

APPLE INC  
Form 10-Q  
May 03, 2017

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

FORM 10-Q

(Mark One)

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

For the quarterly period ended April 1, 2017

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: 001-36743

Apple Inc.  
(Exact name of Registrant as specified in its charter)

California 94-2404110  
(State or other jurisdiction (I.R.S. Employer Identification No.)  
of incorporation or organization)

1 Infinite Loop 95014  
Cupertino, California  
(Address of principal executive offices) (Zip Code)

(408) 996-1010  
(Registrant's telephone number, including area code)

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, smaller reporting company, or an emerging growth company. See the definitions of "large accelerated filer," "accelerated filer," "smaller reporting company," and "emerging growth 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  
Emerging growth company

If an emerging growth company, indicate by check mark if the Registrant has elected not to use the extended transition period for complying with any new or revised financial accounting standards provided pursuant to Section 13(a) of the Exchange Act.

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Indicate by check mark whether the Registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act).

Yes      No

5,213,840,000 shares of common stock, par value \$0.00001 per share, issued and outstanding as of April 21, 2017

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Apple Inc.  
 Form 10-Q  
 For the Fiscal Quarter Ended April 1, 2017  
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## PART I — FINANCIAL INFORMATION

## Item 1. Financial Statements

Apple Inc.

## CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS (Unaudited)

(In millions, except number of shares which are reflected in thousands and per share amounts)

	Three Months Ended		Six Months Ended	
	April 1, 2017	March 26, 2016	April 1, 2017	March 26, 2016
Net sales	\$52,896	\$ 50,557	\$131,247	\$126,429
Cost of sales	32,305	30,636	80,480	76,085
Gross margin	20,591	19,921	50,767	50,344
Operating expenses:				
Research and development	2,776	2,511	5,647	4,915
Selling, general and administrative	3,718	3,423	7,664	7,271
Total operating expenses	6,494	5,934	13,311	12,186
Operating income	14,097	13,987	37,456	38,158
Other income/(expense), net	587	155	1,408	557
Income before provision for income taxes	14,684	14,142	38,864	38,715
Provision for income taxes	3,655	3,626	9,944	9,838
Net income	\$11,029	\$ 10,516	\$28,920	\$28,877
Earnings per share:				
Basic	\$2.11	\$ 1.91	\$5.50	\$5.22
Diluted	\$2.10	\$ 1.90	\$5.46	\$5.19
Shares used in computing earnings per share:				
Basic	5,225,791	5,514,381	5,262,226	5,536,656
Diluted	5,261,688	5,540,886	5,294,841	5,567,506
Cash dividends declared per share	\$0.57	\$ 0.52	\$1.14	\$1.04

See accompanying Notes to Condensed Consolidated Financial Statements.

Apple Inc.

## CONDENSED CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME (Unaudited)

(In millions)

	Three Months Ended		Six Months Ended	
	April 1, 2017	March 26, 2016	April 1, 2017	March 26, 2016
Net income	\$11,029	\$10,516	\$28,920	\$28,877
Other comprehensive income/(loss):				
Change in foreign currency translation, net of tax effects of \$(44), \$(19), \$32 and \$0, respectively	214	120	(161	) 18
Change in unrealized gains/losses on derivative instruments:				
Change in fair value of derivatives, net of tax benefit/(expense) of \$(25), \$1, \$(253) and \$(37), respectively	(300	) (178	) 1,168	109
Adjustment for net (gains)/losses realized and included in net income, net of tax expense/(benefit) of \$311, \$144, \$100 and \$210, respectively	(1,032	) (528	) (726	) (973
Total change in unrealized gains/losses on derivative instruments, net of tax	(1,332	) (706	) 442	(864
Change in unrealized gains/losses on marketable securities:				
Change in fair value of marketable securities, net of tax benefit/(expense) of \$(256), \$(530), \$733 and \$(22), respectively	464	969	(1,344	) 47
Adjustment for net (gains)/losses realized and included in net income, net of tax expense/(benefit) of \$7, \$(27), \$(4) and \$(53), respectively	(13	) 49	7	96
Total change in unrealized gains/losses on marketable securities, net of tax	451	1,018	(1,337	) 143
Total other comprehensive income/(loss)	(667	) 432	(1,056	) (703
Total comprehensive income	\$10,362	\$10,948	\$27,864	\$28,174
See accompanying Notes to Condensed Consolidated Financial Statements.				

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Apple Inc.

## CONDENSED CONSOLIDATED BALANCE SHEETS (Unaudited)

(In millions, except number of shares which are reflected in thousands and par value)

