petition a court of competent jurisdiction at the expense of the Trust for appointment of a Beneficiaries' Representative who need not be a nonemployee Director (if none are willing or able to serve), but shall in no event be an Officer or Director elected or appointed after a Change in Control who was not a Beneficiary prior to such Change in Control. The designation or appointment of a successor Beneficiaries' Representative shall become effective only upon the execution of a counterpart of this Agreement whereby such successor Beneficiaries' Representative shall assume and become bound by all the duties and responsibilities of a Beneficiaries' Representative under this Agreement.

**3.5 Right of Beneficiaries to Receive Payments.** Subject to court order to the contrary, the rights of the Beneficiaries to make a Demand and receive distributions from the Trustee shall not be affected or diminished in any way by the existence of any dispute between one or more Beneficiaries and Grantor or anyone acting on behalf of Grantor in a derivative or representative capacity, and the Trustee in making distributions from the Trust Fund shall be entitled to rely upon the simple Demand of a Beneficiary, as conveyed by the Beneficiaries' Representative pursuant to Section 4.7. Such distributions shall be made notwithstanding any notice or demand by or on behalf of Grantor or anyone acting on behalf of Grantor in a derivative or representative capacity that the distributions should not be made, whether based on Grantor's claim that any Beneficiary is not entitled to some or all of the amount of such distributions or otherwise. The Trustee shall have no responsibility or liability to Grantor for making any payment despite having received any such notice or demand by or on behalf of Grantor. The Trustee shall have no responsibility to inquire into the accuracy or truthfulness of any such notice or demand, whether from Grantor or the Beneficiaries' Representative.

**ARTICLE 4**  
**THE TRUST FUND**

**4.1 Trust Fund; Grantor Trust.** The Trustee shall hold all property received by it as custodian in Trust hereunder as one fund which, together with the income and gains therefrom and additions thereto, shall constitute the "**Trust Fund**." The Trust is intended to be a grantor trust within the meaning of Section 671 of the Internal Revenue Code of 1986, as amended, and shall be construed accordingly. The Trust Fund shall not be paid to Grantor or any trustee in bankruptcy of Grantor, shall be held separate and apart from other funds of Grantor, and shall be used exclusively for the purposes set forth herein.

**4.2 Minimum Balance.** Grantor shall cause the Trustee to treat the 2009 Trust funds as part of the Minimum Balance under this Agreement to this Trust effective June 30, 2016. Grantor shall transfer as of the effective date of this Agreement an additional sum sufficient to cause the total balance held by the Trustee to equal \$50,000,000 which thereafter shall be the "**Minimum Balance**," and Trustee shall hold such funds in trust for the stated uses and purposes in accordance with the terms of this Agreement. Nothing contained in this Agreement shall preclude Grantor from making additional transfers of funds from time to time to the Trustee, whether required under the terms of this Agreement or not, to be held in trust as part of the Trust Fund. If Grantor makes additional transfers of funds to the Trust Fund, such additional transfers shall be deemed an increase of the Minimum Balance and **Exhibit A** shall be automatically amended without further action by the parties to this Agreement. Grantor and the Beneficiaries' Representative shall periodically, but no less than every third anniversary of this Agreement, review the adequacy of the Minimum Balance.

**4.3 Maintenance of Minimum Balance.** The Trustee agrees to provide monthly reports to Grantor and the Beneficiaries' Representative showing the current fair market value of the Trust Fund. If any such report shows that the current fair market value of the Trust Fund is less than the Minimum Balance, then within ten (10) days after such report, Grantor agrees to deliver cash funds to the Trustee equal to the difference between the fair market value of the Trust Fund and the Minimum Balance so that the Trust balance is at least equal to the Minimum Balance. Notwithstanding the foregoing, Grantor shall have no obligation to make payments to the Trustee in excess of \$400,000,000 (including the initial transfer of the 2009 Trust funds and the additional funds pursuant to Section 4.4) under or with respect to this Agreement.

**4.4 Additional Contributions.** Subject to the aggregate limitation of \$400,000,000 set forth in Section 4.3, Grantor agrees to make additional contributions ("**Additional Contributions**") to the Trust Fund within ten (10) days after receipt of a written request from the Beneficiaries' Representative certifying in good faith that Claims have or are reasonably expected to be asserted against Beneficiaries and that estimated Losses and Expenses for all pending, threatened or anticipated Claims against all Beneficiaries are reasonably expected to exceed the then Trust Fund balance. A copy of such written certification shall be provided to the Trustee at the same time and in the same manner as it is provided to Grantor. Such written certification shall be accompanied by an opinion of independent counsel to the effect that, based on the information made known to such counsel, (a) the Claims do not appear to be Excluded Claims and (b) the amount requested seems reasonable in the circumstances noted above. Independent counsel shall be selected by the Beneficiaries' Representative and shall have no present professional relationship with Grantor or the Beneficiaries who are the subject of the Claims.

**4.5 Excess Balance.** If at any time the fair market value of the Trust Fund shall exceed the Minimum Balance, plus any additional contributions which continue to be required pursuant to Section 4.4, Grantor shall be entitled to withdraw an amount equal to the excess over the said sum upon thirty (30) days' advance written notice to the Beneficiaries' Representative.

**4.6 Direction of Investment.** Notwithstanding anything contained in this Agreement to the contrary, Grantor retains the right to direct the investment of the Trust Fund and the Trustee shall have no duty to review or recommend investments; *provided, however,* that Grantor shall only direct the Trustee to invest the Trust Fund in Eligible Securities in accordance with Grantor's current cash-management policies. If Grantor instructs the Trustee to invest in securities other than in Cash, Government Securities, Municipal Securities, Corporate Securities, Money Market Funds or Treasury Securities, such instruction shall be accompanied by the written consent of the Beneficiaries' Representative as to the investment(s) in such Other Eligible Securities. Unless otherwise instructed by Grantor in writing, the Trustee shall initially maintain the investments in the account or accounts transferred from the 2009 Trust, which amounts following transfer shall be subject to this Section 4.6. If for any reason one or more existing investments shall not be available going forward, and Grantor shall fail to direct the Trustee pursuant to written instructions as to how to invest the Trust Fund (including the consent of the Beneficiaries' Representative if the proposed investment is in other than Eligible Securities), then the Trustee shall invest the Trust Fund in a accordance with the last instruction received. In the event the Trustee is required to make a distribution pursuant to Section 4.7 at a time when the Trust Fund has insufficient cash to cover such distribution, the Trustee shall promptly notify the Grantor. The Grantor shall then direct the Trustee as to which Trust investments to liquidate in order to cover the required distribution; if Grantor does not respond to the Trustee's inquiry within forty-eight (48) hours the Trustee shall liquidate investments in the order specified in **Exhibit B**. The Trustee may purchase or sell to itself or any affiliate, as principal or agent, investments authorized by this Agreement. Grantor and the Beneficiaries' Representative acknowledge that regulations of the Comptroller of the Currency grant the right to receive brokerage confirmations of the security transactions as they occur, at no additional cost. To the extent permitted by law, Grantor and the Beneficiaries' Representative specifically waive compliance with 12 CFR 12 and hereby notify the Trustee that no brokerage confirmations need be sent relating to the security transactions as they occur.

#### **4.7 Distributions from Trust Fund.**

**4.7.1 Duties of Beneficiary.** A Beneficiary making a demand for indemnity shall certify in each demand regarding a Claim for a Covered Act (a "**Demand**") delivered to the Beneficiaries' Representative that (a) he or she is entitled to payment of at least the amount demanded, (b) no part of the Demand is an Excluded Claim or is precluded by the Act or applicable successor statute, (c) the Beneficiary will repay to the Trust any amounts paid or applied to or for the use of such Beneficiary in the event of an Ultimate Determination that such payments are Excluded Claims or precluded by the Act, or in the event the Beneficiary receives payment for the same Claim from another source, (d) a request to Grantor for indemnification has remained unsatisfied for twenty (20) days and that no part of the amount then being demanded

from the Trust Fund has been previously received from Grantor, and (e) he or she has complied with any applicable requirements of Grantor's Articles and policy with respect to indemnification, if any, with respect to the Demand.

**4.7.2 Duties of Beneficiaries' Representative.** The Beneficiaries' Representative shall convey a Beneficiary's Demand to the Trustee. Along with the conveyance of such Demand to the Trustee, the Beneficiaries' Representative shall submit, in a writing signed by the Beneficiaries' Representative, a statement (a) that such Demand is being made pursuant to the Articles and this Agreement, as each such may be amended and restated from time to time, provided that any such amendment shall be given effect under this Agreement only to the extent that such amendment provides broader indemnification rights than existed prior to such amendment, (b) that the Demand is for satisfaction of indemnification obligations of Grantor, (c) that the Demand is being made by a Beneficiary, (d) that specifies the amounts being demanded by such Beneficiary, and (e) that the Beneficiaries' Representative is not aware of any facts or conditions that would make such Demand for indemnification pursuant to this Agreement invalid, *provided, however*, that the Beneficiaries' Representative has no duty to independently investigate the validity of a Demand.

**4.7.3 Duties of Trustee.** The Trustee shall deliver a copy of each Demand to Grantor as promptly as reasonably possible. A copy of the Beneficiaries' Representative's statement also shall be delivered to Grantor. As soon as practicable after any such Demand is conveyed by the Beneficiaries' Representative, subject to the provisions of Section 3.5, the Trustee shall distribute funds to the Beneficiary specified in such Demand in the amount and manner set forth therein. If the Trustee does not have sufficient funds to satisfy all pending Demands of Beneficiaries in full, the Trustee shall make all reasonable efforts to make pro rata payments, less any amounts due the Trustee, to the Beneficiaries as specified by the Beneficiaries' Representative. If and to the extent the Trust Fund is replenished, the Trustee shall continue to make pro rata distributions, less any amounts due the Trustee, until the Demand is satisfied or to satisfy subsequent Demands.

**4.8 Taxes.** Grantor agrees to pay any and all taxes on the Trust Fund or the income thereof which the Beneficiaries or the Trustee would otherwise be required to pay with respect to the interest of any person or persons therein, and to provide the Trustee and the Beneficiaries' Representative with proof of payment. This does not include any taxes payable upon an indemnification payment distribution from the Trust if the same would be taxable to the recipient Beneficiary under applicable law.

**4.9 Duties and Responsibilities of Beneficiaries' Representative.** The Beneficiaries' Representative (and any successor Beneficiaries' Representative) shall have the following affirmative duties and responsibilities:

4.9.1 To demand deposits from Grantor so as to maintain the Minimum Balance of the Trust in accordance with Section 3.3 and any Additional Contributions required by Section 3.4;

4.9.2 To demand payment by the Trustee to a Beneficiary who has made a Demand and who, in the good faith judgment of the Beneficiaries' Representative, has satisfied the conditions for indemnification as set forth in this Agreement and the Articles, *provided, however*, that the Beneficiaries' Representative has no duty to independently investigate the validity of a Demand; and

4.9.3 To use commercially reasonable efforts to cause Grantor and the Trustee to discharge their respective responsibilities under this Agreement and the responsibilities of Grantor under the Articles, including the bringing of legal actions and proceedings to enforce such agreement.

**4.10 Administrative Powers of Trustee.** Subject to Grantor's right pursuant to Section 4.6 to direct investment of the Trust Fund in Eligible Securities, the Trustee shall have the power to do any of the following:

4.10.1 To cause any investment to be registered and held in the name of one or more of its nominees, or one or more nominees of any system for the central handling of securities, without increase or decrease of liability;

4.10.2 To collect and receive any and all money and other property due to the Trust Fund and to give full discharge therefor; and

4.10.3 To hold uninvested, without liability for interest thereon, such monies received by the Trustee as the Trustee considers necessary to meet anticipated and imminent disbursements.

**4.11 Adverse Determination.** In the event the trust arrangement created hereby is deemed to be invalid or ineffective as a trust by a court of competent jurisdiction, whether in connection with the bankruptcy of one of the parties hereto or otherwise (an "**Adverse Determination**"), then the parties agree that the nature of their relationship shall be Grantor as debtor, the Trustee as securities intermediary and the Beneficiaries' Representative as secured party for the benefit of the Beneficiaries. To that end, and to secure the obligation of Grantor to indemnify Beneficiaries, Grantor hereby grants the Beneficiaries' Representative for the benefit of the Beneficiaries a continuing security interest in, and pledges all rights, title and interest in and to, the following (for purposes of this Section 4.11, the "**Collateral**"):

4.11.1 The Trust(s) account and the Trust Fund, and any certificates or instruments representing or evidencing the Trust Fund, and all cash, investment property, interest, dividends, rights and other property at any time and from time to time received, receivable or otherwise issued, distributed or distributable in respect of or in exchange for any or all of the Trust Fund;

4.11.2 All other investment property and other property hereafter issued, delivered or deliverable to Trustee in substitution for or in addition to any of the foregoing, all certificates and instruments representing or evidencing such other property and all cash, investment property, interest, dividends, rights and other property at any time and from time to time received, receivable or otherwise issued, distributed or distributable after the date hereof in respect of or in exchange for any or all thereof; and

4.11.3 All proceeds of all of the foregoing.

Grantor and, at the direction of the Beneficiaries' Representative, the Trustee shall execute such other documents and instruments as the Beneficiaries' Representative may reasonably require from time to time to perfect and protect the first priority security interest of the Beneficiaries' Representative on behalf of the Beneficiaries in the Collateral. In the event of an Adverse Determination, the Beneficiaries' Representative shall have and shall be deemed to have had all the rights and remedies of a secured party under Article 9 of the Uniform Commercial Code ("**UCC**") and may exercise any of the rights and remedies available to the Beneficiaries' Representative under the UCC as in effect from time to time in the State of Washington or otherwise available to the Beneficiaries' Representative, including, without limitation, sale, assignment or other disposal of the Collateral in exchange for cash or credit. Grantor agrees that a Demand is also a notice of disposition under Section 9-611 of the UCC and that five (5) Business Days is reasonable notice if notice of a disposition is required under Section 9-611 of the UCC. Furthermore, Grantor agrees that any Beneficiary may be the purchaser of the Collateral consisting of Cash, Corporate Securities, Government Securities or Municipal Securities at a private sale without notice because the Collateral is of a type sold on a recognized market or the subject of widely distributed standard price quotations. The Beneficiaries' Representative shall provide the Trustee with an Adverse Determination notice as soon as practicable, although failure to provide such notice shall not affect the rights or obligations of the parties hereunder, except that a Beneficiary shall not take any action with respect to the Trustee as securities intermediary until such notice is provided. Except for the amounts due to the Trustee pursuant to Section 7.3, the Trustee waives any right of set-off, banker's lien or other lien or claim it may have to the Collateral.

Grantor covenants and agrees that it shall not pledge, assign, hypothecate or transfer its interest in the Trust account or the Trust Fund. Grantor further covenants and agrees that it shall not so direct the Trustee, and the Trustee agrees that it will not acknowledge or agree to any such pledge, assignment, hypothecation or transfer.

**ARTICLE 5**  
**RESIGNATION, REMOVAL, OR DEATH OF TRUSTEE**

**5.1 Resignation of Trustee.** The Trustee may resign at any time by filing its written resignation with Grantor and the Beneficiaries' Representative. Such resignation shall take effect sixty (60) days from the date of such filing or upon appointment of a successor pursuant to Section 5.3, whichever shall first occur.

**5.2 Removal of Trustee.** Grantor and the Beneficiaries' Representative may remove the Trustee at any time by delivering to the Trustee a written notice of its removal and the appointment of a successor pursuant to Section 5.3.

### **5.3 Appointment of Successor Trustee.**

5.3.1 Removal of the Trustee and the appointment of a successor Trustee shall take effect sixty (60) days following delivery to the Trustee of (a) an instrument in writing removing the Trustee and appointing such successor, executed by Grantor and accompanied by an instrument in writing signed by the Beneficiaries' Representative certifying the Beneficiaries' Representative's agreement to such removal and appointment, and (b) an acceptance in writing, executed by such successor, both acknowledged in the same form as this Agreement. The Trustee may agree to an earlier effective date. In the event of the merger, sale (of all or substantially all of the Trustee's corporate trust business) or dissolution of the Trustee, a successor trustee shall be appointed by Grantor (which successor trustee may be the acquiring party or successor entity in the case of sale or merger of the Trustee in Grantor's sole discretion) with the approval of the Beneficiaries' Representative, which approval shall not be unreasonably withheld, and a writing to such effect and an acceptance in writing, as referred to above, shall be delivered to the Trustee. In order to qualify to serve as Trustee, any successor trustee must, at a minimum: (i) be authorized under state or federal law to exercise corporate trust powers, (ii) have a combined capital and surplus of at least \$250,000,000, and (iii) be subject to supervision or examination by federal or state authority.

5.3.2 All of the provisions set forth herein with respect to the Trustee shall relate to each successor with the same force and effect as if such successor had been originally named as the Trustee under this Trust.

5.3.3 If a successor is not appointed within sixty (60) days after the Trustee gives notice of its resignation pursuant to Section 4.1, or within sixty (60) days after the Trustee's merger, sale (of all or substantially all of the Trustee's corporate trust business) or dissolution, the Trustee or the Beneficiaries' Representative may apply to any court of competent jurisdiction at the expense of the Trust for appointment of a successor.

**5.4 Transfer of Fund to Successor.** Upon appointment of a successor trustee as set forth above, the Trustee shall transfer and deliver the Trust Fund to such successor with authority to retain only reasonable reserves pending settlement of its final account as provided in Section 7.4.

## **ARTICLE 6 DURATION, TERMINATION, AND AMENDMENT OF TRUST**

### **6.1 Term.**

6.1.1 The term of this Trust shall be for a period extending from the Effective Date until June 30, 2025, unless extended or terminated according to the terms of this Trust. This Trust may be terminated by consent of a majority of the then serving Board of Directors and a majority of the Beneficiaries serving as Officers at the time; *provided, however*, no such termination shall be effective (a) following a Change of Control, or (b) so as to reduce indemnification otherwise available to a Beneficiary of this Trust, specifically including any Beneficiaries who are not at such time current Officers, for any Demand then existing and still



pending or with respect to any later asserted Demand arising out of a Covered Act occurring before the effective date of such termination. Expiration or termination of this Trust shall operate prospectively only, so that all provisions of this Agreement shall remain in full force and effect as to any Demand asserted prior to the effective date of expiration or termination relating to a Covered Act that occurs prior to the effective date of expiration or termination. Grantor and the Beneficiaries' Representative shall notify the Trustee of termination of the Trust by, with respect to Grantor, an instrument in writing executed by Grantor together with a certified copy of the resolution of the Board of Directors authorizing such termination and, with respect to the Beneficiaries' Representative, written evidence of the consent of a majority of the Beneficiaries serving as Officers at the time. Termination by consent of Grantor and majority of the Beneficiaries shall be effective on the later to occur of (i) the Board of Directors resolution and (ii) receipt by the Beneficiaries' Representative of written consents from at least a majority of the Beneficiaries as provided in this Section 6.1.1.

6.1.2 Grantor and the Beneficiaries' Representative (jointly or separately) as applicable shall provide the Trustee and the Beneficiaries and their successors in interest with written notice of expiration at least thirty (30) days prior to the expiration date.

6.1.3 In the event of a proposed termination prior to the expiration of the term of this Trust, Beneficiaries may assert a Demand if, in such Beneficiaries' good faith judgment, there is a reasonable likelihood that following such proposed termination, a Claim will be asserted arising out of a Covered Act that occurred before the effective date of such termination. If so made, such Demand(s) shall be treated as a then existing and still pending Demand hereunder.

**6.2 Distribution Upon Termination.** When this Trust expires or is terminated in accordance with Section 6.1, the Trustee shall distribute the Trust Fund to Grantor less any full and adequate provision or reserves for any distributions to be made pursuant to any outstanding Demands under Sections 4.7 and 6.1.3 and any deductions authorized or required by Section 7.3.

### **6.3 Amendment of Trust Instrument.**

6.3.1 Except in the event of a Change of Control, this Trust may be amended by consent of a majority of the Board of Directors, a majority of the Beneficiaries serving as Executive Officers at the time and the Trustee, *provided, however*, no such amendment shall be effective (a) following a Change of Control, or (b) so as to reduce indemnification or advancement of expenses otherwise available to a Beneficiary of this Trust for any Claim then existing and still pending or with respect to any later asserted Claim arising out of a Covered Act occurring before the effective date of such amendment and *provided further*, that approval of the Trustee shall only be required if the proposed amendment affects in any way the Trustee's rights or duties under this Agreement. If the Trust is amended without the consent of the Trustee as provided above, Grantor shall deliver notice of amendment to the Trustee or its successor in interest thirty (30) days prior to the proposed effective date of the amendment by an instrument in writing executed by Grantor and the Beneficiaries' Representative, together with a certified copy of the resolution of Grantor's Board of Directors authorizing such amendment. Grantor shall send a copy of such notice to each individual Beneficiary or his or her successors in interest.

6.3.2 In the event of a proposed amendment of this Trust, a Beneficiary may assert a Demand if, in such Beneficiary's good faith judgment, there is a reasonable likelihood that following such proposed amendment, a Claim will be asserted arising out of a Covered Act that occurred before the effective date of such amendment and that will be affected by such amendment. If so made, such Demand(s) shall be treated as a then existing and still pending Demand hereunder.

## **ARTICLE 7 RIGHTS AND OBLIGATIONS OF THE TRUSTEE**

**7.1 Duties of Trustee.** The duties and liabilities of the Trustee shall at all times be limited to those expressly stated in this Agreement and no implied duties or covenants shall be read into this Agreement against the Trustee. The Trustee shall discharge its duties hereunder with the care, skill, prudence and diligence under the circumstances then prevailing that a reasonable person acting in a like capacity and familiar with such matters would use in the conduct of an enterprise of a like character and with like aims. The Trustee shall not be liable for any loss sustained by the Trust Fund by reason of the purchase, retention, sale, or exchange or any investment made in good faith and in accordance with Grantor's written directions and the provisions of this Agreement.

**7.2 Indemnification of Trustee.** The Trustee shall not be liable for any action taken or omitted by it in good faith and believed by it to be authorized hereby or within the rights or powers conferred upon it hereunder, or taken or omitted by it in accordance with advice of counsel (which counsel may be of the Trustee's own choosing and which may be house counsel of the Trustee), and shall not be liable for any mistake of fact or error of judgment or for any acts or omissions of any kind unless caused by willful misconduct or gross negligence. Grantor agrees to indemnify the Trustee and its officers, directors, agents and employees and hold it and them harmless against any and all liabilities, losses, claims, expenses (including reasonable attorneys' fees and expenses) and damages incurred by it hereunder, except for liabilities, losses, claims, expenses, and damages incurred by the Trustee resulting from its own willful misconduct or gross negligence. This Section 7.2 shall survive the termination of this Agreement and the earlier removal or resignation of the Trustee.

**7.3 Expenses and Compensation.** The Trustee shall pay from the Trust Fund, to the extent not paid by Grantor, the Trustee's reasonable expenses of administration of the Trust, including reasonable compensation and expenses of counsel (including house counsel) and any agents engaged by the Trustee to assist it in such administration. Grantor shall pay the Trustee reasonable compensation for its services as Trustee hereunder and the Trustee shall have a lien on the Trust Fund for such compensation and expenses until paid.

**7.4 Accounts of Trustees.** The Trustee shall keep full accounts of all of its receipts and disbursements. Its financial statements, books, and records with respect to the Trust Fund shall be open to inspection by Grantor or the Beneficiaries' Representative or their representatives at all reasonable times during business hours of the Trustee and may be audited not more frequently than once in each fiscal year by an independent certified public accountant engaged by the Beneficiaries' Representative. Within ninety (90) days after the close of each fiscal year, or any termination of the duties of the Trustee, the Trustee shall submit in duplicate to Grantor an accounting of its transactions as Trustee hereunder.

**7.5 Rights of Trustee.** None of the provisions of this Agreement shall require the Trustee to expend or risk its own funds or otherwise to incur any liability, financial or otherwise, in the performance of any of its duties hereunder. The Trustee may conclusively rely and shall be fully protected in acting or refraining from acting upon any resolution, certificate, statement, instrument, opinion, report, notice, request, consent, order, approval or other paper or document believed by it to be genuine and to have been signed or presented by the proper party or parties. The Trustee may execute any of the trusts or powers hereunder or perform any duties hereunder either directly or by or through agents, attorneys, custodians or nominees appointed with due care, and shall not be responsible for the negligence or misconduct of any agent, attorney, custodian or nominee so appointed, *provided, however*, the Trustee shall remain responsible for the performance of its obligations hereunder. Anything in this Agreement to the contrary notwithstanding, in no event shall the Trust be liable for special, indirect, punitive or consequential loss or damage of any kind whatsoever (including but not limited to lost profits), even if the Trustee has been advised of the likelihood of such loss or damage and regardless of the form of action. The Trustee shall not be liable for an error in judgment made in good faith by an officer or officers of the Trustee, unless the Trustee was grossly negligent in ascertaining the pertinent facts.

Whenever in the administration of the provisions of this Agreement the Trustee shall deem it necessary or desirable that a matter be proved or established prior to taking or suffering any action to be taken hereunder, such matter (unless other evidence in respect thereof be herein specifically prescribed) may, in the absence of gross negligence or bad faith on the part of the Trustee, be deemed to be conclusively proved and established by a certificate signed by the Beneficiaries' Representative and an officer of Grantor and delivered to the Trustee, and such certificate, in the absence of gross negligence or bad faith on the part of the Trustee, shall be full warrant to the Trustee for any action taken, suffered or omitted by it under the provisions of this Agreement upon the faith thereof. The Trustee shall not be bound to make any investigation into the facts or matters stated in any resolution, certificate, statement, instrument, opinion, report, notice, request, consent, entitlement order, approval or other paper or document.

## **ARTICLE 8 MISCELLANEOUS**

**8.1 Governing Law; Waiver of Jury Trial.** The validity, interpretation, performance and enforcement of this Agreement and the Trust created hereby shall be governed by the laws of the State of Washington, *provided, however*, that the rights, duties, obligations and protections of the Trustee hereunder shall be governed by the laws of the State of California. The parties irrevocably submit to the jurisdiction and venue of any Washington State or United States Federal Court sitting in Seattle, Washington. Any proceeding with respect to this Trust shall be in King County Superior Court unless otherwise consented to by Grantor.

Each party hereto hereby agrees not to elect a trial by jury of any issue triable of right by jury, and waives any right to trial by jury fully to the extent that any such right shall now or hereafter exist with regard to this Agreement, or any claim, counterclaim or other action arising in

connection herewith. This waiver of right to trial by jury is given knowingly and voluntarily by each party, and is intended to encompass individually each instance and each issue as to which the right to a trial by jury would otherwise accrue.

**8.2 Assignment; Successors.** Neither this Agreement nor any rights or benefits hereunder may be assigned (including by operation of law), transferred, pledged or otherwise hypothecated without the prior written consent of the other parties, *provided, however*, that with respect to the merger, sale or dissolution of the Trustee, only the consents required under Section 5.3.1 hereof shall be required. This Agreement and the Trust created hereby shall be binding upon and shall inure to the benefit of the spouses, heirs, personal and legal representatives and estates of the Beneficiaries, and to the permitted assigns of the parties hereto.

**8.3 Third Party Beneficiaries.** The Beneficiaries are specifically acknowledged as third party beneficiaries of this Agreement and shall have the right to bring actions to enforce this Agreement where the Beneficiaries' Representative fails to bring such an action or fails to prosecute an action in good faith following a demand by a Beneficiary to so act.

**8.4 Enforcement Expenses.** Grantor shall be responsible for all costs and expenses, including reasonable attorneys' fees and costs, incurred in any action brought to enforce or interpret this Agreement, whether brought by the Beneficiaries' Representative, a Beneficiary, the Trustee or otherwise, unless the court determines that such Claim for enforcement was not brought in good faith or was frivolous.

**8.5 Titles and Headings Not to Control.** The titles to articles and headings of sections in this Agreement are for convenience of reference only and in case of any conflict the text of this Agreement, rather than any title or heading, shall control.

**8.6 Notices, Consents and Other Communications.** All notices, consents, or other communications required or contemplated by this Agreement shall be in writing and shall be deemed to have been given when delivered by (a) personal delivery, (b) prepaid overnight courier, (c) postage prepaid return receipt requested certified mail, (d) facsimile, or (e) email (however as to the Trustee pursuant and subject to the terms of Section 8.8):

If to a Beneficiary: The last address given to the Trustee by each respective Beneficiary

If to Beneficiaries' Representative: The last address given to the Trustee by the Beneficiaries' Representative

If to Microsoft: Microsoft Corporation  
One Microsoft Way  
Redmond, WA 98052-6399  
Attention: Deputy General Counsel, Corporate  
Telephone No.: (425) 882-8080  
Facsimile No.: (425) 869-1327  
Email: [john.seethoff@microsoft.com](mailto:john.seethoff@microsoft.com)

With a copy to: K&L Gates LLP  
925 Fourth Avenue, Suite 2900  
Seattle, WA 98104-1158  
Attention: Seattle Administrative Partner  
Telephone No.: (206) 623-7580  
Facsimile No.: (206) 623-7022  
Email: [pallavi.wahi@klgates.com](mailto:pallavi.wahi@klgates.com)

If to Trustee: The Bank of New York Mellon Trust Company, N.A.  
400 South Hope Street  
Suite 500  
Los Angeles, CA 90071  
Attention: Robert Cuadra  
Telephone No.: (213) 630-6230  
Facsimile No.: (213) 630-6480  
Email: [RobertJose.Cuadrall@bnymellon.com](mailto:RobertJose.Cuadrall@bnymellon.com)

Notice by personal delivery shall be effective upon the date delivery is made and notice by certified mail or overnight courier shall be effective on the date it is recorded as delivered by the U.S. Postal Service or the overnight courier, respectively. Facsimile notice shall be effective on the date recorded in the sender's equipment as a confirmed transmission to the recipient's facsimile address. Email notice shall be effective on the date sent to a valid address so long as no notice of failure of delivery is received by sender. Each Beneficiary and the Beneficiaries' Representative shall provide Trustee and Grantor with prompt notice of changes of address.

**8.7 Force Majeure.** From the effective date of this Agreement, the Trustee, or any successor in interest, shall not be considered in breach of or in default in its obligations with respect to any obligations created hereunder in the event of an unavoidable delay in the performance of such obligations due to unforeseeable causes beyond its control and without its fault or negligence, including, but not limited to, acts of God, or of the public enemy, acts of a government, acts of the other party, fires, floods, epidemics, quarantine restrictions, strikes, freight embargoes, earthquakes, explosion, mob violence, riot, inability to procure or general sabotage or rationing of labor, equipment, facilities, sources of energy, material or supplies in the open market, malicious mischief, condemnation, and unusually severe weather or delays of suppliers or subcontractors due to such causes or any similar event and/or occurrences beyond the control of the Trustee.

**8.8 Electronic Instruction.** The Trustee agrees to accept and act upon instructions or directions pursuant to this Agreement sent by facsimile transmission, unsecured email or other similar electronic methods, *provided, however,* that Grantor and/or the Beneficiaries' Representative shall provide to the Trustee an incumbency certificate listing persons as may be designated and authorized to sign for Grantor and the Beneficiaries' Representative, which such incumbency certificate shall contain appropriate contact information and shall be amended whenever a person is to be added or deleted from the listing, or there is a change in authorized contact data.

If Grantor or the Beneficiaries' Representative elects to give the Trustee email or facsimile instructions (or instructions by a similar electronic method) and the Trustee in its discretion elects to act upon such instructions, the Trustee's understanding of such instructions shall be deemed controlling. The Trustee shall not be liable for any losses, costs or expenses arising directly or indirectly from the Trustee's reliance upon and compliance with such instructions notwithstanding that such instructions conflict or are inconsistent with a subsequent written instruction. Grantor and the Beneficiaries' Representative agree to assume all risks arising out of the use of such electronic methods to submit instructions and directions to the Trustee, including without limitation the risk of the Trustee acting on unauthorized instructions, and the risk of interception and misuse by third parties.

**8.9 Counterparts.** This Agreement may be executed in two or more counterparts, and by facsimile, and shall be deemed an original and shall bind the signatory but all of which shall be considered one and the same agreement and shall become effective when one or more counterparts have been signed by each of the parties and delivered to the others, it being understood that all parties need not sign the same counterpart.

*[remainder of page intentionally left blank]*

IN WITNESS WHEREOF, the parties hereto have executed this Agreement as of the 30th day of June, 2016.

THE BANK OF NEW YORK MELLON  
TRUST COMPANY, N.A.  
("Trustee")

/S/ R. TARNAS

Name: R. TARNAS  
Title: Vice President

MICROSOFT CORPORATION  
("Grantor")

/S/ JOHN A. SEETHOFF

Name: JOHN A. SEETHOFF  
Title: Vice President and Corporate Secretary

ADDITIONAL PARTY  
("Beneficiaries' Representative")

/S/ CHARLES H. NOSKI

CHARLES H. NOSKI

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**EXHIBIT A**

Grantor shall cause the Trustee to treat the 2009 Trust funds as part of the Minimum Balance under this Agreement to this Trust effective June 30, 2016. Grantor shall transfer as of the effective date of this Agreement an additional sum sufficient to cause the total balance held by the Trustee to equal \$50,000,000 which thereafter shall be the Minimum Balance, and Trustee shall hold such funds in trust for the stated uses and purposes in accordance with the terms of this Agreement.



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## EXHIBIT B

**Liquidation of Investments.** If Trustee receives no instructions from Grantor for the liquidation of assets pursuant to Section 4.6, Trustee shall liquidate the Trust Fund in the following order, liquidating the entire amount of each class of funds before liquidating additional funds from the next class sufficient to make a distribution:

1. Cash
2. Money market funds
3. Other Eligible Securities (Treasury Securities, Government Securities, Municipal Securities, Corporate Securities), in order of nearest maturity

**AMENDED AND RESTATED  
DIRECTORS' INDEMNIFICATION TRUST AGREEMENT**

This AMENDED AND RESTATED DIRECTORS' INDEMNIFICATION TRUST AGREEMENT (this "**Trust**" or this "**Agreement**") between MICROSOFT CORPORATION, a Washington corporation ("**Grantor**"), and The Bank of New York Mellon Trust Company, N.A. the "**Trustee**"), whose address is 400 South Hope Street, Suite 500, Los Angeles, California 90071, and, as an additional party, Charles H. Noski (the "**Beneficiaries' Representative**") shall be effective as of the date of the receipt of the last Beneficiary consent necessary to constitute the consent of a majority of the living Beneficiaries (the "**Effective Date**").

**RECITALS**

- A. Grantor initially established the directors' indemnification trust by an agreement dated as of June 30, 2003 (the "**Original Trust Agreement**") to be a source of indemnification for Grantor's Directors who are eligible for such indemnification as stated in this Trust as it is in effect from time to time.
- B. Grantor and Beneficiaries of this Trust adopted an amendment to the Original Agreement in November 2006, and further amended and restated the Trust in July of 2010 (the "**Amended and Restated 2003 Indemnification Trust Agreement**").
- C. Grantor has determined, after due diligence, that it has and will continue to derive substantial economic benefits from this Trust, including from economic terms that are more favorable to Grantor than obtaining protection for its Directors through the current director insurance market.
- D. Grantor's Articles of Incorporation (the "**Articles**") provide for mandatory indemnification of Grantor's Directors to the maximum extent provided by law, and as such, this Trust is not an exclusive source of indemnification for such Directors.
- E. Grantor has determined that continuation and further amendment of this Trust is necessary in order for Grantor to attract and retain the most qualified persons to serve as Directors.
- F. Grantor and the Beneficiaries under the Amended and Restated 2003 Indemnification Trust Agreement wish to amend certain provisions in that trust agreement and to restate in its entirety the Amended and Restated 2003 Indemnification Trust Agreement and replace it with this amended and restated Agreement. Grantor's Board of Directors has acted by resolution adopted March 15, 2016 to amend and restate the Amended and Restated 2003 Indemnification Trust Agreement effective as of the Effective Date. The terms of the Amended and Restated 2003 Indemnification Trust Agreement shall continue to govern the Trust until the Effective Date.
- G. Except as otherwise noted, the capitalized terms have the meaning ascribed to them in the body of this Agreement.