	April 1, 2017	September 24, 2016
<b>ASSETS:</b>		
Current assets:		
Cash and cash equivalents	\$ 15,157	\$ 20,484
Short-term marketable securities	51,944	46,671
Accounts receivable, less an allowance of \$53 at each period end	11,579	15,754
Inventories	2,910	2,132
Vendor non-trade receivables	9,033	13,545
Other current assets	11,367	8,283
Total current assets	101,990	106,869
Long-term marketable securities	189,740	170,430
Property, plant and equipment, net	27,163	27,010
Goodwill	5,473	5,414
Acquired intangible assets, net	2,617	3,206
Other non-current assets	7,549	8,757
Total assets	\$ 334,532	\$ 321,686
<b>LIABILITIES AND SHAREHOLDERS' EQUITY:</b>		
Current liabilities:		
Accounts payable	\$ 28,573	\$ 37,294
Accrued expenses	23,096	22,027
Deferred revenue	7,682	8,080
Commercial paper	9,992	8,105
Current portion of long-term debt	3,999	3,500
Total current liabilities	73,342	79,006
Deferred revenue, non-current	3,107	2,930
Long-term debt	84,531	75,427
Other non-current liabilities	39,470	36,074
Total liabilities	200,450	193,437
Commitments and contingencies		
Shareholders' equity:		
Common stock and additional paid-in capital, \$0.00001 par value: 12,600,000 shares authorized; 5,205,815 and 5,336,166 shares issued and outstanding, respectively	33,579	31,251
Retained earnings	100,925	96,364
Accumulated other comprehensive income/(loss)	(422 )	634
Total shareholders' equity	134,082	128,249
Total liabilities and shareholders' equity	\$ 334,532	\$ 321,686
See accompanying Notes to Condensed Consolidated Financial Statements.		

Apple Inc.  
 CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS (Unaudited)  
 (In millions)

	Six Months Ended	
	April 1, 2017	March 26, 2016
Cash and cash equivalents, beginning of the period	\$20,484	\$21,120
Operating activities:		
Net income	28,920	28,877
Adjustments to reconcile net income to cash generated by operating activities:		
Depreciation and amortization	5,319	5,431
Share-based compensation expense	2,473	2,126
Deferred income tax expense	2,822	3,092
Other	(209)	) 308
Changes in operating assets and liabilities:		
Accounts receivable, net	4,183	4,538
Inventories	(778)	) 68
Vendor non-trade receivables	4,512	5,899
Other current and non-current assets	(896)	) 186
Accounts payable	(6,862)	) (9,388)
Deferred revenue	(221)	) 219
Other current and non-current liabilities	316	(2,292)
Cash generated by operating activities	39,579	39,064
Investing activities:		
Purchases of marketable securities	(99,821)	) (86,242)
Proceeds from maturities of marketable securities	12,429	9,148
Proceeds from sales of marketable securities	60,454	50,051
Payments made in connection with business acquisitions, net	(67)	) (140)
Payments for acquisition of property, plant and equipment	(6,309)	) (5,948)
Payments for acquisition of intangible assets	(126)	) (657)
Payments for strategic investments	—	(126)
Other	116	(196)
Cash used in investing activities	(33,324)	) (34,110)
Financing activities:		
Proceeds from issuance of common stock	273	247
Excess tax benefits from equity awards	225	264
Payments for taxes related to net share settlement of equity awards	(788)	) (751)
Payments for dividends and dividend equivalents	(6,134)	) (5,871)
Repurchases of common stock	(18,012)	) (13,530)
Proceeds from issuance of term debt, net	10,975	15,584
Change in commercial paper, net	1,879	(503)
Cash used in financing activities	(11,582)	) (4,560)
Increase/(Decrease) in cash and cash equivalents	(5,327)	) 394
Cash and cash equivalents, end of the period	\$15,157	\$21,514
Supplemental cash flow disclosure:		
Cash paid for income taxes, net	\$6,878	\$6,630
Cash paid for interest	\$1,007	\$565

See accompanying Notes to Condensed Consolidated Financial Statements.





Apple Inc.

Notes to Condensed Consolidated Financial Statements (Unaudited)

Note 1 – Summary of Significant Accounting Policies

Apple Inc. and its wholly-owned subsidiaries (collectively “Apple” or the “Company”) designs, manufactures and markets mobile communication and media devices and personal computers, and sells a variety of related software, services, accessories, networking solutions and third-party digital content and applications. The Company’s products and services include iPhone®, iPad®, Mac®, Apple Watch®, Apple TV®, a portfolio of consumer and professional software applications, iOS, macOS®, watchOS® and tvOS™ operating systems, iCloud®, Apple Pay® and a variety of accessory, service and support offerings. The Company sells and delivers digital content and applications through the iTunes Store®, App Store®, Mac App Store, TV App Store, iBooks Store™ and Apple Music® (collectively “Digital Content and Services”). The Company sells its products worldwide through its retail stores, online stores and direct sales force, as well as through third-party cellular network carriers, wholesalers, retailers and value-added resellers. In addition, the Company sells a variety of third-party Apple-compatible products, including application software and various accessories through its retail and online stores. The Company sells to consumers, small and mid-sized businesses and education, enterprise and government customers.

Basis of Presentation and Preparation

The accompanying condensed consolidated financial statements include the accounts of the Company. Intercompany accounts and transactions have been eliminated. In the opinion of the Company’s management, the condensed consolidated financial statements reflect all adjustments, which are normal and recurring in nature, necessary for fair financial statement presentation. The preparation of these condensed consolidated financial statements in conformity with U.S. generally accepted accounting principles (“GAAP”) requires management to make estimates and assumptions that affect the amounts reported in these condensed consolidated financial statements and accompanying notes. Actual results could differ materially from those estimates. Certain prior period amounts in the condensed consolidated financial statements have been reclassified to conform to the current period’s presentation. These condensed consolidated financial statements and accompanying notes should be read in conjunction with the Company’s annual consolidated financial statements and the notes thereto included in its Annual Report on Form 10-K for the fiscal year ended September 24, 2016 (the “2016 Form 10-K”).

The Company’s fiscal year is the 52 or 53-week period that ends on the last Saturday of September. The Company’s fiscal year 2017 will include 53 weeks and ends on September 30, 2017 and its fiscal year 2016 included 52 weeks and ended on September 24, 2016. A 14th week was included in the first quarter of 2017, as is done every five or six years, to realign fiscal quarters with calendar quarters. Unless otherwise stated, references to particular years, quarters, months and periods refer to the Company’s fiscal years ended in September and the associated quarters, months and periods of those fiscal years.

Earnings Per Share

Basic earnings per share is computed by dividing income available to common shareholders by the weighted-average number of shares of common stock outstanding during the period. Diluted earnings per share is computed by dividing income available to common shareholders by the weighted-average number of shares of common stock outstanding during the period increased to include the number of additional shares of common stock that would have been outstanding if the potentially dilutive securities had been issued. Potentially dilutive securities include outstanding stock options, shares to be purchased by employees under the Company’s employee stock purchase plan, unvested restricted stock and unvested restricted stock units (“RSUs”). The dilutive effect of potentially dilutive securities is reflected in diluted earnings per share by application of the treasury stock method. Under the treasury stock method, an increase in the fair market value of the Company’s common stock can result in a greater dilutive effect from potentially dilutive securities.

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The following table shows the computation of basic and diluted earnings per share for the three- and six-month periods ended April 1, 2017 and March 26, 2016 (net income in millions and shares in thousands):

	Three Months Ended		Six Months Ended	
	April 1, 2017	March 26, 2016	April 1, 2017	March 26, 2016
Numerator:				
Net income	\$ 11,029	\$ 10,516	\$ 28,920	\$ 28,877
Denominator:				
Weighted-average shares outstanding	5,225,791	5,143,381	5,262,226	5,536,656
Effect of dilutive securities	35,897	26,505	32,615	30,850
Weighted-average diluted shares	5,261,688	5,540,886	5,294,841	5,567,506

Basic earnings per share	\$ 2.11	\$ 1.91	\$ 5.50	\$ 5.22
Diluted earnings per share	\$ 2.10	\$ 1.90	\$ 5.46	\$ 5.19

Potentially dilutive securities whose effect would have been antidilutive are excluded from the computation of diluted earnings per share.

Note 2 – Financial Instruments

Cash, Cash Equivalents and Marketable Securities

The following tables show the Company's cash and available-for-sale securities by significant investment category as of April 1, 2017 and September 24, 2016 (in millions):

	April 1, 2017				Cash and Cash Equivalents	Short-Term Marketable Securities	Long-Term Marketable Securities
	Adjusted Cost	Unrealized Gains	Unrealized Losses	Fair Value			
Cash	\$ 7,600	\$ —	\$ —	\$ 7,600	\$ 7,600	\$ —	\$ —
Level 1 <sup>(1)</sup> :							
Money market funds	2,742	—	—	2,742	2,742	—	—
Mutual funds	997	—	(120)	877	—	877	—
Subtotal	3,739	—	(120)	3,619	2,742	877	—
Level 2 <sup>(2)</sup> :							
U.S. Treasury securities	53,365	65	(300)	53,130	2,280	16,067	34,783
U.S. agency securities	5,680	3	(10)	5,673	687	3,687	1,299
Non-U.S. government securities	7,151	135	(67)	7,219	—	193	7,026
Certificates of deposit and time deposits	6,386	—	—	6,386	921	4,665	800
Commercial paper	3,233	—	—	3,233	877	2,356	—
Corporate securities	147,939	643	(449)	148,133	50	23,992	124,091
Municipal securities	950	3	(3)	950	—	77	873
Mortgage- and asset-backed securities	21,086	31	(219)	20,898	—	30	20,868
Subtotal	245,790	880	(1,048)	245,622	4,815	51,067	189,740
Total	\$ 257,129	\$ 880	\$ (1,168)	\$ 256,841	\$ 15,157	\$ 51,944	\$ 189,740



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September 24, 2016

	Adjusted Cost	Unrealized Gains	Unrealized Losses	Fair Value	Cash and Cash Equivalents	Short-Term Marketable Securities	Long-Term Marketable Securities
Cash	\$8,601	\$ —	\$ —	\$8,601	\$ 8,601	\$ —	\$ —
Level 1 <sup>(1)</sup> :							
Money market funds	3,666	—	—	3,666	3,666	—	—
Mutual funds	1,407	—	(146 )	1,261	—	1,261	—
Subtotal	5,073	—	(146 )	4,927	3,666	1,261	—
Level 2 <sup>(2)</sup> :							
U.S. Treasury securities	41,697	319	(4 )	42,012	1,527	13,492	26,993
U.S. agency securities	7,543	16	—	7,559	2,762	2,441	2,356
Non-U.S. government securities	7,609	259	(27 )	7,841	110	818	6,913
Certificates of deposit and time deposits	6,598	—	—	6,598	1,108	3,897	1,593
Commercial paper	7,433	—	—	7,433	2,468	4,965	—
Corporate securities	131,166	1,409	(206 )	132,369	242	19,599	112,528
Municipal securities	956	5	—	961	—	167	794
Mortgage- and asset-backed securities	19,134	178	(28 )	19,284	—	31	19,253
Subtotal	222,136	2,186	(265 )	224,057	8,217	45,410	170,430
Total	\$235,810	\$ 2,186	\$ (411 )	\$237,585	\$ 20,484	\$ 46,671	\$ 170,430

(1) Level 1 fair value estimates are based on quoted prices in active markets for identical assets or liabilities.