## AGREEMENT

NOW, THEREFORE, as of the Effective Date, Grantor and the Trustee acknowledge that the funds held under the Amended and Restated 2003 Indemnification Trust Agreement shall be held in trust under this Agreement and the Trustee accepts the trust created hereby and agrees that it will hold all property which it may receive or hold hereunder specifically including the Minimum Balance as defined in Section 4.2 at the Effective Date, together with the additional funds, as custodian IN TRUST, for the purposes and upon the terms and conditions hereinafter stated, and Grantor, the Trustee and the Beneficiaries' Representative agree as follows:

### ARTICLE 1 DEFINITIONS

**"Act"** means the Washington Business Corporation Act RCW 23B or succession legislation.

**"Additional Contributions"** is defined in Section 4.4.

**"Adverse Determination"** is defined in Section 4.12.

**"Agreement"** is defined in the Preamble.

**"Amended and Restated 2003 Indemnification Trust Agreement"** is defined in Section B of the Recitals.

**"Articles"** is defined in Section D of the Recitals.

**"Beneficiary"** and **"Beneficiaries"** are defined in Section 3.1.

**"Beneficiaries' Representative"** is defined in the Preamble.

**"Board of Directors"** means the board of directors of Microsoft Corporation as constituted from time to time.

**"Business Day"** means any day, excluding Saturday, Sunday and any day on which banking institutions located in Los Angeles, California or Seattle, Washington are authorized by applicable law to be closed.

**"Cash"** means (a) currency of the United States, and (b) certificates of deposit or time deposits having, in each case, a tenor of not more than six (6) months, issued by any U.S. commercial bank or any branch or agency of a non-U.S. bank licensed to conduct business in the U.S. having combined capital and surplus of not less than \$250,000,000 (including the Trustee and its affiliates).

**"Change of Control"** is defined in Section 3.1.

**"Claim"** or **"Claims"** includes, without limitation, any threatened, pending, or completed action, suit, or proceeding, whether civil, derivative, criminal, administrative, investigative, or otherwise, initiated by a person other than the Beneficiary (including any Claims by or in the right of Grantor), unless the Claim was initiated by the Beneficiary in good faith to establish or enforce a right to indemnification under the Articles, this Trust or applicable statute.

**"Collateral"** is defined in Section 4.12.

**"Covered Act"** means any act or omission (including, without limitation, any alleged breach of duty, neglect, error, misstatement, misleading statement, or otherwise, or appearing as or preparing to be a witness) by a Beneficiary, and any Claim against such Beneficiary, by reason of the fact that that Beneficiary is or was a director of Grantor, or of any subsidiary or division, or is or was serving at the request of Grantor as a director, officer, partner, trustee, fiduciary, employee or agent of another corporation, partnership, joint venture, trust, employee benefit plan or other enterprise.

**"Corporate Securities"** means US dollar denominated senior debt obligations that are obligations (whether direct or by virtue of guarantees) of corporations organized in the United States whose long-term, unsecured, unsubordinated debt securities are rated at least "A" (or its equivalent successor rating) in the case of Standard & Poor's Ratings Group or "A2" (or its equivalent successor rating) in the case of Moody's Investors Service, Inc.

**"Demand"** is defined in Section 4.7.1.

**"Director"** means a current, past or future member of the Board of Directors.

**"Effective Date"** is defined in the Preamble.

**"Eligible Securities"** means Cash, Treasury Securities, Government Securities, Municipal Securities, Corporate Securities, Money Market Funds and Other Eligible Securities. All Eligible Securities must be in a form suitable for delivery and retransfer, and must be capable of being priced by recognized third-party dealers.

**"Excluded Claim"** means any payment for Losses or Expenses in connection with any Claim the payment of which is Ultimately Determined to be prohibited by the Act, public policy, or other applicable law (including binding regulations and orders of, and undertakings or other commitments with, any governmental entity or agency) as the same exists or may hereafter be amended (but, in the case of any such amendment, only to the extent that such amendment permits Grantor to provide broader indemnification rights than said law permitted Grantor to provide prior to such amendment). For the avoidance of doubt, a **"knowing violation of law"** means a conscious, intentional and deliberate act or failure to act (a) that is a material breach of applicable law, (b) that is done with actual knowledge that such act or failure to act is a material breach of applicable law, (c) that is done with the intent that such act or failure to act will be a material breach of applicable law, (d) that is done with actual knowledge that such act or failure to act will inflict material harm on Grantor, (e) that is done with the intent that such act or failure to act will inflict material harm on Grantor, and (f) that such act or failure to act does inflict such material

harm on Grantor. For the avoidance of doubt, **"intentional misconduct"** means a conscious, intentional and deliberate act or failure to act (a) that is done with actual knowledge that such misconduct will inflict material harm on Grantor, (b) that is done with the intent to inflict material harm on Grantor, and (c) that such misconduct does inflict such material harm on Grantor.

**"Expenses"** means any reasonable expenses incurred by Beneficiary as a result of a Claim or Claims made against him or her for Covered Acts including, without limitation, counsel fees and costs of investigative, judicial, or administrative proceedings and any appeals.

**"Fines"** shall include any fine, penalty or, with respect to an employee benefit plan, any excise tax, or penalty assessed with respect thereto.

**"Government Securities"** means bonds, notes, debentures, obligations or other evidence of indebtedness issued and/or guaranteed by the Federal National Mortgage Association, the Federal Home Loan Mortgage Corporation or the Government National Mortgage Association, including mortgage participation certificates, mortgage pass-through certificates and other mortgage-backed securities, but excluding collateralized mortgage obligations and mortgage-related securities representing payments of interest only or principal only and REMIC securities and CMBS (commercial mortgage backed securities).

**"Grantor"** is defined in the Preamble.

**"Loss"** means any amount which a Beneficiary is legally obligated to pay as a result of any Claim or Claims made against him or her for Covered Acts including, without limitation, Fines, damages, judgments, costs of defense of any Claims and sums paid in settlement of any Claim or Claims, specifically including fees of plaintiff's counsel.

**"Minimum Balance"** is defined in Section 4.2.

**"Money Market Funds"** means money market funds rated "AAAm" or "AAAm-G" by Standard & Poor's Rating Service, including funds for which the Trustee or its affiliates provide investment advisory or other management services.

**"Municipal Securities"** means senior and unsubordinated debt obligations that are obligations (whether direct or by virtue of guarantees) of U.S. state or municipal issuers whose long-term, unsecured, unsubordinated, debt securities are rated at least "A" (or its equivalent successor rating) in the case of Standard & Poor's Ratings Group or "A2" (or its equivalent successor rating) in the case of Moody's Investors Service, Inc., excluding "A" or "A2" rated debt securities of housing and hospital issuers and municipal funds and partnerships where the rating is not based upon the rating of a third-party credit enhancer of such securities.

**"Officer"** means any employee of Grantor elected, designated or appointed by the Board of Directors as an officer at a level "corporate vice president" or higher as of July 1, 2009 and from time to time thereafter.

**"Original Trust Agreement"** is defined in Section A of the Recitals.

**"Other Eligible Securities"** means securities other than Cash, Corporate Securities, Treasury Securities, Government Securities, Money Market Funds and Municipal Securities mutually agreed upon in writing by the Beneficiaries' Representative and Grantor.

**"Treasury Securities"** means securities issued or guaranteed by the United States government, including United States Department of the Treasury obligations and any other obligations the timely payment of principal and interest of which is fully and unconditionally guaranteed by the United States government.

**"Trust"** is defined in the Preamble.

**"Trust Fund"** is defined in Section 4.1.

**"Trustee"** is defined in the Preamble.

**"UCC"** is defined in Section 4.12.3.

**"Ultimate Determination"** means a final order from which there is no further right of appeal in any action in which a Beneficiary seeks indemnification. Such an order shall constitute the Ultimate Determination of the Beneficiary's right to indemnification from Grantor. **"Ultimately Determined"** shall have a correlative meaning.

## **ARTICLE 2 PRIOR COVERED ACTS AND CLAIMS**

**2.1 Indemnification for Covered Acts.** The Beneficiaries under this Trust shall be indemnified for any Losses, Expenses or Fines that result from a Claim based on a Covered Act asserted while this Trust is in effect without regard to whether the Covered Act occurred on, before or after the establishment of this Trust. Rights to coverage as a Beneficiary under this Agreement shall be deemed to vest with and upon such person's election as a Director. If a Beneficiary of this Trust was also a "Beneficiary" of the Original Trust and/or the Amended and Restated 2003 Indemnification Trust Agreement because such person was or is a Director prior to the Effective Date, such person shall be covered by this Trust as a Beneficiary under this Trust as well for "Covered Acts" as defined herein that occurred prior to the Effective Date.

**2.2 Nonexclusive Remedy.** The rights of Beneficiaries to indemnification from this Trust are limited to the assets of the Trust, but this does not limit any Beneficiary's rights, if any, to indemnification (without duplication) from Grantor, or other Grantor arrangements or obligations, including but not limited to any applicable insurance coverage.

**ARTICLE 3  
THE BENEFICIARIES AND THE  
BENEFICIARIES' REPRESENTATIVE**

**3.1 The Beneficiaries.** All present and future Directors and all "Beneficiaries" of the Original Trust Agreement and/or the Amended and Restated 2003 Indemnification Trust Agreement who were "Beneficiaries" of such trusts as Directors shall be "**Beneficiaries**" of this Trust (and each a "**Beneficiary**"), *provided, however*, that if there is a Change in Control of Grantor, no directors elected or appointed after or in connection with such Change in Control shall be entitled to be Beneficiaries who were not Beneficiaries prior to such Change in Control. For purposes of this Agreement, "**Change of Control**" shall mean (a) a tender offer or exchange offer in which the purpose of such offer is to take over and control Grantor and such offer is accepted by owners of securities of Grantor representing 50% or more of the combined voting power of Grantor's then outstanding voting securities, (b) Grantor is merged or consolidated with another corporation and as a result of such merger or consolidation less than 50% of the outstanding voting securities of the surviving or resulting corporation shall then be owned in the aggregate by the former shareholders of Grantor, (c) Grantor transfers substantially all of its assets to another corporation which is not a wholly-owned subsidiary of Grantor, or (d) during any period of twelve (12) consecutive months, individuals who at the beginning of such twelve (12) month period were directors of Grantor cease for any reason to constitute at least a majority of Grantor's Board of Directors. The Beneficiaries' Representative shall promptly notify the Trustee in writing of a Change in Control. Any Beneficiary shall remain a Beneficiary despite his or her resignation, removal, or other failure to continue to be a member of Grantor's Board of Directors during the term of this Agreement. A person whose conduct gives rise to a right of indemnification both as a member of the Board of Directors and as an Officer of Grantor, shall be a Beneficiary hereunder as to all such conduct without being required to separate his or her activities between the role of Director and the role of Officer.

**3.2 New Beneficiaries.** If prior to a Change in Control an individual is duly elected to the Board of Directors, Grantor agrees to notify the Trustee and the Beneficiaries' Representative promptly of such election or appointment; *provided, however*, Grantor's failure to so notify the Trustee and the Beneficiaries' Representative shall not affect in any way an individual Director's rights as a Beneficiary under this Trust. The Trustee and the Beneficiaries' Representative shall have the right to rely on the accuracy and completeness of any statement provided to it by Grantor's Secretary, Assistant Secretary or Chief Executive Officer as to the Beneficiary status of any individual.

**3.3 Beneficiaries' Representative.** Except as expressly provided elsewhere in this Agreement, all communications or demands made by and among the Trustee and the Beneficiaries are to be made through the individual then designated as the Beneficiaries' Representative. The Beneficiaries' Representative shall have the exclusive right to convey Demands from time to time on the Trustee to direct payment to one or more of the Beneficiaries.

**3.4 Identity of Beneficiaries' Representative.** The Beneficiaries' Representative shall be a Beneficiary who is a present or past nonemployee Director of Grantor, designated in writing to the Trustee and Grantor from time to time by a majority of the current nonemployee

Directors who are Beneficiaries under this Agreement. For this purpose, a Director who has not been employed by Grantor during the current calendar year and the preceding three (3) years shall be regarded as a nonemployee Director. The Trustee and Grantor shall be entitled to rely on the original appointment of that individual as the Beneficiaries' Representative unless notified in writing of a change in the Beneficiaries' Representative by a writing signed by the former Beneficiaries' Representative. A Beneficiary shall be deemed to have consented to such change in Beneficiaries' Representative if such Beneficiary is provided with notice of such change in accordance with Section 8.6 and does not provide written notice of objection to the change within ten (10) days. The Trustee shall be entitled to rely on such subsequent appointment as of the date the writing is received by the Trustee. The Trustee shall be entitled to rely on the accuracy and completeness of a written list delivered to the Trustee by Grantor, and certified by the Secretary of Grantor to be accurate and to have been prepared in good faith, identifying the individuals who constitute the present nonemployee Directors who are Beneficiaries under this Agreement. In the absence of an effective appointment of a Beneficiaries' Representative, the Trustee or any Beneficiary may, after ten (10) days' written notice to all Beneficiaries and Grantor, petition a court of competent jurisdiction at the expense of the Trust for appointment of a Beneficiaries' Representative who need not be a Beneficiary (if none are willing or able to serve), but shall in no event be an Officer or Director elected or appointed after a Change in Control who was not a Beneficiary prior to such Change in Control. The designation or appointment of a successor Beneficiaries' Representative shall become effective only upon the execution of a counterpart of this Agreement whereby the successor Beneficiaries' Representative shall assume and become bound by all the duties and responsibilities of a Beneficiaries' Representative under this Agreement.

**3.5 Right of Beneficiaries to Receive Payments.** Subject to court order to the contrary, the rights of the Beneficiaries to make a Demand and receive distributions from the Trustee shall not be affected or diminished in any way by the existence of any dispute between one or more Beneficiaries and Grantor or anyone acting on behalf of Grantor in a derivative or representative capacity, and the Trustee in making distributions from the Trust Fund shall be entitled to rely upon the simple Demand of a Beneficiary, as conveyed by the Beneficiaries' Representative pursuant to Section 4.7. Such distributions shall be made notwithstanding any notice or demand by or on behalf of Grantor or anyone acting on behalf of Grantor in a derivative or representative capacity that the distributions should not be made, whether based on Grantor's claim that any Beneficiary is not entitled to some or all of the amount of such distributions or otherwise. The Trustee shall have no responsibility or liability to Grantor for making any payment despite having received any such notice or demand by or on behalf of Grantor. The Trustee shall have no responsibility to inquire into the accuracy or truthfulness of any such notice or demand, whether from Grantor or the Beneficiaries' Representative.

#### **ARTICLE 4 THE TRUST FUND**

**4.1 Trust Fund; Grantor Trust.** The Trustee shall hold all property received by it as custodian in Trust hereunder as one fund which, together with the income and gains therefrom and additions thereto, shall constitute the "**Trust Fund**." The Trust is intended to be a grantor trust within the meaning of Section 671 of the Internal Revenue Code of 1986, as amended, and shall be



construed accordingly. The Trust Fund shall not be paid to Grantor or any trustee in bankruptcy of Grantor, shall be held separate and apart from other funds of Grantor, and shall be used exclusively for the purposes set forth herein.

**4.2 Minimum Balance.** The Trustee shall continue to hold the amount in the Trust Fund immediately prior to the date of execution of this Agreement as part of the Minimum Balance under this Agreement. Grantor shall transfer as of the effective date of this Agreement an additional sum sufficient to cause the total balance held by the Trustee to equal \$50,000,000 which thereafter shall be the "**Minimum Balance**," to be held in trust, for the stated uses and purposes in accordance with the terms of this Agreement. Nothing contained herein shall preclude Grantor from making additional transfers of funds from time to time to the Trustee, whether required under the terms of this Agreement or not, to be held in trust as part of the Trust Fund. If Grantor makes additional transfers of funds to the Trust Fund, such additional transfers shall be deemed an increase of the Minimum Balance and **Exhibit A** shall be automatically amended without further action by the parties to this Agreement. Grantor and the Beneficiaries' Representative shall periodically, but no less than every third anniversary of this Agreement, review the adequacy of the Minimum Balance.

**4.3 Maintenance of Minimum Balance.** The Trustee agrees to provide monthly reports to Grantor and the Beneficiaries' Representative showing the current fair market value of the Trust Fund. If any such report shows that the current fair market value of the Trust Fund is less than the Minimum Balance, then within ten (10) days after such report, Grantor agrees to deliver cash funds to the Trustee equal to the difference between the fair market value of the Trust Fund and the Minimum Balance so that the Trust balance is at least equal to the Minimum Balance. Notwithstanding the foregoing, Grantor shall have no obligation to make payments to the Trustee in excess of \$400,000,000 (including the Minimum Balance at the Effective Date and the additional funds contributed following execution of this Agreement) under or with respect to this Agreement.

**4.4 Additional Contributions.** Subject to the aggregate limitation of \$400,000,000 set forth in Section 4.3, Grantor agrees to make additional contributions ("**Additional Contributions**") to the Trust Fund within ten (10) days after receipt of a written request from the Beneficiaries' Representative certifying in good faith that Claims have or are reasonably expected to be asserted against Beneficiaries and that estimated Losses and Expenses for all pending, threatened or anticipated Claims against all Beneficiaries are reasonably expected to exceed the then Trust Fund balance. A copy of the written certification shall be provided to the Trustee at the same time and in the same manner as it is provided to Grantor. The written certification shall be accompanied by an opinion of independent counsel to the effect that, based on the information made known to such counsel, (a) the Claims do not appear to be Excluded Claims and (b) the amount requested seems reasonable in the circumstances noted above. Independent counsel shall be selected by the Beneficiaries' Representative and shall have no present or past professional relationship to the Beneficiaries who are the subject of the Claims.

**4.5 Excess Balance.** If at any time the fair market value of the Trust Fund shall exceed the Minimum Balance, plus any additional contributions which continue to be required pursuant to Section 4.4, Grantor shall be entitled to withdraw an amount equal to the excess over the said sum upon thirty (30) days' advance written notice to the Beneficiaries' Representative.

**4.6 Direction of Investment.** Notwithstanding anything contained in this Agreement to the contrary, Grantor retains the right to direct the investment of the Trust Fund and the Trustee shall have no duty to review or recommend investments; *provided, however*, that Grantor shall only direct the Trustee to invest the Trust Fund in Eligible Securities in accordance with Grantor's current cash-management policies. If Grantor instructs the Trustee to invest in securities other than in Cash, Government Securities, Municipal Securities, Corporate Securities, Money Market Funds or Treasury Securities, such instruction shall be accompanied by the written consent of the Beneficiaries' Representative as to the investment(s) in such Other Eligible Securities. If for any reason Grantor shall fail to direct the Trustee pursuant to written instructions as to how to invest the Trust Fund (including the consent of the Beneficiaries' Representative if the proposed investment is in other than Eligible Securities), the Trustee shall invest the Trust Fund in accordance with the last instruction received. In the event the Trustee is required to make a distribution pursuant to Section 4.7 at a time when the Trust Fund has insufficient cash to cover such distribution, the Trustee shall promptly notify the Grantor. The Grantor shall then direct the Trustee as to which Trust investments to liquidate in order to cover the required distribution; if Grantor does not respond to the Trustee's inquiry within two (2) Business Days the Trustee shall liquidate investments in the order specified in **Exhibit B**. The Trustee may purchase or sell to itself or any affiliate, as principal or agent, investments authorized by this Agreement. Grantor and the Beneficiaries' Representative acknowledge that regulations of the Comptroller of the Currency grant the right to receive brokerage confirmations of the security transactions as they occur, at no additional cost. To the extent permitted by law, Grantor and the Beneficiaries' Representative specifically waive compliance with 12 CFR 12 and hereby notify the Trustee that no brokerage confirmations need be sent relating to the security transactions as they occur.