(2) Level 2 fair value estimates are based on observable inputs other than quoted prices in active markets for identical assets and liabilities, quoted prices for identical or similar assets or liabilities in inactive markets, or other inputs that are observable or can be corroborated by observable market data for substantially the full term of the assets or liabilities.

The Company may sell certain of its marketable securities prior to their stated maturities for strategic reasons including, but not limited to, anticipation of credit deterioration and duration management. The maturities of the Company's long-term marketable securities generally range from one to five years.

The Company considers the declines in market value of its marketable securities investment portfolio to be temporary in nature. The Company typically invests in highly-rated securities, and its investment policy generally limits the amount of credit exposure to any one issuer. The policy generally requires investments to be investment grade, with the primary objective of minimizing the potential risk of principal loss. Fair values were determined for each individual security in the investment portfolio. When evaluating an investment for other-than-temporary impairment, the Company reviews factors such as the length of time and extent to which fair value has been below its cost basis, the financial condition of the issuer and any changes thereto, changes in market interest rates and the Company's intent to sell, or whether it is more likely than not it will be required to sell the investment before recovery of the investment's cost basis. As of April 1, 2017, the Company does not consider any of its investments to be other-than-temporarily impaired.

#### Derivative Financial Instruments

The Company may use derivatives to partially offset its business exposure to foreign currency and interest rate risk on expected future cash flows, on net investments in certain foreign subsidiaries and on certain existing assets and liabilities. However, the Company may choose not to hedge certain exposures for a variety of reasons including, but not limited to, accounting considerations and the prohibitive economic cost of hedging particular exposures. There can

be no assurance the hedges will offset more than a portion of the financial impact resulting from movements in foreign currency exchange or interest rates.

To help protect gross margins from fluctuations in foreign currency exchange rates, certain of the Company's subsidiaries whose functional currency is the U.S. dollar may hedge a portion of forecasted foreign currency revenue, and subsidiaries whose functional currency is not the U.S. dollar and who sell in local currencies may hedge a portion of forecasted inventory purchases not denominated in the subsidiaries' functional currencies. The Company may enter into forward contracts, option contracts or other instruments to manage this risk and may designate these instruments as cash flow hedges. The Company typically hedges portions of its forecasted foreign currency exposure associated with revenue and inventory purchases, typically for up to 12 months.

To help protect the net investment in a foreign operation from adverse changes in foreign currency exchange rates, the Company may enter into foreign currency forward and option contracts to offset the changes in the carrying amounts of these investments due to fluctuations in foreign currency exchange rates. In addition, the Company may use non-derivative financial instruments, such as its foreign currency-denominated debt, as economic hedges of its net investments in certain foreign subsidiaries. In both of these cases, the Company designates these instruments as net investment hedges.

The Company may also enter into non-designated foreign currency contracts to partially offset the foreign currency exchange gains and losses generated by the remeasurement of certain assets and liabilities denominated in non-functional currencies.

The Company may enter into interest rate swaps, options, or other instruments to manage interest rate risk. These instruments may offset a portion of changes in income or expense, or changes in fair value of the Company's term debt or investments. The Company designates these instruments as either cash flow or fair value hedges. The Company's hedged interest rate transactions as of April 1, 2017 are expected to be recognized within 10 years.

#### Cash Flow Hedges

The effective portions of cash flow hedges are recorded in accumulated other comprehensive income ("AOCI") until the hedged item is recognized in earnings. Deferred gains and losses associated with cash flow hedges of foreign currency revenue are recognized as a component of net sales in the same period as the related revenue is recognized, and deferred gains and losses related to cash flow hedges of inventory purchases are recognized as a component of cost of sales in the same period as the related costs are recognized. Deferred gains and losses associated with cash flow hedges of interest income or expense are recognized in other income/(expense), net in the same period as the related income or expense is recognized. The ineffective portions and amounts excluded from the effectiveness testing of cash flow hedges are recognized in other income/(expense), net.

Derivative instruments designated as cash flow hedges must be de-designated as hedges when it is probable the forecasted hedged transaction will not occur in the initially identified time period or within a subsequent two-month time period. Deferred gains and losses in AOCI associated with such derivative instruments are reclassified immediately into other income/(expense), net. Any subsequent changes in fair value of such derivative instruments are reflected in other income/(expense), net unless they are re-designated as hedges of other transactions.

#### Net Investment Hedges

The effective portions of net investment hedges are recorded in other comprehensive income ("OCI") as a part of the cumulative translation adjustment. The ineffective portions and amounts excluded from the effectiveness testing of net investment hedges are recognized in other income/(expense), net.

#### Fair Value Hedges

Gains and losses related to changes in fair value hedges are recognized in earnings along with a corresponding loss or gain related to the change in value of the underlying hedged item.

#### Non-Designated Derivatives

Derivatives that are not designated as hedging instruments are adjusted to fair value through earnings in the financial statement line item to which the derivative relates. As a result, during the three- and six-month periods ended April 1, 2017, respectively, the Company recognized a loss of \$67 million and a gain of \$206 million in net sales, a loss of \$253 million and a gain of \$79 million in cost of sales and a loss of \$76 million and a gain of \$432 million in other income/(expense), net.

The Company records all derivatives in the Condensed Consolidated Balance Sheets at fair value. The Company's accounting treatment for these derivative instruments is based on its hedge designation. The following tables show the Company's derivative instruments at gross fair value as of April 1, 2017 and September 24, 2016 (in millions):

April 1, 2017		
Fair Value	Fair Value of Derivatives Not Designated as Hedge Instruments	Total Fair Value
Derivative assets	Derivative liabilities	Net

Derivative assets <sup>(1)</sup>:

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Foreign exchange contracts	\$ 691	\$	272		\$ 963
Interest rate contracts	\$ 161	\$	—		\$ 161
Derivative liabilities <sup>(2)</sup> :					
Foreign exchange contracts	\$ 832	\$	245		\$ 1,077
Interest rate contracts	\$ 354	\$	—		\$ 354

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	September 24, 2016		
	Fair		
	Value of	Fair Value of	Total
	of	Derivatives Not Designated	Fair Value
	Derivatives	as Hedge Instruments	
	as Hedge Instruments		
Derivative assets <sup>(1)</sup> :			
Foreign exchange contracts	\$ 518	\$ 153	\$ 671
Interest rate contracts	\$ 728	\$ —	\$ 728
Derivative liabilities <sup>(2)</sup> :			
Foreign exchange contracts	\$ 935	\$ 134	\$ 1,069
Interest rate contracts	\$ 7	\$ —	\$ 7

(1) The fair value of derivative assets is measured using Level 2 fair value inputs and is recorded as other current assets in the Condensed Consolidated Balance Sheets.

(2) The fair value of derivative liabilities is measured using Level 2 fair value inputs and is recorded as accrued expenses in the Condensed Consolidated Balance Sheets.

The following table shows the pre-tax gains and losses of the Company's derivative and non-derivative instruments designated as cash flow, net investment and fair value hedges in OCI and the Condensed Consolidated Statements of Operations for the three- and six-month periods ended April 1, 2017 and March 26, 2016 (in millions):

	Three Months Ended		Six Months Ended	
	April 1,	March 26,	April 1,	March 26,
	2017	2016	2017	2016
Gains/(Losses) recognized in OCI – effective portion:				
Cash flow hedges:				
Foreign exchange contracts	\$ (317 )	\$ (138 )	\$ 1,410	\$ 188
Interest rate contracts	2	(50 )	9	(42 )
Total	\$ (315 )	\$ (188 )	\$ 1,419	\$ 146
Net investment hedges:				
Foreign exchange contracts	\$ —	\$ —	\$ —	\$ —
Foreign currency debt	(85 )	(87 )	37	(77 )
Total	\$ (85 )	\$ (87 )	\$ 37	\$ (77 )
Gains/(Losses) reclassified from AOCI into net income – effective portion:				
Cash flow hedges:				
Foreign exchange contracts	\$ 1,344	\$ 668	\$ 833	\$ 1,183
Interest rate contracts	(2 )	(3 )	(3 )	(7 )
Total	\$ 1,342	\$ 665	\$ 830	\$ 1,176
Gains/(Losses) on derivative instruments:				
Fair value hedges:				
Interest rate contracts	\$ (50 )	\$ 250	\$ (922 )	\$ 139
Gains/(Losses) related to hedged items:				
Fair value hedges:				
Interest rate contracts	\$ 50	\$ (250 )	\$ 922	\$ (139 )





The following table shows the notional amounts of the Company's outstanding derivative instruments and credit risk amounts associated with outstanding or unsettled derivative instruments as of April 1, 2017 and September 24, 2016 (in millions):

	April 1, 2017		September 24, 2016	
	Notional Credit Risk Amount	Notional Credit Risk Amount	Notional Credit Risk Amount	Notional Credit Risk Amount
Instruments designated as accounting hedges:				
Foreign exchange contracts	\$37,550	\$ 691	\$44,678	\$ 518
Interest rate contracts	\$31,000	\$ 161	\$24,500	\$ 728

Instruments not designated as accounting hedges:

Foreign exchange contracts	\$50,573	\$ 272	\$54,305	\$ 153
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The notional amounts for outstanding derivative instruments provide one measure of the transaction volume outstanding and do not represent the amount of the Company's exposure to credit or market loss. The credit risk amounts represent the Company's gross exposure to potential accounting loss on derivative instruments that are outstanding or unsettled if all counterparties failed to perform according to the terms of the contract, based on then-current currency or interest rates at each respective date. The Company's exposure to credit loss and market risk will vary over time as currency and interest rates change. Although the table above reflects the notional and credit risk amounts of the Company's derivative instruments, it does not reflect the gains or losses associated with the exposures and transactions that the instruments are intended to hedge. The amounts ultimately realized upon settlement of these financial instruments, together with the gains and losses on the underlying exposures, will depend on actual market conditions during the remaining life of the instruments.

The Company generally enters into master netting arrangements, which are designed to reduce credit risk by permitting net settlement of transactions with the same counterparty. To further limit credit risk, the Company generally enters into collateral security arrangements that provide for collateral to be received or posted when the net fair value of certain financial instruments fluctuates from contractually established thresholds. The Company presents its derivative assets and derivative liabilities at their gross fair values in its Condensed Consolidated Balance Sheets. As of April 1, 2017, the net cash collateral posted by the Company related to derivative instruments under its collateral security arrangements was \$230 million, which was recorded as other current assets in the Condensed Consolidated Balance Sheet. As of September 24, 2016, the net cash collateral received by the Company related to derivative instruments under its collateral security arrangements was \$163 million, which was recorded as accrued expenses in the Condensed Consolidated Balance Sheet.