#### **4.7 Distributions from Trust Fund.**

**4.7.1 Duties of Beneficiary.** A Beneficiary making a demand for indemnity shall certify in each demand regarding a Claim for a Covered Act (a "**Demand**") delivered to the Beneficiaries' Representative that (a) he or she is entitled to payment of at least the amount demanded, (b) no part of the Demand is an Excluded Claim or is precluded by the Act or applicable successor statute, (c) the Beneficiary will repay to the Trust any amounts paid or applied to or for the use of such Beneficiary in the event of an Ultimate Determination that such payments are Excluded Claims or precluded by the Act, or in the event the Beneficiary receives payment for the same Claim from another source, (d) a request to Grantor for indemnification has remained unsatisfied for twenty (20) days and that no part of the amount then being demanded from the Trust Fund has previously been received from Grantor, and (e) he or she has complied with any applicable requirements of Grantor's Articles and policy with respect to indemnification, if any, with respect to the Demand.

**4.7.2 Duties of Beneficiaries' Representative.** The Beneficiaries' Representative shall convey a Beneficiary's Demand to the Trustee. Along with the conveyance of such Demand to the Trustee, the Beneficiaries' Representative shall submit, in a writing signed by the Beneficiaries' Representative, a statement (a) that the Demand is being made pursuant to the Articles and this Agreement, as each such may be amended or restated from time to time, provided that any such amendment shall be given effect under this Agreement only to the extent that the amendment provides broader indemnification rights than existed prior to such amendment, (b) that the Demand is for satisfaction of indemnification obligations, (c) that the Demand is being made by a Beneficiary, (d) that specifies the amounts being demanded by the Beneficiary, and (e) that he or she is not aware of any facts or conditions that would make indemnification pursuant to this Agreement invalid, *provided, however*, that the Beneficiaries' Representative has no duty to independently investigate the validity of a Demand.

**4.7.3 Duties of Trustee.** The Trustee shall deliver a copy of each Demand to Grantor as promptly as reasonably possible. A copy of the Beneficiaries' Representative's statement also shall be delivered to Grantor. As soon as practicable after any such Demand is conveyed by the Beneficiaries' Representative, subject to the provisions of Section 3.5, the Trustee shall distribute funds to the Beneficiary specified in such Demand in the amount and manner set forth therein. If the Trustee does not have sufficient funds to satisfy all pending Demands of Beneficiaries in full, the Trustee shall make all reasonable efforts to make pro rata payments, less any amounts due the Trustee, to the Beneficiaries as specified by the Beneficiaries' Representative. If and to the extent the Trust Fund is replenished, the Trustee shall continue to make pro rata distributions, less any amounts due the Trustee, until the Demand is satisfied or to satisfy subsequent Demands.

**4.8 Taxes.** Grantor agrees to pay any and all taxes on the Trust Fund or the income thereof which the Beneficiaries or the Trustee otherwise would be required to pay with respect to the interest of any person or persons therein, and to provide the Trustee and the Beneficiaries' Representative with proof of payment. This does not include any taxes payable upon an indemnification payment distribution from the Trust if the same would be taxable to the recipient Beneficiary under applicable law.

**4.9 Duties and Responsibilities of Beneficiaries' Representative.** The Beneficiaries' Representative (and any successor Beneficiaries' Representative) shall have the following affirmative duties and responsibilities:

4.9.1 To demand deposits from Grantor so as to maintain the Minimum Balance of the Trust in accordance with Section 3.3 and any Additional Contributions required by Section 3.4;

4.9.2 To demand payment by the Trustee to a Beneficiary who has made a Demand and who, in the good faith judgment of the Beneficiaries' Representative, has satisfied the conditions for indemnification as set forth in this Agreement and the Articles, *provided, however*, that the Beneficiaries' Representative has no duty to independently investigate the validity of a Demand; and

4.9.3 To use commercially reasonable efforts to cause Grantor and the Trustee to discharge their respective responsibilities under this Agreement and the responsibilities of Grantor under the Articles, including the bringing of legal actions and proceedings to enforce such agreement.

**4.10 Investment Powers of the Trustee.** Subject to Grantor's rights pursuant to Section 4.6 to direct investment of the Trust Fund, the Trustee shall have those powers provided under Washington law with respect to any property at any time held by it and constituting part of the Trust Fund.

**4.11 Administrative Powers of Trustee.** Subject to Grantor's right pursuant to Section 4.6 to direct investment of the Trust Fund in Eligible Securities, the Trustee shall have the power to do any of the following:

4.11.1 To cause any investment to be registered and held in the name of one or more of its nominees, or one or more nominees of any system for the central handling of securities, without increase or decrease of liability;

4.11.2 To collect and receive any and all money and other property due to the Trust Fund and to give full discharge therefor;

4.11.3 To hold uninvested, without liability for interest thereon, such monies received by the Trustee as the Trustee considers necessary to meet anticipated and imminent disbursements.

**4.12 Adverse Determination.** In the event the trust arrangement created hereby is deemed to be invalid or ineffective as a trust by a court of competent jurisdiction, whether in connection with the bankruptcy of one of the parties hereto or otherwise (an "**Adverse Determination**"), then the parties agree that the nature of their relationship shall be Grantor as debtor, the Trustee as securities intermediary and the Beneficiaries' Representative as secured party for the benefit of the Beneficiaries. To that end, and to secure the obligation of Grantor to indemnify Beneficiaries, Grantor hereby grants the Beneficiaries' Representative for the benefit of the Beneficiaries a continuing security interest in, and pledges all rights, title and interest in and to, the following (for purposes of this Section 4.12, the "**Collateral**"):

4.12.1 The Trust account and the Trust Fund, and any certificates or instruments representing or evidencing the Trust Fund, and all cash, investment property, interest, dividends, rights and other property at any time and from time to time received, receivable or otherwise issued, distributed or distributable in respect of or in exchange for any or all of the Trust Fund;

4.12.2 All other investment property and other property hereafter issued, delivered or deliverable to Trustee in substitution for or in addition to any of the foregoing, all certificates and instruments representing or evidencing such other property and all cash, investment property, interest, dividends, rights and other property at any time and from time to time received, receivable or otherwise issued, distributed or distributable after the date hereof in respect of or in exchange for any or all thereof; and

4.12.3 All proceeds of all of the foregoing.

Grantor and, at the direction of the Beneficiaries' Representative, the Trustee shall execute such other documents and instruments as the Beneficiaries' Representative reasonably may require from time to time to perfect and protect the first priority security interest of the Beneficiaries' Representative on behalf of the Beneficiaries in the Collateral. In the event of an Adverse Determination, the Beneficiaries' Representative shall have and shall be deemed to have had all the rights and remedies of a secured party under Article 9 of the Uniform Commercial Code ("**UCC**") and may exercise any of the rights and remedies available to the Beneficiaries' Representative under the UCC as in effect from time to time in the State of Washington or otherwise available to the Beneficiaries' Representative, including, without limitation, sale, assignment or other disposal of the Collateral in exchange for cash or credit. Grantor agrees that a Demand is also a notice of disposition under Section 9-611 of the UCC and that five (5) Business Days is reasonable notice if notice of a disposition is required under Section 9-611 of the UCC. Furthermore, Grantor agrees that any Beneficiary may be the purchaser of the Collateral consisting of Cash, Corporate Securities, Government Securities or Municipal Securities at a private sale without notice because the Collateral is of a type sold on a recognized market or the subject of widely distributed standard price quotations. The Beneficiaries' Representative shall provide the Trustee with an Adverse Determination notice as soon as practicable, although failure to provide such notice shall not affect the rights or obligations of the parties to this Trust, except that a Beneficiary shall not take any action with respect to the Trustee as securities intermediary until such notice is provided. Except for the amounts due to the Trustee pursuant to Section 7.3, the Trustee waives any right of set-off, banker's lien or other lien or claim it may have to the Collateral.

Grantor covenants and agrees that it shall not pledge, assign, hypothecate or transfer its interest in the Trust account or the Trust Fund. Grantor further covenants and agrees that it shall not so direct the Trustee, and the Trustee agrees that it will not acknowledge or agree to any such pledge, assignment, hypothecation or transfer.

**ARTICLE 5**  
**RESIGNATION, REMOVAL, OR DEATH OF TRUSTEE**

**5.1 Resignation of Trustee.** The Trustee may resign at any time by delivering its written resignation to Grantor and the Beneficiaries' Representative. Such resignation shall take effect sixty (60) days from the date of delivery or upon appointment of a successor pursuant to Section 5.3, whichever shall first occur.

**5.2 Removal of Trustee.** Grantor and the Beneficiaries' Representative may remove the Trustee at any time by delivering to the Trustee a written notice of its removal and the appointment of a successor pursuant to Section 5.3.

### 5.3 Appointment of Successor Trustee.

5.3.1 Removal of the Trustee and the appointment of a successor Trustee shall take effect sixty (60) days following delivery to the Trustee of (a) an instrument in writing removing the Trustee and appointing such successor, executed by Grantor and accompanied by an instrument in writing signed by the Beneficiaries' Representative certifying that a majority of the current non-employee Directors who are Beneficiaries agree to such removal and appointment, and (b) an acceptance in writing, executed by such successor, both acknowledged in the same form as this Agreement. The Trustee may agree to an earlier effective date. In the event of the merger, sale or dissolution of the Trustee, a successor trustee shall be appointed by Grantor (which successor trustee may be in Grantor's sole discretion the acquiring party or successor entity in the case of sale or merger of the Trustee) with the approval of the Beneficiaries' Representative, which approval shall not be unreasonably withheld, and a writing to such effect and an acceptance in writing, as referred to above, shall be delivered to the Trustee. In order to qualify to serve as Trustee, any successor trustee must, at a minimum: (i) be authorized under state or federal law to exercise corporate trust powers, (ii) have a combined capital and surplus of at least \$250,000,000, and (iii) be subject to supervision or examination by federal or state authority.

5.3.2 All of the provisions set forth herein with respect to the Trustee shall relate to each successor with the same force and effect as if such successor had been originally named as the Trustee under this Trust.

5.3.3 If a successor is not appointed within sixty (60) days after the Trustee gives notice of its resignation pursuant to Section 4.1, or within sixty (60) days after the Trustee's death or dissolution, the Trustee or the Beneficiaries' Representative may apply to any court of competent jurisdiction at the expense of the Trust for appointment of a successor.

**5.4 Transfer of Fund to Successor.** Upon appointment of a successor trustee as set forth above, the Trustee shall transfer and deliver the Trust Fund to such successor with authority to retain only reasonable reserves pending settlement of its final account as provided in Section 7.4.

## ARTICLE 6 DURATION, TERMINATION, AND AMENDMENT OF TRUST

### 6.1 Term.

6.1.1 The term of this Trust shall be for a period extending from the effective date of the Original Trust Agreement until June 30, 2025, unless extended or terminated according to the terms of this Trust. This Trust may be terminated by consent of a majority of the Board of Directors and a majority of the then living Beneficiaries; *provided, however*, no such termination shall be effective (a) following a Change of Control, or (b) so as to reduce indemnification otherwise available to a Beneficiary of this Trust for any Demand then existing and still pending or with respect to any later asserted Demand arising out of a Covered Act occurring before the effective date of such termination. Expiration or termination of this Trust shall operate prospectively only, so that all provisions of this Agreement shall remain in full force and effect as

to any Demand asserted prior to the effective date of expiration or termination relating to a Covered Act that occurs prior to the effective date of expiration or termination. Grantor and the Beneficiaries' Representative shall notify the Trustee of termination of the Trust by, with respect to Grantor, an instrument in writing executed by Grantor together with a certified copy of the resolution of the Board of Directors authorizing such termination and, with respect to the Beneficiaries' Representative, written evidence of the consent of a majority of the then living Beneficiaries. Termination by consent of Grantor and majority of the then living Beneficiaries shall be effective on the later to occur of (i) Grantor's board resolution and (ii) receipt by the Beneficiaries' Representative of written consents from a majority of the then living Beneficiaries.

6.1.2 Grantor and the Beneficiaries' Representative (jointly or separately) as applicable shall provide the Trustee and the Beneficiaries and their successors in interest with written notice of expiration at least thirty (30) days prior to the expiration date.

6.1.3 In the event of a proposed termination prior to the expiration of the term of this Trust, Beneficiaries may assert a Demand if, in such Beneficiaries' good faith judgment, there is a reasonable likelihood that following such proposed termination, a Claim will be asserted arising out of a Covered Act that occurred before the effective date of such termination. If so made, such Demand(s) shall be treated as a then existing and still pending Demand hereunder.

**6.2 Distribution Upon Termination.** When this Trust expires or is terminated in accordance with Section 6.1, the Trustee shall distribute the Trust Fund to Grantor less any full and adequate provision or reserves for any distributions to be made pursuant to any outstanding Demands under Sections 4.7 and 6.1.3 and any deductions authorized or required by Section 7.3.

**6.3 Amendment of Trust Instrument.**

6.3.1 Except in the event of a Change of Control, this Trust may be amended by consent of a majority of the then current Board of Directors and the Trustee, *provided, however*, no such amendment shall be effective (a) following a Change of Control, or (b) so as to reduce indemnification or advancement of expenses otherwise available to a Beneficiary of this Trust for any Claim then existing and still pending or with respect to any later asserted Claim arising out of a Covered Act occurring before the effective date of such amendment and *provided further*, that approval of the Trustee shall only be required if the proposed amendment affects in any way the Trustee's rights or duties under this Agreement. If the Trust is amended without the consent of the Trustee as permitted above, Grantor shall deliver notice of amendment to the Trustee or its successor in interest thirty (30) days prior to the proposed effective date of the amendment by an instrument in writing executed by Grantor and the Beneficiaries' Representative, together with a certified copy of the resolution of Grantor's Board of Directors authorizing such amendment. Grantor shall send a copy of such notice to each individual Beneficiary or his or her successors in interest.

6.3.2 In the event of a proposed amendment of this Trust, a Beneficiary may assert a Demand if, in the Beneficiary's good faith judgment, there is a reasonable likelihood that following such proposed amendment, a Claim will be asserted arising out of a Covered Act that occurred before the effective date of such amendment and that will be affected by such amendment. If so made, such Demand(s) shall be treated as a then existing and still pending Demand hereunder.

**ARTICLE 7  
RIGHTS AND OBLIGATIONS OF THE TRUSTEE**

**7.1 Duties of Trustee.** The duties and liabilities of the Trustee shall at all times be limited to those expressly stated in this Agreement. The Trustee shall discharge its duties hereunder with the care, skill, prudence and diligence under the circumstances then prevailing that a prudent person acting in a like capacity and familiar with such matters would use in the conduct of an enterprise of a like character and with like aims. The Trustee shall not be liable for any loss sustained by the Trust Fund by reason of the purchase, retention, sale, or exchange or any investment made in good faith and in accordance with Grantor's written directions and the provisions of this Agreement.

**7.2 Indemnification of Trustee.** The Trustee shall not be liable for any action taken or omitted by it in good faith and believed by it to be authorized hereby or within the rights or powers conferred upon it hereunder, or taken or omitted by it in accordance with advice of counsel (which counsel may be of the Trustee's own choosing and which may be house counsel of the Trustee), and shall not be liable for any mistake of fact or error of judgment or for any acts or omissions of any kind unless caused by willful misconduct or gross negligence. Grantor agrees to indemnify the Trustee and hold it harmless against any and all liabilities, losses, claims, expenses (including reasonable attorneys' fees) and damages incurred by it hereunder, except for liabilities, losses, claims, expenses, and damages incurred by the Trustee resulting from its own willful misconduct or gross negligence.

**7.3 Expenses and Compensation.** The Trustee shall pay from the Trust Fund, to the extent not paid by Grantor, the Trustee's reasonable expenses of administration of the Trust, including reasonable compensation of counsel (including house counsel) and any agents engaged by the Trustee to assist it in such administration. Grantor shall pay the Trustee reasonable compensation for its services as Trustee hereunder and the Trustee shall have a lien on the Trust Fund for such compensation and expenses until paid.

**7.4 Accounts of Trustees.** The Trustee shall keep full accounts of all of its receipts and disbursements. Its financial statements, books, and records with respect to the Trust Fund shall be open to inspection by Grantor or the Beneficiaries' Representative or their representatives at all reasonable times during business hours of the Trustee and may be audited not more frequently than once in each fiscal year by an independent certified public accountant engaged by the Beneficiaries' Representative. Within ninety (90) days after the close of each fiscal year, or any termination of the duties of the Trustee, the Trustee shall prepare, sign and submit in duplicate to Grantor an account of its acts and transactions as Trustee under this Trust.

**7.5 Rights of Trustee.** None of the provisions of this Agreement shall require the Trustee to expend or risk its own funds or otherwise to incur any liability, financial or otherwise, in the performance of any of its duties hereunder. The Trustee may conclusively rely and shall be fully protected in acting or refraining from acting upon any resolution, certificate, statement,



instrument, opinion, report, notice, request, consent, order, approval or other paper or document believed by it to be genuine and to have been signed or presented by the proper party or parties. The Trustee may execute any of the trusts or powers hereunder or perform any duties hereunder either directly or by or through agents, attorneys, custodians or nominees appointed with due care, and shall not be responsible for the negligence or misconduct of any agent, attorney, custodian or nominee so appointed, *provided, however*, the Trustee shall be responsible for the performance of its obligations hereunder. Anything in this Agreement to the contrary notwithstanding, in no event shall the Trust be liable for special, indirect, punitive or consequential loss or damage of any kind whatsoever (including but not limited lost profits), even if the Trustee has been advised of the likelihood of such loss or damage and regardless of the form of action. The Trustee shall not be liable for an error in judgment made in good faith by an officer or officers of the Trustee, unless the Trustee was grossly negligent in ascertaining the pertinent facts.