Under master netting arrangements with the respective counterparties to the Company's derivative contracts, the Company is allowed to net settle transactions with a single net amount payable by one party to the other. As of both April 1, 2017 and September 24, 2016, the potential effects of these rights of set-off associated with the Company's derivative contracts, including the effects of collateral, would be a reduction to both derivative assets and derivative liabilities of \$1.5 billion, resulting in a net derivative liability of \$77 million as of April 1, 2017 and a net derivative asset of \$160 million as of September 24, 2016.

Accounts Receivable

Trade Receivables

The Company has considerable trade receivables outstanding with its third-party cellular network carriers, wholesalers, retailers, value-added resellers, small and mid-sized businesses and education, enterprise and government customers. The Company generally does not require collateral from its customers; however, the Company will require collateral in certain instances to limit credit risk. In addition, when possible, the Company attempts to limit credit risk on trade receivables with credit insurance for certain customers or by requiring third-party financing, loans or leases to support credit exposure. These credit-financing arrangements are directly between the third-party financing company and the end customer. As such, the Company generally does not assume any recourse or credit risk sharing related to any of these arrangements.

As of April 1, 2017, the Company had two customers that individually represented 10% or more of total trade receivables, one of which accounted for 12% and the other 10%. As of September 24, 2016, the Company had one

customer that represented 10% or more of total trade receivables, which accounted for 10%. The Company's cellular network carriers accounted for 52% and 63% of trade receivables as of April 1, 2017 and September 24, 2016, respectively.

**Vendor Non-Trade Receivables**

The Company has non-trade receivables from certain of its manufacturing vendors resulting from the sale of components to these vendors who manufacture sub-assemblies or assemble final products for the Company. The Company purchases these components directly from suppliers. As of April 1, 2017, the Company had three vendors that individually accounted for 42%, 17% and 14% of total vendor non-trade receivables. As of September 24, 2016, the Company had two vendors that individually accounted for 47% and 21% of total vendor non-trade receivables.

## Note 3 – Condensed Consolidated Financial Statement Details

The following tables show the Company's condensed consolidated financial statement details as of April 1, 2017 and September 24, 2016 (in millions):

## Property, Plant and Equipment, Net

	April 1, 2017	September 24, 2016
Land and buildings	\$11,746	\$ 10,185
Machinery, equipment and internal-use software	46,688	44,543
Leasehold improvements	6,690	6,517
Gross property, plant and equipment	65,124	61,245
Accumulated depreciation and amortization	(37,961 )	(34,235 )
Total property, plant and equipment, net	\$27,163	\$ 27,010

## Other Non-Current Liabilities

	April 1, 2017	September 24, 2016
Deferred tax liabilities	\$28,226	\$ 26,019
Other non-current liabilities	11,244	10,055
Total other non-current liabilities	\$39,470	\$ 36,074

## Other Income/(Expense), Net

The following table shows the detail of other income/(expense), net for the three- and six-month periods ended April 1, 2017 and March 26, 2016 (in millions):

	Three Months Ended		Six Months Ended	
	April 1, 2017	March 26, 2016	April 1, 2017	March 26, 2016
Interest and dividend income	\$ 1,282	\$ 986	\$2,506	\$ 1,927
Interest expense	(530 )	(321 )	(1,055 )	(597 )
Other expense, net	(165 )	(510 )	(43 )	(773 )
Total other income/(expense), net	\$ 587	\$ 155	\$1,408	\$ 557

## Note 4 – Acquired Intangible Assets

The Company's acquired intangible assets with definite useful lives primarily consist of patents and licenses. The following table summarizes the components of acquired intangible asset balances as of April 1, 2017 and September 24, 2016 (in millions):

	April 1, 2017			September 24, 2016		
	Gross Carrying Amount	Accumulated Amortization	Net Carrying Amount	Gross Carrying Amount	Accumulated Amortization	Net Carrying Amount
Definite-lived and amortizable acquired intangible assets	\$7,258	\$ (4,741 )	\$ 2,517	\$8,912	\$ (5,806 )	\$ 3,106
Indefinite-lived and non-amortizable acquired intangible assets	100	—	100	100	—	100
Total acquired intangible assets	\$7,358	\$ (4,741 )	\$ 2,617	\$9,012	\$ (5,806 )	\$ 3,206

## Note 5 – Income Taxes

As of April 1, 2017, the Company recorded gross unrecognized tax benefits of \$8.8 billion, of which \$3.0 billion, if recognized, would affect the Company's effective tax rate. As of September 24, 2016, the total amount of gross unrecognized tax benefits was \$7.7 billion, of which \$2.8 billion, if recognized, would have affected the Company's effective tax rate. The Company's total gross unrecognized tax benefits are classified as other non-current liabilities in the Condensed Consolidated Balance Sheets. The Company had \$1.3 billion and \$1.0 billion of gross interest and penalties accrued as of April 1, 2017 and September 24, 2016, respectively, which are classified as other non-current liabilities in the Condensed Consolidated Balance Sheets.

The Company believes that an adequate provision has been made for any adjustments that may result from tax examinations. However, the outcome of tax audits cannot be predicted with certainty. If any issues addressed in the Company's tax audits are resolved in a manner not consistent with its expectations, the Company could be required to adjust its provision for income taxes in the period such resolution occurs. Although timing of the resolution and/or closure of audits is not certain, the Company believes it is reasonably possible that its gross unrecognized tax benefits could decrease (whether by payment, release or a combination of both) in the next 12 months by as much as \$1.3 billion.

On August 30, 2016, the European Commission announced its decision that Ireland granted state aid to the Company by providing tax opinions in 1991 and 2007 concerning the tax allocation of profits of the Irish branches of two subsidiaries of the Company (the "State Aid Decision"). The State Aid Decision orders Ireland to calculate and recover additional taxes from the Company for the period June 2003 through December 2014. Irish legislative changes, effective as of January 2015, eliminated the application of the tax opinions from that date forward. The Company believes the State Aid Decision to be without merit and appealed to the General Court of the Court of Justice of the European Union. Ireland has also appealed the State Aid Decision. While the European Commission announced a recovery amount of up to €13 billion, plus interest, the actual amount of additional taxes subject to recovery is to be calculated by Ireland in accordance with the European Commission's guidance. Once the recovery amount is computed by Ireland, the Company anticipates funding it, including interest, out of foreign cash into escrow, where it will remain pending conclusion of all appeals. The Company believes that any incremental Irish corporate income taxes potentially due related to the State Aid Decision would be creditable against U.S. taxes.

## Note 6 – Debt

## Commercial Paper

The Company issues unsecured short-term promissory notes ("Commercial Paper") pursuant to a commercial paper program. The Company uses net proceeds from the commercial paper program for general corporate purposes, including dividends and share repurchases. As of April 1, 2017 and September 24, 2016, the Company had \$10.0 billion and \$8.1 billion of Commercial Paper outstanding, respectively, with maturities generally less than nine months. The weighted-average interest rate of the Company's Commercial Paper was 0.80% as of April 1, 2017 and 0.45% as of September 24, 2016.

The following table provides a summary of cash flows associated with the issuance and maturities of Commercial Paper for the six months ended April 1, 2017 and March 26, 2016 (in millions):

	Six Months Ended	
	April 1, 2017	March 26, 2016
Maturities less than 90 days:		
Proceeds from/(Repayments of) commercial paper, net	\$(1,318)	\$ 660
Maturities greater than 90 days:		
Proceeds from commercial paper	7,057	669
Repayments of commercial paper	(3,860 )	(1,832 )
Proceeds from/(Repayments of) commercial paper, net	3,197	(1,163 )
Total change in commercial paper, net	\$ 1,879	\$ (503 )



## Long-Term Debt

As of April 1, 2017, the Company had outstanding floating- and fixed-rate notes with varying maturities for an aggregate principal amount of \$88.9 billion (collectively the “Notes”). The Notes are senior unsecured obligations, and interest is payable in arrears, quarterly for the U.S. dollar-denominated and Australian dollar-denominated floating-rate notes, semi-annually for the U.S. dollar-denominated, Australian dollar-denominated, British pound-denominated and Japanese yen-denominated fixed-rate notes and annually for the euro-denominated and Swiss franc-denominated fixed-rate notes. The following table provides a summary of the Company’s term debt as of April 1, 2017 and September 24, 2016:

	April 1, 2017		September 24, 2016		
	Maturities	Amount (in millions)	Effective Interest Rate	Amount (in millions)	Effective Interest Rate
2013 debt issuance of \$17.0 billion:					
Floating-rate notes	2018	\$2,000	1.10%	\$2,000	1.10%
Fixed-rate 1.000% – 3.850% notes	2018–2043	12,500	1.08%–3.91%	12,500	1.08%–3.91%
2014 debt issuance of \$12.0 billion:					
Floating-rate notes	2017–2019	2,000	1.10%–1.33%	2,000	0.86%–1.09%
Fixed-rate 1.050% – 4.450% notes	2017–2044	10,000	1.10%–4.48%	10,000	0.85%–4.48%
2015 debt issuances of \$27.3 billion:					
Floating-rate notes	2017–2020	1,785	1.08%–1.87%	1,781	0.87%–1.87%
Fixed-rate 0.350% – 4.375% notes	2017–2045	24,668	0.28%–4.51%	25,144	0.28%–4.51%
2016 debt issuances of \$24.9 billion:					
Floating-rate notes	2019–2021	1,350	1.17%–2.18%	1,350	0.91%–1.95%
Fixed-rate 1.100% – 4.650% notes	2018–2046	23,616	1.13%–4.78%	23,609	1.13%–4.58%
Second quarter 2017 debt issuance of \$10.0 billion:					
Floating-rate notes	2019	500	1.12%	—	—%
Floating-rate notes	2020	500	1.24%	—	—%
Floating-rate notes	2022	1,000	1.54%	—	—%
Fixed-rate 1.550% notes	2019	500	1.59%	—	—%
Fixed-rate 1.900% notes	2020	1,000	1.24%	—	—%
Fixed-rate 2.500% notes	2022	1,500	1.53%	—	—%
Fixed-rate 3.000% notes	2024	1,750	1.83%	—	—%
Fixed-rate 3.350% notes	2027	2,250	1.98%	—	—%
Fixed-rate 4.250% notes	2047	1,000	4.26%	—	—%
Second quarter 2017 debt issuance of \$1.0 billion:					
Fixed-rate 4.300% notes	2047	1,000	4.30%	—	—%
Total term debt		88,919		78,384	
Unamortized premium/(discount) and issuance costs, net		(184)		(174)	
Hedge accounting fair value adjustments		(205)		717	
Less: Current portion of long-term debt		(3,999)		(3,500)	
Total long-term debt		\$84,531		\$75,427	

During the second quarter of 2017, the Company issued \$10.0 billion of U.S. dollar-denominated notes in the United States and \$1.0 billion of U.S. dollar-denominated notes in Taiwan. To manage interest rate risk on the fixed-rate notes maturing in 2020, 2022, 2024 and 2027, the Company entered into interest rate swaps with an aggregate notional amount of \$6.5 billion, which effectively converted the fixed interest rates on these notes to floating interest rates.