Whenever in the administration of the provisions of this Agreement the Trustee shall deem it necessary or desirable that a matter be proved or established prior to taking or suffering any action to be taken hereunder, such matter (unless other evidence in respect thereof be herein specifically prescribed) may, in the absence of gross negligence or bad faith on the part of the Trustee, be deemed to be conclusively proved and established by a certificate signed by the Beneficiaries' Representative and an officer of Grantor and delivered to the Trustee, and such certificate, in the absence of gross negligence or bad faith on the party of the Trustee, shall be full warrant to the Trustee for any action taken, suffered or omitted by it under the provisions of this Agreement upon the faith thereof. The Trustee shall not be bound to make any investigation into the facts or matters stated in any resolution, certificate, statement, instrument, opinion, report, notice, request, consent, entitlement order, approval or other paper or document.

**ARTICLE 8  
MISCELLANEOUS**

**8.1 Governing Law.** The validity, interpretation, performance, and enforcement of this Agreement and the Trust created hereby shall be governed by the laws of the State of Washington, *provided, however*, that the rights, duties, obligations and protections of the Trustee hereunder shall be governed by the laws of the State of California. The parties irrevocably submit to the jurisdiction and venue of any Washington State or United States Federal Court sitting in Seattle, Washington. Any proceeding with respect to this Trust shall be in King County Superior Court unless otherwise consented to by Grantor.

Each party hereto hereby agrees not to elect a trial by jury of any issue triable of right by jury, and waives any right to trial by jury fully to the extent that any such right shall now or hereafter exist with regard to this Agreement, or any claim, counterclaim or other action arising in connection herewith. This waiver of right to trial by jury is given knowingly and voluntarily by each party, and is intended to encompass individually each instance and each issue as to which the right to a trial by jury would otherwise accrue.

**8.2 Assignment; Successors.** Neither this Agreement nor any rights or benefits hereunder may be assigned, transferred or pledged without the prior written consent of the other parties, *provided, however*, in the event of a sale, dissolution or merger of the Trustee, only such

consents to such event as set forth in Section 5.3.1 hereof shall be required. This Agreement and the Trust created hereby shall be binding upon and shall inure to the benefit of the spouses, heirs, and personal and legal representatives, estates of the Beneficiaries, and to the permitted assigns of the parties to this Trust.

**8.3 Third Party Beneficiaries.** The Beneficiaries are specifically acknowledged as third party beneficiaries of this Agreement and shall have the right to bring actions to enforce this Agreement where the Beneficiaries' Representative fails to bring such an action or fails to prosecute an action in good faith.

**8.4 Enforcement Expenses.** Grantor shall be responsible for all costs and expenses, including reasonable attorneys' fees and costs, incurred in any action brought to enforce or interpret this Agreement, whether brought by the Beneficiaries' Representative, a Beneficiary, the Trustee, or otherwise, unless the court determines that such Claim for enforcement was not brought in good faith or was frivolous.

**8.5 Titles and Headings Not to Control.** The titles to articles and headings of sections in this Agreement are for convenience of reference only and in case of any conflict the text of this Agreement, rather than any title or heading, shall control.

**8.6 Notices, Consents and Other Communications.** All notices, consents, or other communications required or contemplated by this Agreement shall be in writing and shall be deemed to have been given when delivered by (a) personal delivery, (b) prepaid overnight courier, (c) postage prepaid return receipt requested certified mail, (d) facsimile, or (e) email:

If to a Beneficiary: The last address given to the Trustee by each respective Beneficiary

If to Beneficiaries' Representative: The last address given to the Trustee by the Beneficiaries' Representative

If to Microsoft: Microsoft Corporation  
One Microsoft Way  
Redmond, WA 98052-6399  
Attention: Deputy General Counsel, Corporate  
Telephone No.: (425) 882-8080  
Facsimile No.: (425) 869-1327  
Email: *john.seethoff@microsoft.com*

With a copy to: K&L Gates LLP  
925 Fourth Avenue, Suite 2900  
Seattle, WA 98104-1158  
Attention: Seattle Administrative Partner  
Telephone No.: (206) 623-7580  
Facsimile No.: (206) 623-7022  
Email: *pallavi.wahi@klgates.com*

If to Trustee: The Bank of New York Mellon Trust Company, N.A.  
400 South Hope Street  
Suite 500  
Los Angeles, CA 90071  
Attention: Robert Cuadra  
Telephone No.: (213) 630-6230  
Facsimile No.: (213) 630-6480  
Email: [RobertJose.Cuadrall@bnymellon.com](mailto:RobertJose.Cuadrall@bnymellon.com)

Notice by personal delivery shall be effective upon the date delivery is made and notice by certified mail or overnight courier shall be effective on the date it is recorded as delivered by the U.S. Postal Service or the overnight courier, respectively. Facsimile notice shall be effective on the date recorded in the sender's equipment as a confirmed transmission to the recipient's facsimile address. Email notice shall be effective on the date sent to a valid address so long as no notice of failure of delivery is received by sender. Each Beneficiary and the Beneficiaries' Representative shall provide Trustee and Grantor with prompt notice of changes of address.

**8.7 Force Majeure.** From the effective date of this Agreement, the Trustee, or any successor in interest, shall not be considered in breach of or in default in its obligations with respect to any obligations created hereunder in the event of an unavoidable delay in the performance of such obligations due to unforeseeable causes beyond its control and without its fault or negligence, including, but not limited to, acts of God, or of the public enemy, acts of a government, acts of the other party, fires, floods, epidemics, quarantine restrictions, strikes, freight embargoes, earthquakes, explosion, mob violence, riot, inability to procure or general sabotage or rationing of labor, equipment, facilities, sources of energy, material or supplies in the open market, malicious mischief, condemnation, and unusually severe weather or delays of suppliers or subcontractors due to such causes or any similar event and/or occurrences beyond the control of the Trustee.

**8.8 Electronic Instruction.** The Trustee agrees to accept and act upon facsimile transmission, unsecured email or other similar electronic methods of written instructions and/or directions pursuant to this Agreement, *provided, however,* that Grantor and/or the Beneficiaries' Representative shall provide to the Trustee an incumbency certificate listing persons as may be designated and authorized to sign for Grantor and the Beneficiaries' Representative, which such incumbency certificate shall contain appropriate contact information and shall be amended whenever a person is to be added or deleted from the listing, or there is a change in authorized contact data.

If Grantor or the Beneficiaries' Representative elects to give the Trustee email or facsimile instructions (or instructions by a similar electronic method) and the Trustee in its discretion elects to act upon such instructions, the Trustee's understanding of such instructions shall be deemed controlling. The Trustee shall not be liable for any losses, costs or expenses arising directly or indirectly from the Trustee's reliance upon and compliance with such instructions notwithstanding that such instructions conflict or are inconsistent with a subsequent written instruction. Grantor and the Beneficiaries' Representative agree to assume all risks arising out of the use of such

electronic methods to submit instructions and directions to the Trustee, including without limitation the risk of the Trustee acting on unauthorized instructions, and the risk of interception and misuse by third parties.

**8.9 Counterparts.** This Agreement may be executed in two or more counterparts, and by facsimile, and shall be deemed an original and shall bind the signatory but all of which shall be considered one and the same agreement and shall become effective when one or more counterparts have been signed by each of the parties and delivered to the others, it being understood that all parties need not sign the same counterpart.

*[remainder of page intentionally left blank]*

IN WITNESS WHEREOF, the parties hereto have executed this Agreement as of the 30th day of June, 2016.

THE BANK OF NEW YORK MELLON  
TRUST COMPANY, N.A.  
("Trustee")

/S/ R TARNAS

Name: R. TARNAS  
Title: Vice President

MICROSOFT CORPORATION  
("Grantor")

/S/ JOHN A. SEETHOFF

Name: JOHN A. SEETHOFF  
Title: Vice President and Corporate Secretary

ADDITIONAL PARTY  
("Beneficiaries' Representative")

/S/ CHARLES H. NOSKI

CHARLES H. NOSKI

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**EXHIBIT A**

The Trustee shall continue to hold the amount in the Trust Fund immediately prior to the date of execution of this Agreement as part of the Minimum Balance under this Agreement. Grantor shall transfer as of the effective date of this Agreement an additional sum sufficient to cause the total balance held by the Trustee to equal \$50,000,000 which thereafter shall be the Minimum Balance, to be held in trust, for the stated uses and purposes in accordance with the terms of this Agreement.

## EXHIBIT B

**Liquidation of Investments.** If Trustee receives no instructions from Grantor for the liquidation of assets pursuant to Section 4.6, Trustee shall liquidate the Trust Fund in the following order, liquidating the entire amount of each class of funds before liquidating additional funds from the next class sufficient to make a distribution:

1. Cash
2. Money market funds
3. Other Eligible Securities (Treasury Securities, Government Securities, Municipal Securities, Corporate Securities), in order of nearest maturity

**MICROSOFT CORPORATION  
EXECUTIVE INCENTIVE PLAN**

**ARTICLE 1  
Purpose**

The Microsoft Corporation Executive Incentive Plan is intended to provide incentive compensation to executive officers of the Company and those other senior officers that the Committee has determined should participate in the Plan. Awards under the Plan may be intended to qualify as performance-based compensation under Sections 162(m) and 409A of the Internal Revenue Code. The Plan was amended and restated to read as set forth herein on September 19, 2016.

**ARTICLE 2  
Definitions**

The terms used in this Plan include the feminine as well as the masculine gender and the plural as well as the singular, as the context in which they are used requires. The following terms, unless the context requires otherwise, are defined as follows:

- 2.1** “**Award**” means the incentive compensation awarded by the Committee under Section 4.1. Awards may be in the form of cash awards and/or equity-based awards issued under the Stock Plan.
- 2.2** “**Business Criteria**” means the following: sales or licensing volume, revenues, customer satisfaction, expenses, organizational health/productivity, earnings (which includes similar measurements such as net profits, operating income and net income, and which may be calculated before or after taxes, interest, depreciation, amortization or taxes), margins, cash flow, shareholder return, return on equity, return on assets or return on investments, working capital, product shipments or releases, technology advances and innovations, brand or product recognition or acceptance (including market share) and/or stock price.
- 2.3** “**Code**” means the Internal Revenue Code of 1986, as amended.
- 2.4** “**Committee**” means the Compensation Committee of the Company’s Board of Directors.
- 2.5** “**Company**” means Microsoft Corporation.
- 2.6** “**Deferred Compensation Plan**” means the Microsoft Corporation Deferred Compensation Plan, or a similar or successor plan or other arrangement for the deferral of compensation specified by the Committee.
- 2.7** “**Participant**” means an employee described in Article 3 of the Plan.
- 2.8** “**Performance Goals**” means the written objective performance goals for Awards under the Plan. To the extent required by Section 162(m), the Performance Goals shall be stated in terms of one or more Business Criteria. Performance Goals may be measured: individually, alternatively or in any combination, including through an index; with respect to the Company, a Company subsidiary, division, business unit, product line, product or any



combination of the foregoing; on an absolute basis, or relative to a target, to a designated comparison group, to results in other periods or to other external measures. The Committee may specify any reasonable definition of the measures it uses. Such definitions may provide for reasonable adjustments to the measures and may include or exclude items, including but not limited to: extraordinary or unusual and nonrecurring gains or losses, litigation or claim judgments or settlements, material changes in tax laws, acquisitions or divestitures, the cumulative effect of accounting changes, asset write-downs, restructuring charges, or the results of discontinued operations or products.

- 2.9** “**Performance Period**” means the period for which an Award is made for purposes of this Plan as determined by the Committee. For the avoidance of doubt, the applicable grant documentation for an Award may set forth performance requirements in addition to the Performance Goals, and such additional performance requirements may be based on a shorter or longer period than the Performance Period.
- 2.10** “**Plan**” means the Microsoft Corporation Executive Incentive Plan, as it may be amended from time to time.
- 2.11** “**Section 162(m)**” means Code Section 162(m) and applicable IRS guidance issued thereunder.
- 2.12** “**Stock Plan**” means the Company’s 2001 Stock Plan, or a similar or successor plan or other arrangement of the issuance of equity-based awards specified by the Committee.

### **ARTICLE 3 Eligibility and Participation**

Executive officers of the Company are eligible to receive Awards under the Plan. In addition, other senior officers of the Company may be designated by the Committee to receive Awards under the Plan. Any person who receives an Award under Section 4.1 shall be a Participant in the Plan and shall continue to be a Participant until any amounts due under any Awards he may receive have been paid.

### **ARTICLE 4 Incentive Awards**

#### **4.1 Grants of Awards.**

- (a) **Establishment of Written Terms**—Not later than 90 days after the beginning of a Performance Period for which the Committee has determined to grant Awards under the Plan (or within the first 25% of the Performance Period for any Performance Period that is less than 12 months) or any other date required or permitted under Section 162(m), the Committee shall determine in writing (a) the Participants receiving Awards for the Performance Period, (b) the Performance Goals for each Participant for the Performance Period, and (c) the amount payable to a Participant upon attainment of the applicable Performance Goals for the Performance Period.
- (b) **Incentive Pools**—Unless otherwise determined by the Committee, the amount payable to a Participant upon attainment of the applicable Performance Goals for a Performance Period will be stated as a percentage of an incentive pool. As described in Section 4.3 below, the amount of a

Participant's Award may be reduced below the amount determined by multiplying the incentive pool percentage by the incentive pool for the Performance Period. The total of the incentive pool percentages assigned to all Participants for a Performance Period shall not exceed 100%, and the amount of the incentive pool shall be determined under an objective formula or basis.

- (c) **Maximum Amount**—The maximum number of shares of Company common stock with respect to which equity-based Awards may be granted to any Participant based on one or more Performance Periods ending in a fiscal year of the Company shall not exceed (i) 20,000,000 shares for stock options or stock appreciation rights, and (ii) 5,000,000 shares for stock awards (increased, in both cases proportionately, in the event of any stock split, stock dividend or similar event with respect to the shares). The maximum Awards settled in cash based on one or more Performance Periods ending in a fiscal year of the Company shall (i) not exceed the stock award share limit above multiplied by the closing price per share of Company common stock on the last trading day coinciding with or preceding the date the cash Award is paid, and (ii) reduce the share limits for the Performance Period(s) for equity awards by the number of whole shares that could be purchased with the cash Award on the date of payment of the cash Award.
- (d) **New Executive Officers**—The Committee may grant an Award to an individual who becomes an executive officer during a Company fiscal year based on performance during the balance of the fiscal year or such other Performance Period as it determines. If the Performance Period for such an Award is less than 12 months, within the first 25% of the Performance Period or any other date required or permitted under Section 162(m), the Committee shall determine in writing (a) Performance Goals for the Performance Period, and (b) the amount payable to the Participant upon attainment of the applicable Performance Goals for the Performance Period. The amount payable to such a Participant upon attainment of the applicable Performance Goals for a Performance Period may be stated as a percentage of an incentive pool.
- (e) **EIP Awards**—Unless otherwise determined by the Committee, each Company fiscal year for which the Committee intends to grant an Award is a Performance Period for which the Committee will specify (1) the Participants, (2) if applicable, an incentive pool that is a percentage of the Company's operating income for the fiscal year, as reported in the Company's financial statements ("Operating Income"), and (3) if applicable, each Participant's incentive pool percentage for the Performance Period. In addition, if an employee becomes an executive officer of the Company after the first quarter of the Company's fiscal year, then the remainder of that fiscal year, including the quarter in which the employee becomes an executive officer, may be a Performance Period for which the Committee will specify: (1) such Participant (or Participants), (2) an incentive pool that is a percentage of the Company's Operating Income for the Performance Period, and (3) each Participant's incentive pool percentage for the Performance Period.

No payments will be made under an Award described in Section 4.1(e) unless the Company's Operating Income for the Performance Period is greater than zero; this positive Operating Income requirement is the Performance Goal for the applicable Performance Period.

- 4.2 Performance Goal Satisfaction and Certification.** Within a reasonable time after the close of a Performance Period, the Committee shall determine whether the Performance Goals established for that Performance Period have been met. If the Performance Goals have been met, the Committee shall so certify in writing to the extent required by Section 162(m).

- 4.3 Award Amount.** If the Committee has made the written certification under Section 4.2 for a Performance Period, each Participant to whom the certification applies shall be eligible to receive a payment under their Award for that Performance Period, subject to any additional requirements set forth in the written terms governing the Award and the applicable grant documentation. For any Performance Period, however, the Committee (and, with respect to Awards for the chief executive officer, two or more independent members of the Company's Board of Directors who are outside directors within the meaning of Section 162(m)) shall have the absolute discretion to reduce the amount of, or eliminate entirely, the payment under an Award to one or more of the Participants. Payment of all or part of an Award amount in the form of an equity compensation grant shall be made under, and subject to the terms and conditions of, the Stock Plan and the applicable grant documentation.
- 4.4 Payment of the Award.**
- (a) Unless otherwise determined by the Committee in the applicable grant documentation, payment of an Award for a Performance Period ending with a Company's fiscal year shall be made by the end of the fiscal quarter following the end of the fiscal year, and no later than March 15 of the calendar year following the close of the Performance Period (or if later, by the 15th day of the third month following the end of the Company's fiscal year containing the last day of the Performance Period).
- (b) As permitted by the Committee, a Participant may, in accordance with section 409A of the Code, voluntarily defer receipt of an Award in the form of cash under the terms of the Deferred Compensation Plan.
- (c) The Company shall have the right to deduct from any Award payable in cash any applicable Federal, state and local income and employment taxes and any other amounts that the Company is required to deduct. Deductions from an Award in the form of an equity compensation award shall be governed by the Company's 2001 Stock Plan and the applicable grant documentation.
- 4.5 Eligibility for Payments.** Unless otherwise determined by the Committee, a Participant shall be eligible to receive payment under an Award for a Performance Period only if the Participant is employed by the Company or a Company subsidiary on the last day of the Performance Period, and only if the Participant satisfies any other conditions to receipt of the Award specified by the Committee.
- 4.6 Discretionary Awards.** The Committee may grant Awards under the Plan that are not intended to qualify as performance-based compensation under Section 162(m) and as such will not need to meet the requirements of this Article 4.

## **ARTICLE 5 Administration**

- 5.1 General Administration.** The Plan is to be administered by the Committee. Subject to the terms and conditions of the Plan, the Committee is authorized and empowered in its sole discretion to select Participants and to make Awards in such amounts and upon such terms and conditions as it shall determine.

- 5.2 Administrative Rules.** The Committee shall have full power and authority to adopt, amend and rescind administrative guidelines, rules and regulations pertaining to this Plan and to interpret the Plan and rule on any questions respecting any of its provisions, terms and conditions.
- 5.3 Decisions Binding.** All decisions of the Committee concerning this Plan shall be binding on the Company and its subsidiaries and their respective boards of directors, and on all Participants and other persons claiming rights under the Plan.
- 5.4 Section 162(m) and Shareholder Approval.** Other than Awards issued under Section 4.6, Awards under this Plan are intended to satisfy the applicable requirements for the performance-based compensation exception under Section 162(m). It is intended that the Plan be administered, interpreted and construed so that such Awards ("162(m) Awards") meet such requirements. Payments under 162(m) Awards shall be contingent upon shareholder approval of the material terms of the Plan in accordance with Section 162(m). Unless and until such shareholder approval is obtained, no amounts shall be paid under 162(m) Awards.
- 5.5 Recovery Policy.** Amounts paid under the Plan shall be subject to recovery by the Company under its executive compensation recovery policy as in effect from time to time.

## **ARTICLE 6 Amendments and Termination**

The Plan may be amended or terminated by the Committee at any time. All amendments to this Plan, including an amendment to terminate the Plan, shall be in writing. An amendment shall not be effective without the approval of the shareholders of the Company if such approval is necessary to continue to qualify Awards (other than those issued under Section 4.6) as performance-based compensation under Section 162(m), or otherwise under Internal Revenue Service or SEC regulations, the rules of NASDAQ or any other applicable law or regulations, as reasonably interpreted by the Committee in its sole discretion.

## **ARTICLE 7 Miscellaneous**

- 7.1 Duration of the Plan.** The Plan shall remain in effect until all Performance Periods related to Awards made under the Plan have expired and any payments under such Awards have been made.
- 7.2 Awards Not Assignable.** No Award, or any right thereto, shall be assignable or transferable by a Participant except by will or by the laws of descent and distribution. Any attempted assignment or alienation shall be void and of no force or effect.
- 7.3 Participant Rights.** The right of any Participant to receive any Award payments under the provisions of the Plan shall be an unsecured claim against the general assets of the Company. The Plan shall not create, nor be construed in any manner as having created, any right by a Participant to any Award for a Performance Period because of a Participant's participation in the Plan for any prior Performance Period.

- 7.4 Employment at Will.** Neither this Plan nor any action or communication under this Plan: (1) gives any employee any right with respect to employment or continuation of current employment with the Company or its subsidiaries or to employment that is not terminable at will, or (2) sets any employee's employment with the Company or its subsidiaries for any minimum or fixed period. Employment by the Company or a Company subsidiary may be terminated by either the employee or the employer at any time, for any reason or no reason, with or without cause, and with or without notice or any kind of pre- or post-termination warning, discipline or procedure. This Section 7.4 applies to employment in the United States.
- 7.5 Successors.** Any successor (whether direct or indirect, by purchase, merger, consolidation or otherwise) to all or substantially all of the Company's business or assets, shall assume the Company's liabilities under this Plan and perform any duties and responsibilities in the same manner and to the same extent that the Company would be required to perform if no such succession had taken place.
- 7.6 References.** All statutory and regulatory references in this Plan include successor provisions.
- 7.7 Severability.** If any provision of the Plan is held invalid or illegal for any reason, any illegality or invalidity shall not affect the remaining parts of the Plan, but the Plan shall be construed and enforced as if the illegal or invalid provision had never been inserted.
- 7.8 Applicable Law and Venue.** The Plan shall be governed by the laws of the State of Washington. If the Company or any Participant (or beneficiary) initiates litigation related to this Plan, the venue for such action will be in King County, Washington.

**EXECUTIVE INCENTIVE PLAN****(Executive Officer SAs)****STOCK AWARD AGREEMENT UNDER  
THE MICROSOFT CORPORATION 2001 STOCK PLAN**

Award Number &lt;&lt;GrantIdentifier&gt;&gt;

This Award Agreement sets forth the terms and conditions of an award (the "Award") of performance-based Stock Awards ("SAs") awarded to <<FullName>> ("Awardee") by Microsoft Corporation (the "Company") in the exercise of its sole discretion under the Microsoft Corporation 2001 Stock Plan (the "Plan") and pursuant to the Microsoft Corporation Executive Incentive Plan (the "EIP") on <<GrantDate>> (the "Award Date"). Capitalized terms used but not defined in this Award Agreement shall have the meanings assigned to them in the Plan.

**1. Award.**

(a) The number of SAs initially subject to the Award (the "GrantedSAs") is <<Granted SAs>>. The performance period of the Award (the "Performance Period") is the Company's <<Year>> fiscal year. At the end of the Performance Period, the Committee (as that term is defined in Section 2(f) of the Plan) will determine the number of SAs earned under the Award as set forth in Section 2 (these earned SAs are the "Earned SAs").

(b) The Earned SAs represent the Company's unfunded and unsecured promise to issue Common Shares at a future date, subject to the terms of this Award Agreement and the Plan. Awardee has no rights under the Earned SAs other than the rights of a general unsecured creditor of the Company.

**2. Performance Goal; Earned SAs.**

(a) The performance goal for the Performance Period is that the Company have positive operating income for the Performance Period, as reported in the Company's financial statements (the "Performance Goal").

(b) Within a reasonable time after the close of the Performance Period, and in no event later than 90 days following the close of the Performance Period, the Committee shall determine whether the Performance Goal has been met and, if applicable, certify in accordance with the requirements of Code Section 162(m) to its satisfaction. The date the Committee makes this determination is the "Determination Date". If the Performance Goal has not been met, the number of Earned SAs will be zero. If the Performance Goal has been met, the number of Earned SAs will be the number of Granted SAs.

### 3. Vesting of SAs.

(a) Subject to the terms of this Award Agreement and the Plan and provided that Awardee remains continuously employed through the vesting dates set out below, the Earned SAs shall vest as follows:

Vesting Date	Percentage of Earned SAs
The Determination Date, as defined under Section 2(b) above or, if later, the August 31 following the Performance Period	25%
<i>[Insert 18-month anniversary of last business day in August preceding the Award Date] ("18 month Vest Date")</i>	12.5%
<i>Each 6 month anniversary of the 18 month Vest Date</i>	12.5%

Vesting will not occur before the first NASDAQ Stock Market regular trading day that is on or after the applicable vesting date.

(b) Awardee agrees that the SAs subject to this Award Agreement, and other incentive or performance-based compensation Awardee receives or has received from the Company, shall be subject to the Company's executive compensation recovery policy, as amended from time to time.

(c) AWARDEE'S RIGHTS IN THE SAs SHALL BE AFFECTED, WITH REGARD TO BOTH VESTING SCHEDULE AND TERMINATION, BY LEAVES OF ABSENCE, CHANGES IN THE NUMBER OF HOURS WORKED, PARTIAL DISABILITY, AND OTHER CHANGES IN AWARDEE'S EMPLOYMENT STATUS AS PROVIDED IN THE COMPANY'S CURRENT POLICIES FOR THESE MATTERS. ACCOMPANYING THIS AWARD AGREEMENT IS A CURRENT COPY OF THESE POLICIES. THESE POLICIES MAY CHANGE FROM TIME TO TIME WITHOUT NOTICE IN THE COMPANY'S SOLE DISCRETION, AND AWARDEE'S RIGHTS WILL BE GOVERNED BY THE POLICIES IN EFFECT AT THE TIME OF ANY EMPLOYMENT STATUS CHANGE. E-MAIL "BENEFITS" FOR A COPY OF THE MOST CURRENT POLICIES.

4. Termination. Unless terminated earlier under Section 5, 6 or 7 below, an Awardee's rights under this Award Agreement with respect to the SAs under this Award Agreement shall terminate at the time the SAs are converted into Common Shares and distributed to Awardee.

5. Termination of Awardee's Status as a Participant. Except as otherwise specified in Section 6, 7 and 8 below, in the event of termination of Awardee's Continuous Status as a Participant (as that term is defined in Section 2(j) of the Plan), Awardee's rights under this Award Agreement in any unvested SAs shall terminate. For the avoidance of doubt, an Awardee's Continuous Status as a Participant terminates at the time Awardee's actual employer ceases to be the Company or a "Subsidiary" of the Company, as that term is defined in Section 2(y) of the Plan, and except as otherwise specified in Section 6, 7 and 8 below, no person shall have any rights as an Awardee under this Award Agreement unless he or she is in Continuous Status as a Participant on the Award Date.

6. Disability of Awardee. Notwithstanding the provisions of Section 5 above, in the event of termination of Awardee's Continuous Status as a Participant as a result of total and permanent disability (as that term is defined in Section 12(c) of the Plan), outstanding unvested Earned SAs shall become immediately vested.

7. Death of Awardee. Notwithstanding the provisions of Section 5 above, if Awardee is, at the time of death, in Continuous Status as a Participant, outstanding unvested Earned SAs shall become immediately vested.

8. Retirement of Awardee; Severance.

(a) Notwithstanding the provisions of Section 5 above, in the event of Awardee's Retirement, Awardee shall be treated as continuously employed through the vesting dates in Section 3(a) above. For this purpose, "Retirement" means termination of employment with the Company or a Subsidiary after the earlier of (a) age 65, or (b) attaining age 55 and 15 years of Continuous Service, provided that immediately prior to termination of employment Awardee is employed by Microsoft (or a Subsidiary) in the United States.

This Section 8 will only apply to a Retirement if (a) the Retirement occurs more than one year after the Award Date, (b) Awardee executes a release in conjunction with the Retirement in the form provided by the Company, and (c) Awardee's employment does not terminate due to misconduct (as determined in the sole discretion of the Company's senior corporate officer in charge of the Human Resources department), including but not limited to misconduct in violation of Company policy and misconduct that adversely affects the Company's interests or reputation.

For purposes of this Section 8, "Continuous Service" means that Awardee has continuously remained an employee of the Company or a Subsidiary, measured from Awardee's "most recent hire date" as reflected in the Company records. For an Awardee who became an employee of the Company following the acquisition of his or her employer by the Company or a Subsidiary, service with the acquired employer shall count toward Continuous Service, and Continuous Service shall be measured from Awardee's acquired company hire date as reflected in the Company's records.

If the Awardee dies after an eligible Retirement under this Section 8, then any shares that would, but for the Awardee's death, be distributed pursuant to this Section 8 on vesting dates that follow the Awardee's death shall be immediately vested and distributed in accordance with this Award Agreement.

(b) Awardee may vest in shares following Awardee's termination of employment to the extent provided in a Company severance benefit plan, including the Senior Executive Severance Benefit Plan. In no event, however, shall any accelerated or continued vesting under a Company severance benefit plan change the time of payment specified under this Award Agreement.

9. Value of Unvested SAs. In consideration of the award of these SAs, Awardee agrees that upon and following termination of Awardee's Continuous Status as a Participant for any reason (whether or not in breach of applicable laws), and regardless of whether Awardee is terminated with or without cause, notice, or pre-termination procedure or whether Awardee asserts or prevails on a claim that Awardee's employment was terminable only for cause or only with notice or pre-termination procedure, any unvested SAs under this Award Agreement shall be deemed to have a value of zero dollars (\$0.00).



#### 10. Conversion of SAs to Common Shares; Responsibility for Taxes.

(a) Provided Awardee has satisfied the requirements of Section 10(b) below, on the vesting of any Earned SAs, the vested Earned SAs shall be converted into an equivalent number of Common Shares that will be distributed to Awardee (or Awardee's legal representative, if applicable) within 90 days after the date of the vesting event (but in no event prior to the Determination Date). Notwithstanding the foregoing, if accelerated vesting of an SA occurs pursuant to a provision of the Plan not addressed in this Award Agreement, distribution of the related Common Share shall not occur until the date distribution would have occurred under this Award Agreement absent this accelerated vesting. The distribution to Awardee (Awardee's legal representative, if applicable) of Common Shares in respect of the vested Earned SAs shall be evidenced by means that the Company determines to be appropriate. In the event ownership or issuance of Common Shares is not feasible due to applicable exchange controls, securities regulations, tax laws or other provisions of applicable law, as determined by the Company in its sole discretion, Awardee (Awardee's legal representative, if applicable) shall receive cash proceeds in an amount equal to the value of the Common Shares otherwise distributable to Awardee, as determined by the Company in its sole discretion, net of amounts withheld in satisfaction of the requirements of Section 10(b) below.

(b) Regardless of any action the Company or Awardee's actual employer takes with respect to any or all income tax (including federal, state and local taxes), social insurance, payroll tax, payment on account, or other tax-related withholding items ("Tax-Related Items") that arise in connection with the SAs, Awardee acknowledges and agrees that the ultimate liability for any Tax-Related Items determined by the Company in its discretion to be legally due by Awardee, is and remains Awardee's responsibility. Awardee acknowledges and agrees that the Company and/or Awardee's actual employer (i) make no representations or undertakings regarding the treatment of any Tax-Related Items in connection with any aspect of the SAs, including the grant of the SAs, the vesting of Earned SAs, the conversion of Earned SAs into Common Shares or the receipt of an equivalent cash payment, the subsequent sale of any Common Shares acquired and the receipt of any dividends; and (ii) do not commit to and are under no obligation to structure the terms of the grant or any aspect of the SAs to reduce or eliminate Awardee's liability for any Tax-Related Items.

Prior to the relevant taxable or tax-withholding event, as applicable, Awardee shall pay, or make adequate arrangements satisfactory to the Company or to Awardee's actual employer (in their sole discretion) to satisfy all obligations for Tax-Related Items. In this regard, Awardee authorizes the Company or Awardee's actual employer to withhold all applicable Tax-Related Items from Awardee's wages or other cash compensation payable to Awardee by the Company or Awardee's actual employer. Alternatively, or in addition, the Company or Awardee's actual employer may, in their sole discretion, and without notice to or authorization by Awardee, (i) sell or arrange for the sale of Common Shares to be issued upon the vesting of Earned SAs or other event to satisfy the withholding obligation, and/or (ii) withhold in Common Shares, provided that the Company and Awardee's actual employer shall withhold only the amount of shares necessary to satisfy the minimum withholding amount or such other amount determined by the Company as not resulting in negative accounting consequences for the Company. Awardee will be deemed to have been issued the full number of Common Shares subject to the Earned SAs, notwithstanding that a number of whole vested Common Shares are held back solely for the purpose of paying the Tax-Related Items. Awardee shall pay to the Company or to Awardee's actual employer any amount of Tax-Related Items that the Company or Awardee's actual employer may be required to withhold as a result of Awardee's receipt of SAs, the vesting of Earned SAs, or the conversion of vested Earned SAs to Common Shares that cannot be satisfied by the means described in this

paragraph. Except where applicable legal or regulatory provisions prohibit and notwithstanding anything in the Plan to the contrary, the standard process for the payment of an Awardee's Tax-Related Items shall be for the Company or Awardee's actual employer to withhold in Common Shares only to the amount of shares necessary to satisfy the minimum withholding amount or such other amount determined by the Company as not resulting in negative accounting consequences for the Company. The Company may refuse to deliver Common Shares to Awardee if Awardee fails to comply with Awardee's obligation in connection with the Tax-Related Items as described in this section 10.

(c) In lieu of issuing fractional Common Shares, on the vesting of a fraction of an Earned SA, the Company shall round the shares down to the nearest whole share and any such share that represents a fraction of a SA will be included in a subsequent vest date.

(d) Until the distribution to Awardee of the Common Shares in respect of the vested Earned SAs is evidenced by deposit in Awardee's brokerage account, Awardee shall have no right to vote or receive dividends or any other rights as a shareholder with respect to such Common Shares, notwithstanding the vesting of Earned SAs. No adjustment will be made for a dividend or other right for which the record date is prior to the date Awardee is recorded as the owner of the Common Shares, except as provided in Section 14 of the Plan.

(e) By accepting the Award of SAs evidenced by this Award Agreement, Awardee agrees not to sell any of the Common Shares received on account of vested Earned SAs at a time when applicable laws or Company policies prohibit a sale. This restriction shall apply so long as Awardee is an Employee, Consultant or outside director of the Company or a Subsidiary of the Company.

11. Non-Transferability of SAs. Awardee's right in the SAs awarded under this Award Agreement and any interest therein may not be sold, pledged, assigned, hypothecated, transferred, or disposed of in any manner, other than by will or by the laws of descent or distribution. SAs shall not be subject to execution, attachment or other process.

12. Acknowledgment of Nature of Plan and SAs. In accepting the Award, Awardee acknowledges that:

(a) the Plan is established voluntarily by the Company, it is discretionary in nature and may be modified, amended, suspended or terminated by the Company at any time, as provided in the Plan;

(b) the Award of SAs is voluntary and occasional and does not create any contractual or other right to receive future awards of SAs or other awards, or benefits in lieu of SAs even if SAs have been awarded repeatedly in the past;

(c) all decisions with respect to SAs or other future awards, if any, will be at the sole discretion of the Company;

(d) Awardee's participation in the Plan is voluntary;

(e) the future value of the underlying Common Shares is unknown and cannot be predicted with certainty;

(f) if Awardee receives Common Shares, the value of the Common Shares acquired on vesting of Earned SAs may increase or decrease in value;

(g) notwithstanding any terms or conditions of the Plan to the contrary and consistent with Section 5 above, in the event of termination of Awardee's Continuous Status as a Participant under circumstances where Section 8 above does not apply (whether or not in breach of applicable laws), Awardee's right to receive SAs and vest under the Plan, if any, will terminate effective as of the date that Awardee is no longer actively employed and will not be extended by any notice period mandated under applicable law. Awardee's right to receive Common Shares pursuant to any Earned SAs after termination of Continuous Status as a Participant, if any, will be calculated as of the date of termination of Awardee's active employment and will not be extended by any notice period mandated under applicable law. The senior corporate officer in charge of the Human Resources department shall have the exclusive discretion to determine when Awardee is no longer actively employed for purposes of the award of SAs; and

(h) Awardee acknowledges and agrees that, regardless of whether Awardee is terminated with or without cause, notice or pre-termination procedure or whether Awardee asserts or prevails on a claim that Awardee's employment was terminable only for cause or only with notice or pre-termination procedure, Awardee has no right to, and will not bring any legal claim or action for, (a) any damages for any portion of any Earned SAs that have been vested and converted into Common Shares, or (b) termination of any unvested SAs under this Award Agreement.

13. No Employment Right. Awardee acknowledges that neither the fact of this Award of SAs nor any provision of this Award Agreement or the Plan or the policies adopted pursuant to the Plan shall confer upon Awardee any right with respect to employment or continuation of current employment with the Company or with Awardee's actual employer, or to employment that is not terminable at will. Awardee further acknowledges and agrees that neither the Plan nor this Award of SAs makes Awardee's employment with the Company or Awardee's actual employer for any minimum or fixed period, and that this employment is subject to the mutual consent of Awardee and the Company or Awardee's actual employer, and may be terminated by either Awardee or the Company or Awardee's actual employer at any time, for any reason or no reason, with or without cause or notice or any kind of pre- or post-termination warning, discipline or procedure.

14. Administration. Except as otherwise expressly provided in the Plan, the authority to manage and control the operation and administration of this Award Agreement shall be vested in the Committee, and the Committee shall have all powers and discretion with respect to this Award Agreement as it has with respect to the Plan. Any interpretation of the Award Agreement by the Committee and any decision made by the Committee with respect to the Award Agreement shall be final and binding on all parties. References to the Committee in this Award Agreement shall be read to include a reference to any delegate of the Committee acting within the scope of his or her delegation.

15. Plan Governs. This Award Agreement shall be subject to the terms of the Plan and the EIP, and this Award Agreement is subject to all interpretations, amendments, rules and regulations promulgated by the Committee from time to time pursuant to the Plan and the EIP.

16. Notices. Any written notices provided for in this Award Agreement that are sent by mail shall be deemed received three business days after mailing, but not later than the date of actual receipt. Notices shall be directed, if to Awardee, at Awardee's address indicated by the Company's records and, if to the Company, at the Company's principal executive office.

17. Electronic Delivery. The Company may, in its sole discretion, decide to deliver any documents related to SAs awarded under the Plan or future SAs that may be awarded under the Plan by electronic

means or request Awardee's consent to participate in the Plan by electronic means. Awardee hereby consents to receive such documents by electronic delivery and agrees to participate in the Plan through an on-line or electronic system established and maintained by the Company or another third party designated by the Company.

18. Acknowledgment. By Awardee's acceptance of this Award Agreement in the manner prescribed by the Company, Awardee acknowledges that Awardee has received and has read, understood and accepted all the terms, conditions and restrictions of this Award Agreement, the Plan, and the current policies referenced in Sections 3(b) and 3(c) above. Awardee understands and agrees that this Award Agreement is subject to all the terms, conditions, and restrictions stated in this Award Agreement and in the other documents referenced in the preceding sentence, as the latter may be amended from time to time in the Company's sole discretion.

19. Board Approval. These SAs have been awarded pursuant to the Plan and this Award of SAs has been approved by the Compensation Committee of the Board of Directors or the Board of Directors.

20. Governing Law and Venue. This Award Agreement shall be governed by the laws of the State of Washington, U.S.A., without regard to Washington laws that might cause other law to govern under applicable principles of conflicts of law. The venue for any litigation related to this Award Agreement will be in King County, Washington.

21. Severability. If one or more of the provisions of this Award Agreement shall be held invalid, illegal or unenforceable in any respect, the validity, legality and enforceability of the remaining provisions shall not in any way be affected or impaired thereby and the invalid, illegal or unenforceable provisions shall be deemed null and void; however, to the extent permissible by law, any provisions that could be deemed null and void shall first be construed, interpreted or revised retroactively to permit this Award Agreement to be construed so as to foster the intent of this Award Agreement and the Plan.

22. Complete Award Agreement and Amendment. This Award Agreement (including the policies referenced in Sections 3(b) and 3(c)) and the Plan constitute the entire agreement between Awardee and the Company regarding SAs. Any prior agreements, commitments or negotiations concerning these SAs are superseded. This Award Agreement may be amended only by written agreement of Awardee and the Company, without consent of any other person, provided that no consent is necessary to an amendment that in the reasonable judgment of the Committee confers a benefit on Awardee. Awardee agrees not to rely on any oral information regarding this Award of SAs or any written materials not identified in this Section 22.

23. Code Section 409A. This Award Agreement shall be interpreted, operated, and administered in a manner so as not to subject Awardee to the assessment of additional taxes or interest under Code section 409A, and this Award Agreement shall be amended as the Company, in its sole discretion, determines is necessary and appropriate to avoid the application of any such taxes or interest.

24. Code Section 162(m). The Award is intended to satisfy the applicable requirements for the performance-based compensation exception under Code section 162(m) and applicable IRS guidance issued thereunder, and it is intended that the Award be interpreted, operated and administered to meet such requirements.

**SENIOR EXECUTIVE SEVERANCE BENEFIT PLAN**

(As amended effective September 19, 2016)

This Senior Executive Severance Benefit Plan (this "Plan") sets forth the separation benefits that the Compensation Committee of the Board has approved for Microsoft Corporation ("Microsoft" or "Company") executives who participate in Microsoft's Executive Incentive Plan and whose employment is terminated without cause.

**Eligibility**

You will be entitled to receive the separation benefits described in this Plan if all of the following apply:

- Your employment is terminated by Microsoft without Cause (a "Covered Termination"). For this purpose, "Cause" means your: (1) conviction or plea of guilty or no contest to (a) any felony or (b) a misdemeanor charge involving fraud, false statements or misleading omissions, wrongful taking, embezzlement, bribery, forgery, counterfeiting or extortion; (2) engaging in gross misconduct; (3) repeated failure to substantially perform your duties after notice and an opportunity to cure, provided those duties are consistent with your seniority; (4) violation of any securities laws, rules or regulations, or the rules and regulations of any securities exchange or association of which Microsoft or any of its affiliates is a member; or (5) violation of Microsoft's policies designed to prevent violations of law, such as, without limitation, policies pertaining to compliance with the laws prohibiting unlawful discrimination, harassment, or insider trading.
- You received notice from Microsoft that you are eligible for the benefits described in this Plan, and at the time you received notice you were a participant in Microsoft's Executive Incentive Plan.
- You satisfy the "Conditions to Receiving Benefits" described below.

**Separation Benefits**

If you are entitled to separation benefits under this Plan, you will receive the following (less all applicable withholdings):

**Part-Year Annual Cash Award:** A pro-rated portion of your annual target cash award under Microsoft's Executive Incentive Plan for the fiscal year in which the Covered Termination occurs, determined by multiplying (1) your annual salary in effect at time of the Covered Termination, by (2) the target cash award percentage for the fiscal year under the Executive Incentive Plan, and by (3) the number of full and partial calendar months you have worked in that fiscal year divided by 12. This payment will be made at the time annual cash awards for the year are paid to other participants in Microsoft's Executive Incentive Plan. If your cash award is designed to be a performance-based award under Section 162(m) of the Internal Revenue Code, payment of your pro-rated annual target cash awards will be subject to achieving the relevant performance goal established for the year and the other limits of the Executive Incentive Plan.

**Severance Payment:** A severance payment equal to the sum of (1) your annual base salary in effect at the time of the Covered Termination and (2) your target annual cash award under the Microsoft's Executive Incentive Plan for the fiscal year in which the Covered Termination occurs, calculated using your annual salary in effect at time of the Covered Termination. Your payment will be reduced by any severance or similar benefits under any other Microsoft plan, program or policy. The severance payment will be made in a lump sum within 60 days after your employment terminates.

**Vesting of Eligible Stock Awards:** Vesting of eligible stock awards, as follows:

1. Vesting of the portion of your outstanding stock awards that would otherwise vest in the 12 months following the Covered Termination (disregarding any stock award agreement provisions for vesting due to death, disability or retirement). Any stock awards that vest as a result of this paragraph will be delivered in accordance with the terms of the applicable stock award agreement. This paragraph does not apply to performance stock awards.

2. Vesting of a pro-rated portion of the number of shares earned (or, if less, the target award shares) under any performance stock award under the Company's Executive Incentive Plan, provided that:

(i) at least one year of the performance period has been completed at your employment termination, and

(ii) the pro-rated vesting applies to shares earned based on achievement of performance goals under the stock award agreement.

The pro-rated number of shares that vest under your performance stock award is determined by multiplying (i) the number of shares earned based on performance against goals under the stock award agreement, if any (or, if less, the target award shares under that agreement), by (ii) the number of full and partial calendar months during which you have been employed as a participant in the Executive Incentive Plan during the performance period, divided by the number of months in the performance period, then rounding up to the nearest whole share. Any performance stock awards that vest as a result of this paragraph will be delivered following the end of the applicable performance period in accordance with the terms of the applicable stock award agreement.

3. If your unvested stock award provides for continued vesting following an eligible "Retirement" based on your age or age plus service, and if on your termination date you are within one year of becoming eligible for Retirement, then you will be treated as meeting the age and service requirements for Retirement under the stock award agreement. All other requirements for Retirement set forth in the award agreement must still be met.

**Health Benefit Continuation and Outplacement:** Payment of COBRA premiums under the Microsoft Welfare Plan for any COBRA continuation coverage you properly elect for you or your eligible dependents through the six-month anniversary of your termination of employment. In addition, you will have access to outplacement assistance made available by Microsoft for up to 12 months.

**Reductions for Other Severance.** Your Severance Payment and your Part Year Annual Cash Award (in that order) shall be reduced by (i) any period of pay you are provided under applicable law in connection with your employment termination, including the WARN Act or any similar law, (ii) any severance pay or similar pay under any agreement or other arrangement with Microsoft or its affiliates, or (iii) any amounts you receive as severance or similar program due to your employment termination under applicable law. In addition, the vesting of your eligible stock awards under this Plan shall be reduced to the extent vesting of your stock awards (eligible or otherwise) is provided under any law, plan or arrangement with Microsoft or its affiliates or under applicable law.

### **Conditions to Receiving Benefits**

To receive any benefits under this Plan, you must sign, return and not revoke a Separation and Release Agreement in the form provided by Microsoft (without change) within 45 days after your termination.

The form of the Separation and Release Agreement will be determined by Microsoft from time to time (it being understood that it will contain a full waiver and release of claims, confidentiality and non-disparagement provisions, and twelve-month non-compete/non-solicitation restrictions) and be provided to you promptly following termination.

In addition, you will not receive benefits under this Plan if either of the following apply:

- Your employment terminates due to death, disability, retirement or termination by you for any other reason (including so-called constructive termination). For this purpose, "disability" and "retirement" are determined in the same manner as under the Microsoft 2001 Stock Plan and your stock award agreements.
- You do not comply with the terms of your Separation and Release Agreement or your Employee Agreement with Microsoft.

### **Additional Provisions**

**Plan Administration.** The Compensation Committee has the discretionary authority to interpret this Plan, adopt any administrative procedures (including claims procedures) and other rules for carrying out this Plan as may be appropriate and decide any and all matters and make any and all determinations arising under this Plan. The Compensation Committee has delegated these powers to the senior corporate officer in charge of Microsoft's Human Resources department. Any interpretations and decisions of the Compensation Committee or its delegate shall be final, conclusive and binding on all parties affected.

**Plan Termination and Amendment.** The Compensation Committee may amend this Plan in any manner (including to terminate this Plan), provided that, if (1) an amendment will terminate this Plan or (2) an amendment is determined by the Committee to be, in the aggregate, material and adverse to executives who have been notified of their eligibility for Plan benefits, the Company will provide at least six months' notice to those executives prior to the effective date of the amendment.

**Section 409A.** It is the intent that no severance or other payments or benefits provided under this Plan shall be considered “non-qualified deferred compensation” within the meaning of Section 409A of the Internal Revenue Code and this Plan will be interpreted accordingly. If and to the extent that any such severance or other payments or benefits under this Plan are determined by the Committee to constitute non-qualified deferred compensation and is provided to a participant who is a “specified employee” due to a “separation from service” (each, within the meaning of Section 409A), then such payment or benefit will be delayed for six months following such separation from service. For the purposes of this Plan, each payment and benefit set forth herein will be deemed to be separate payments and will be deemed not to be a deferral of compensation subject to Section 409A to the extent any such payment or benefit would constitute a “short-term deferral” or a payment pursuant to a “separation pay plan” within the meaning of Section 409A.

**Governing Law and Venue.** The Plan shall be governed by the laws of the State of Washington to the extent federal laws do not apply. If the Company or any Participant (or beneficiary) initiates litigation related to this Plan, the venue for such action will be in King County, Washington.

**No Employment Rights.** Notwithstanding any provision of this Plan, your employment is terminable at will, meaning that either you or Microsoft may terminate the employment relationship at any time, for any reason, with or without cause or notice. No term of this Plan shall be construed as altering the at-will nature of your employment.



**Executive Incentive Plan**

**(Executive Officer PSAs)**

**PERFORMANCE STOCK AWARD AGREEMENT UNDER  
THE MICROSOFT CORPORATION 2001 STOCK PLAN**

Award Number

This Award Agreement sets forth the terms and conditions of an award (the "Award") of performance stock awards ("PSAs") awarded to <<FullName>> ("Awardee") by Microsoft Corporation (the "Company") in the exercise of its sole discretion under the Microsoft Corporation 2001 Stock Plan (the "Plan") and pursuant to the Microsoft Corporation Executive Incentive Plan (the "EIP") on <<GrantDate>> (the "Award Date"). Capitalized terms used but not defined in this Award Agreement shall have the meanings assigned to them in the Plan.

1. Award.

(a) The Award is earned over a performance period beginning July 1, 2016 and ending June 30, 2019 (the "Performance Period"). Under the Award, the number of shares that may be earned at target performance for the Performance Period is <<TargetShares>> ("Target Award"), and the maximum number of shares that may be earned for the Performance Period is 300% of the Target Award. At the end of the Performance Period, the Committee (as that term is defined in Section 2(f) of the Plan) will determine the number of PSAs earned under the Award as set forth in Section 2 (these earned PSAs are the "Earned PSAs").

(b) The PSAs represent the Company's unfunded and unsecured promise to issue Common Shares at a future date, subject to the terms of this Award Agreement and the Plan. Awardee has no rights under the PSAs other than the rights of a general unsecured creditor of the Company.

2. Performance Goals; Earned PSAs.

(a) The performance goal for the Performance Period is that the Company have positive operating income for the Company's 2017 fiscal year, as reported in the Company's financial statements (the "Threshold Goal").

(b) Within 90 days following the close of the Company's 2017 fiscal year, the Committee shall assess performance against the Threshold Goal in accordance with Section 4.2 of the EIP. If the Threshold Goal is achieved, within 90 days following the close of the Performance Period the Committee shall determine the number of Earned PSAs pursuant to Schedule A; provided that in no event may the number of Earned PSAs exceed the maximum amount specified in Section 1(a) or in Section 4.1 of the EIP. If the Threshold Goal for the Performance Period is not achieved, the number of Earned PSAs shall be zero. The date the Committee makes the determination of the number of Earned PSAs is the "Determination Date" for the Performance Period.

### 3. Vesting of PSAs.

(a) Earned PSAs shall vest on the first NASDAQ Stock Market regular trading day that is on or after the Determination Date, subject to the terms of this Award Agreement and the Plan and provided that Awardee remains continuously employed through the last day of the Performance Period.

(b) Awardee agrees that the PSAs subject to this Award Agreement, and other incentive or performance-based compensation Awardee receives or has received from the Company, shall be subject to the Company's executive compensation recovery policy, as amended from time to time.

4. Termination. Unless terminated earlier under Section 5, 6 or 7 below, an Awardee's rights under this Award Agreement with respect to the PSAs under this Award Agreement shall terminate at the time the PSAs are converted into Common Shares and distributed to Awardee.

5. Termination of Awardee's Status as a Participant. Except as otherwise specified in Section 6 or 7 below, in the event of termination of Awardee's Continuous Status as a Participant (as that term is defined in Section 2(j) of the Plan), Awardee's rights under this Award Agreement in any unvested PSAs shall terminate. For the avoidance of doubt, an Awardee's Continuous Status as a Participant terminates at the time Awardee's actual employer ceases to be the Company or a "Subsidiary" of the Company, as that term is defined in Section 2(y) of the Plan, and except as otherwise specified in Section 6 or 7 below, no person shall have any rights as an Awardee under this Award Agreement unless he or she is in Continuous Status as a Participant on the Award Date.

### 6. Disability or Death of Awardee.

(a) Notwithstanding the provisions of Section 5 above, in the event of termination of Awardee's Continuous Status as a Participant as a result of total and permanent disability (as that term is defined in Section 12(c) of the Plan) before the end of the Performance Period, the Awardee shall become immediately vested in the Target Award.

(b) Notwithstanding the provisions of Section 5 above, if at the time of Awardee's death before the end of the Performance Period he or she is in Continuous Status as a Participant (including pursuant to Section 7(a) below), the Awardee shall become immediately vested in the Target Award. If Awardee vests in the Target Award pursuant to Section 6(b), then no vesting shall occur pursuant to the Retirement vesting provisions of Section 7(a).

### 7. Retirement of Awardee; Severance.

(a) Notwithstanding the provisions of Section 5 above, in the event of Awardee's Retirement, Awardee shall be treated as continuously employed through the vesting date in Section 3(a) above; provided that any Earned PSAs shall be prorated, so that the number of PSAs that vest shall be calculated by multiplying the number of Earned PSAs by (i) the number of calendar months in which Awardee was in Continuous Service (including partial months) from the beginning of the Performance Period to the date of Awardee's Retirement, divided by (ii) the number of calendar months (including partial months) in the Performance Period. For this purpose, "Retirement" means termination of employment with the

Company or a Subsidiary after the earlier of (a) age 65, or (b) attaining age 55 and 15 years of Continuous Service, provided that immediately prior to termination of employment Awardee is employed by Microsoft (or a Subsidiary) in the United States.

This Section 7 will only apply to a Retirement if (i) the Retirement occurs more than one year after the beginning of the Performance Period, (ii) Awardee executes a release in conjunction with the Retirement in the form provided by the Company, and (iii) Awardee's employment does not terminate due to misconduct (as determined in the sole discretion of the Company's senior corporate officer in charge of the Human Resources department), including but not limited to misconduct in violation of Company policy and misconduct that adversely affects the Company's interests or reputation.

For purposes of this Section 7, "Continuous Service" means that Awardee has continuously remained an employee of the Company or a Subsidiary, measured from Awardee's "most recent hire date" as reflected in the Company records. For an Awardee who became an employee of the Company following the acquisition of his or her employer by the Company or a Subsidiary, service with the acquired employer shall count toward Continuous Service, and Continuous Service shall be measured from Awardee's acquired company hire date as reflected in the Company's records.

(b) Awardee may vest in PSAs following Awardee's termination of employment to the extent provided in a Company severance benefit plan, including the Senior Executive Severance Benefit Plan. In no event, however, shall any accelerated or continued vesting under a Company severance benefit plan change the time of payment specified under this Award Agreement.

8. Value of Unvested PSAs. In consideration of the award of these PSAs, Awardee agrees that upon and following termination of Awardee's Continuous Status as a Participant for any reason (whether or not in breach of applicable laws), and regardless of whether Awardee is terminated with or without cause, notice, or pre-termination procedure or whether Awardee asserts or prevails on a claim that Awardee's employment was terminable only for cause or only with notice or pre-termination procedure, any unvested PSAs under this Award Agreement shall be deemed to have a value of zero dollars (\$0.00).

9. Conversion of PSAs to Common Shares; Responsibility for Taxes.

(a) Provided Awardee has satisfied the requirements of Section 9(b) below, on the vesting of any Earned PSAs, the vested Earned PSAs shall be converted into an equivalent number of Common Shares that will be distributed to Awardee (or Awardee's legal representative, if applicable) within 60 days after the date of the vesting event (but in no event prior to the Determination Date, except in the event of accelerated vesting under Section 6 above). Notwithstanding the foregoing, if accelerated vesting of a PSA occurs pursuant to a provision of the Plan not addressed in this Award Agreement, to the extent required by Code section 409A, distribution of the related Common Share shall not occur until the date distribution would have occurred under this Award Agreement absent this accelerated vesting. The distribution to Awardee (or Awardee's legal representative, if applicable) of Common Shares in respect of the vested Earned PSAs shall be evidenced by means that the Company determines to be appropriate. In the event ownership or issuance of Common Shares is not feasible due to applicable exchange controls, securities regulations, tax laws or other provisions of applicable law, as determined by the Company in its sole discretion, Awardee (or Awardee's legal representative, if applicable) shall receive cash proceeds in an

amount equal to the value of the Common Shares otherwise distributable to Awardee, as determined by the Company in its sole discretion, net of amounts withheld in satisfaction of the requirements of Section 9(b) below.

(b) Regardless of any action the Company or Awardee's actual employer takes with respect to any or all income tax (including federal, state and local taxes), social insurance, payroll tax, payment on account, or other tax-related withholding items ("Tax-Related Items") that arise in connection with the PSAs, Awardee acknowledges and agrees that the ultimate liability for any Tax-Related Items determined by the Company in its discretion to be legally due by Awardee, is and remains Awardee's responsibility. Awardee acknowledges and agrees that the Company and/or Awardee's actual employer (i) make no representations or undertakings regarding the treatment of any Tax-Related Items in connection with any aspect of the PSAs, including the grant of the PSAs, the vesting of Earned PSAs, the conversion of Earned PSAs into Common Shares or the receipt of an equivalent cash payment, the subsequent sale of any Common Shares acquired and the receipt of any dividends; and (ii) do not commit to and are under no obligation to structure the terms of the grant or any aspect of the PSAs to reduce or eliminate Awardee's liability for any Tax-Related Items.

Prior to the relevant taxable or tax-withholding event, as applicable, Awardee shall pay, or make adequate arrangements satisfactory to the Company or to Awardee's actual employer (in their sole discretion) to satisfy all obligations for Tax-Related Items. In this regard, Awardee authorizes the Company or Awardee's actual employer to withhold all applicable Tax-Related Items from Awardee's wages or other cash compensation payable to Awardee by the Company or Awardee's actual employer. Alternatively, or in addition, the Company or Awardee's actual employer may, in their sole discretion, and without notice to or authorization by Awardee, (i) sell or arrange for the sale of Common Shares to be issued upon the vesting of Earned PSAs or other event to satisfy the withholding obligation, and/or (ii) withhold in Common Shares, provided that the Company and Awardee's actual employer shall withhold only the amount of shares necessary to satisfy the minimum withholding amount or such other amount determined by the Company as not resulting in negative accounting consequences for the Company. Awardee will be deemed to have been issued the full number of Common Shares subject to the Earned PSAs, notwithstanding that a number of whole vested Common Shares are held back solely for the purpose of paying the Tax-Related Items. Awardee shall pay to the Company or to Awardee's actual employer any amount of Tax-Related Items that the Company or Awardee's actual employer may be required to withhold as a result of Awardee's receipt of PSAs, the vesting of Earned PSAs, or the conversion of vested Earned PSAs to Common Shares that cannot be satisfied by the means described in this paragraph. Except where applicable legal or regulatory provisions prohibit and notwithstanding anything in the Plan to the contrary, the standard process for the payment of an Awardee's Tax-Related Items shall be for the Company or Awardee's actual employer to withhold in Common Shares only to the amount of shares necessary to satisfy the minimum withholding amount or such other amount determined by the Company as not resulting in negative accounting consequences for the Company. The Company may refuse to deliver Common Shares to Awardee if Awardee fails to comply with Awardee's obligation in connection with the Tax-Related Items as described in this Section 9.

(c) In lieu of issuing fractional Common Shares, on the vesting of a fraction of an Earned PSA, the Company shall round the shares down to the nearest whole share.

(d) Until the distribution to Awardee of the Common Shares in respect of the vested Earned PSAs is evidenced by deposit in Awardee's brokerage account, Awardee shall have no right to vote or receive dividends or any other rights as a shareholder with respect to such Common Shares, notwithstanding the vesting of Earned PSAs. No adjustment will be made for a dividend or other right for which the record date is prior to the date Awardee is recorded as the owner of the Common Shares, except as provided in Section 14 of the Plan.

(e) By accepting the Award of PSAs evidenced by this Award Agreement, Awardee agrees not to sell any of the Common Shares received on account of vested Earned PSAs at a time when applicable laws or Company policies prohibit a sale. This restriction shall apply so long as Awardee is an Employee, Consultant or outside director of the Company or a Subsidiary of the Company.

10. Non-Transferability of PSAs. Awardee's right in the PSAs awarded under this Award Agreement and any interest therein may not be sold, pledged, assigned, hypothecated, transferred, or disposed of in any manner, other than by will or by the laws of descent or distribution. PSAs shall not be subject to execution, attachment or other process.

11. Acknowledgment of Nature of Plan and PSAs. In accepting the Award, Awardee acknowledges that:

(a) the Plan is established voluntarily by the Company, it is discretionary in nature and may be modified, amended, suspended or terminated by the Company at any time, as provided in the Plan;

(b) the Award of PSAs is voluntary and occasional and does not create any contractual or other right to receive future awards of PSAs or other awards, or benefits in lieu of PSAs even if PSAs have been awarded repeatedly in the past;

(c) all decisions with respect to PSAs or other future awards, if any, will be at the sole discretion of the Company;

(d) Awardee's participation in the Plan is voluntary;

(e) the future value of the underlying Common Shares is unknown and cannot be predicted with certainty;

(f) if Awardee receives Common Shares, the value of the Common Shares acquired on vesting of Earned PSAs may increase or decrease in value;

(g) notwithstanding any terms or conditions of the Plan to the contrary and consistent with Section 5 above, in the event of termination of Awardee's Continuous Status as a Participant under circumstances where Section 7 above does not apply (whether or not in breach of applicable laws), Awardee's right to receive PSAs, if any, will terminate effective as of the date that Awardee is no longer actively employed and will not be extended by any notice period mandated under applicable law. Awardee's right to

receive Common Shares pursuant to any Earned PSAs after termination of Continuous Status as a Participant, if any, will be calculated as of the date of termination of Awardee's active employment and will not be extended by any notice period mandated under applicable law; or if later, the Determination Date in the event of continued vesting under Section 7 above. The senior corporate officer in charge of the Company's Human Resources department has the exclusive discretion to determine when Awardee is no longer actively employed for purposes of the award of PSAs; and

(h) Awardee acknowledges and agrees that, regardless of whether Awardee is terminated with or without cause, notice or pre-termination procedure or whether Awardee asserts or prevails on a claim that Awardee's employment was terminable only for cause or only with notice or pre-termination procedure, Awardee has no right to, and will not bring any legal claim or action for, (a) any damages for any portion of any Earned PSAs that have been vested and converted into Common Shares, or (b) termination of any unvested PSAs under this Award Agreement.

12. No Employment Right. Awardee acknowledges that neither the fact of this Award of PSAs nor any provision of this Award Agreement or the Plan or the policies adopted pursuant to the Plan shall confer upon Awardee any right with respect to employment or continuation of current employment with the Company or with Awardee's actual employer, or to employment that is not terminable at will. Awardee further acknowledges and agrees that neither the Plan nor this Award of PSAs makes Awardee's employment with the Company or Awardee's actual employer for any minimum or fixed period, and that this employment is subject to the mutual consent of Awardee and the Company or Awardee's actual employer, and may be terminated by either Awardee or the Company or Awardee's actual employer at any time, for any reason or no reason, with or without cause or notice or any kind of pre- or post-termination warning, discipline or procedure.

13. Administration. Except as otherwise expressly provided in the Plan, the authority to manage and control the operation and administration of this Award Agreement shall be vested in the Committee, and the Committee shall have all powers and discretion with respect to this Award Agreement as it has with respect to the Plan. Any interpretation of the Award Agreement by the Committee and any decision made by the Committee with respect to the Award Agreement shall be final and binding on all parties. References to the Committee in this Award Agreement shall be read to include a reference to any delegate of the Committee acting within the scope of his or her delegation.

14. Plan Governs. Except as provided in Schedule A, this Award Agreement shall be subject to the terms of the Plan and the EIP, and this Award Agreement is subject to all interpretations, amendments, rules and regulations promulgated by the Committee from time to time pursuant to the Plan and the EIP.

15. Notices. Any written notices provided for in this Award Agreement that are sent by mail shall be deemed received three business days after mailing, but not later than the date of actual receipt. Notices shall be directed, if to Awardee, at Awardee's address indicated by the Company's records and, if to the Company, at the Company's principal executive office.

16. Electronic Delivery. The Company may, in its sole discretion, decide to deliver any documents related to PSAs awarded under the Plan or future PSAs that may be awarded under the Plan by electronic

means or request Awardee's consent to participate in the Plan by electronic means. Awardee hereby consents to receive such documents by electronic delivery and agrees to participate in the Plan through an on-line or electronic system established and maintained by the Company or another third party designated by the Company.

17. Acknowledgment. By Awardee's acceptance of this Award Agreement in the manner prescribed by the Company, Awardee acknowledges that Awardee has received and has read, understood and accepted all the terms, conditions and restrictions of this Award Agreement (including the policy referenced in Section 3(b)) and the Plan. Awardee understands and agrees that this Award Agreement is subject to all the terms, conditions, and restrictions stated in this Award Agreement and in the other documents referenced in the preceding sentence, as the latter may be amended from time to time in the Company's sole discretion.

18. Board Approval. These PSAs have been awarded pursuant to the Plan and this Award of PSAs has been approved by the Committee or the Board of Directors.

19. Governing Law, Venue and Arbitration. This Award Agreement shall be governed by the laws of the State of Washington, U.S.A., without regard to Washington laws that might cause other law to govern under applicable principles of conflicts of law. The venue for any litigation related to this Award Agreement will be in King County, Washington.

Awardee and the Company agree to resolve any dispute, claim, or controversy relating to this Award Agreement between each other, including claims against the Company's subsidiaries, and the current and former officers, directors, or employees of any of them (collectively "the Company"), in the manner specified in this Section 19. The Company and its affiliates, and Awardee, are referred to below as "parties."

The parties agree to first attempt to resolve all disputes through informal negotiations. The party asserting the dispute shall provide written notice to the other party describing with specificity the nature of the dispute. Written notice to Awardee shall be delivered to Awardee's home address appearing in the Company's records. Written notice to the Company shall be delivered to the attention of its General Counsel. Within five days after delivery of the written notice, the other party shall respond in writing stating its position.

If the parties are unable to resolve the dispute through informal negotiations, the parties agree to resolve all disputes by binding arbitration before a single qualified mutually selected arbitrator in accordance with the National Rules for the Resolution of Employment Disputes of the American Arbitration Association. If the parties are unable to agree on an arbitrator, each party shall select a representative and those two representatives shall select a qualified arbitrator who shall preside over the arbitral proceeding. The party initiating the arbitration normally shall bear the burden of proof and normally must prove any actual damages sought, but these proof issues will be determined by applicable law. The prevailing party shall be entitled to reasonable attorney's fees and costs to the extent consistent with applicable law. The Company shall pay the arbitration costs, including the administrative fees and the arbitrator's fees and expenses. The arbitrator shall issue a written decision

within fifteen days of the end of the hearing. The decision of the arbitrator shall be final and binding and may be enforced and a judgment entered in any court of competent jurisdiction. The arbitration itself, and all testimony, documents, briefs and arguments therein, shall be kept confidential. This Section 19 shall survive the employer-employee relationship between the Company and Awardee.

20. Severability. If one or more of the provisions of this Award Agreement shall be held invalid, illegal or unenforceable in any respect, the validity, legality and enforceability of the remaining provisions shall not in any way be affected or impaired thereby and the invalid, illegal or unenforceable provisions shall be deemed null and void; however, to the extent permissible by law, any provisions that could be deemed null and void shall first be construed, interpreted or revised retroactively to permit this Award Agreement to be construed so as to foster the intent of this Award Agreement and the Plan.

21. Complete Award Agreement and Amendment. This Award Agreement (including the policy referenced in Section 3(b)) and the Plan constitute the entire agreement between Awardee and the Company regarding PSAs. Any prior agreements, commitments or negotiations concerning these PSAs are superseded. This Award Agreement may be amended only by written agreement of Awardee and the Company, without consent of any other person, provided that no consent is necessary to an amendment that in the reasonable judgment of the Committee confers a benefit on Awardee. Awardee agrees not to rely on any oral information regarding this Award of PSAs or any written materials not identified in this Section 21.

22. Code Section 409A. Payments under this Award Agreement are intended to be exempt from Code section 409A to the extent they satisfy the "short-term deferral exception" under Code section 409A and otherwise to be compliant with Code section 409A, and this Award Agreement shall be interpreted, operated and administered accordingly. To the extent applicable, each payment under this Award Agreement shall be treated as a separate payment for purposes of Code section 409A.

23. Code Section 162(m). The Award is intended to satisfy the applicable requirements for the performance-based compensation exception under Code section 162(m) and applicable IRS guidance issued thereunder, and it is intended that the Award be interpreted, operated and administered to meet such requirements.



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**Schedule A to Performance Stock Award Agreement**

[To be separately approved by the Committee]

Microsoft Corporation  
One Microsoft Way  
Redmond, Washington

We have reviewed, in accordance with the standards of the Public Company Accounting Oversight Board (United States), the unaudited interim financial information of Microsoft Corporation and subsidiaries for the three-month periods ended September 30, 2016 and 2015, and have issued our report dated October 20, 2016. As indicated in such report, because we did not perform an audit, we expressed no opinion on that information.

We are aware that our report referred to above, which is included in your Quarterly Report on Form 10-Q for the quarter ended September 30, 2016, is incorporated by reference in Registration Statement Nos. 333-109185, 333-118764, 333-91755, 333-52852, 333-132100, 333-161516, 333-75243, and 333-185757 on Form S-8 and Registration Statement No. 333-207652 on Form S-3.

We also are aware that the aforementioned report, pursuant to Rule 436(c) under the Securities Act of 1933, is not considered a part of the Registration Statement prepared or certified by an accountant or a report prepared or certified by an accountant within the meaning of Sections 7 and 11 of that Act.

/s/ DELOITTE & TOUCHE LLP

Seattle, Washington

October 20, 2016

**CERTIFICATIONS**

I, Satya Nadella, certify that:

1. I have reviewed this quarterly report on Form 10-Q of Microsoft Corporation;
2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;
3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;
4. The registrant's other certifying officer and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f)) for the registrant and have:
  - a) Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;
  - b) Designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles;
  - c) Evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and
  - d) Disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter (the registrant's fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting; and
5. The registrant's other certifying officer and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of registrant's Board of Directors (or persons performing the equivalent functions):
  - a) All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize and report financial information; and
  - b) Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal control over financial reporting.

/s/ SATYA NADELLA

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Satya Nadella  
Chief Executive Officer

October 20, 2016

**CERTIFICATIONS**

I, Amy E. Hood, certify that:

1. I have reviewed this quarterly report on Form 10-Q of Microsoft Corporation;
2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;
3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;
4. The registrant's other certifying officer and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f)) for the registrant and have:
  - a) Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;
  - b) Designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles;
  - c) Evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and
  - d) Disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter (the registrant's fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting; and
5. The registrant's other certifying officer and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of registrant's Board of Directors (or persons performing the equivalent functions):
  - a) All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize and report financial information; and
  - b) Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal control over financial reporting.

/s/ AMY E. HOOD

Amy E. Hood  
Executive Vice President and  
Chief Financial Officer

October 20, 2016

**CERTIFICATIONS PURSUANT TO  
SECTION 906 OF THE SARBANES-OXLEY ACT OF 2002  
(18 U.S.C. SECTION 1350)**

In connection with the Quarterly Report of Microsoft Corporation, a Washington corporation (the "Company"), on Form 10-Q for the quarter ended September 30, 2016, as filed with the Securities and Exchange Commission (the "Report"), Satya Nadella, Chief Executive Officer of the Company, does hereby certify, pursuant to § 906 of the Sarbanes-Oxley Act of 2002 (18 U.S.C. § 1350), that to his knowledge:

- (1) The Report fully complies with the requirements of section 13(a) or 15(d) of the Securities Exchange Act of 1934; and
- (2) The information contained in the Report fairly presents, in all material respects, the financial condition and results of operations of the Company.

/s/ SATYA NADELLA

\_\_\_\_\_  
Satya Nadella  
Chief Executive Officer

October 20, 2016

[A signed original of this written statement required by Section 906 has been provided to Microsoft Corporation and will be retained by Microsoft Corporation and furnished to the Securities and Exchange Commission or its staff upon request.]

**CERTIFICATIONS PURSUANT TO  
SECTION 906 OF THE SARBANES-OXLEY ACT OF 2002  
(18 U.S.C. SECTION 1350)**

In connection with the Quarterly Report of Microsoft Corporation, a Washington corporation (the "Company"), on Form 10-Q for the quarter ended September 30, 2016, as filed with the Securities and Exchange Commission (the "Report"), Amy E. Hood, Chief Financial Officer of the Company, does hereby certify, pursuant to § 906 of the Sarbanes-Oxley Act of 2002 (18 U.S.C. § 1350), that to her knowledge:

- (1) The Report fully complies with the requirements of section 13(a) or 15(d) of the Securities Exchange Act of 1934; and
- (2) The information contained in the Report fairly presents, in all material respects, the financial condition and results of operations of the Company.

/s/ AMY E. HOOD

\_\_\_\_\_  
Amy E. Hood  
Executive Vice President and  
Chief Financial Officer

October 20, 2016

[A signed original of this written statement required by Section 906 has been provided to Microsoft Corporation and will be retained by Microsoft Corporation and furnished to the Securities and Exchange Commission or its staff upon request.]