A portion of the Company's Japanese yen-denominated notes is designated as a hedge of the foreign currency exposure of the Company's net investment in a foreign operation. The foreign currency transaction gain or loss on the Japanese yen-denominated debt designated as a hedge is recorded in OCI as a part of the cumulative translation adjustment. As of April 1, 2017 and September 24, 2016, the carrying value of the debt designated as a net investment hedge was \$1.7 billion and \$1.9 billion, respectively. For further discussion regarding the Company's use of derivative instruments see the Derivative Financial Instruments section of Note 2, "Financial Instruments."



The effective interest rates for the Notes include the interest on the Notes, amortization of the discount and, if applicable, adjustments related to hedging. The Company recognized \$507 million and \$1.0 billion of interest expense on its term debt for the three- and six-month periods ended April 1, 2017, respectively. The Company recognized \$311 million and \$582 million of interest expense on its term debt for the three- and six-month periods ended March 26, 2016, respectively.

As of April 1, 2017 and September 24, 2016, the fair value of the Company's Notes, based on Level 2 inputs, was \$89.7 billion and \$81.7 billion, respectively.

#### Note 7 – Shareholders' Equity

##### Dividends

The Company declared and paid cash dividends per share during the periods presented as follows:

	Dividends Per Share	Amount (in millions)
2017:		
Second quarter	\$ 0.57	\$ 2,988
First quarter	0.57	3,042
Total cash dividends declared and paid	\$ 1.14	\$ 6,030

##### 2016:

Fourth quarter	\$ 0.57	\$ 3,071
Third quarter	0.57	3,117
Second quarter	0.52	2,879
First quarter	0.52	2,898
Total cash dividends declared and paid	\$ 2.18	\$ 11,965

Future dividends are subject to declaration by the Board of Directors.

##### Share Repurchase Program

As of April 1, 2017, the Company had an authorized share repurchase program of \$175 billion of the Company's common stock, of which \$151 billion had been utilized. The Company's share repurchase program does not obligate it to acquire any specific number of shares. Under the program, shares may be repurchased in privately negotiated and/or open market transactions, including under plans complying with Rule 10b5-1 under the Securities Exchange Act of 1934, as amended (the "Exchange Act").

The Company has entered, and in the future may enter, into accelerated share repurchase arrangements ("ASRs") with financial institutions. In exchange for up-front payments, the financial institutions deliver shares of the Company's common stock during the purchase periods of each ASR. The total number of shares ultimately delivered, and therefore the average repurchase price paid per share, is determined at the end of the applicable purchase period of each ASR based on the volume-weighted average price of the Company's common stock during that period. The shares received are retired in the periods they are delivered, and the up-front payments are accounted for as a reduction to shareholders' equity in the Company's Condensed Consolidated Balance Sheets in the periods the payments are made. The Company reflects the ASRs as a repurchase of common stock in the period delivered for purposes of calculating earnings per share and as forward contracts indexed to its own common stock. The ASRs met all of the applicable criteria for equity classification, and therefore were not accounted for as derivative instruments.

The following table shows the Company's ASR activity and related information during the six months ended April 1, 2017 and the year ended September 24, 2016:

	Purchase Period End Date	Number of Shares (in thousands)	Average Repurchase Price Per Share	ASR Amount (in millions)
February 2017 ASR	May 2017	17,527	(1) (1)	\$ 3,000
November 2016 ASR	February 2017	51,157	(2) \$ 117.29	\$ 6,000
August 2016 ASR	November 2016	26,850	\$ 111.73	\$ 3,000
May 2016 ASR	August 2016	60,452	\$ 99.25	\$ 6,000
November 2015 ASR	April 2016	29,122	\$ 103.02	\$ 3,000

"Number of Shares" represents those shares delivered at the beginning of the purchase period and does not represent the final number of shares to be delivered under the ASR. The total number of shares ultimately delivered, and (1) therefore the average repurchase price paid per share, will be determined at the end of the purchase period based on the volume-weighted average price of the Company's common stock during that period. The February 2017 ASR purchase period will end in May 2017.

Includes 44.8 million shares delivered and retired at the beginning of the purchase period, which began in the first (2) quarter of 2017 and 6.3 million shares delivered and retired at the end of the purchase period, which concluded in the second quarter of 2017.

Additionally, the Company repurchased shares of its common stock in the open market, which were retired upon repurchase, during the periods presented as follows:

	Number of Shares (in thousands)	Average Repurchase Price Per Share	Amount (in millions)
2017:			
Second quarter	31,070	\$ 128.74	\$ 4,001
First quarter	44,333	\$ 112.78	5,000
Total open market common stock repurchases	75,403		\$ 9,001
2016:			
Fourth quarter	28,579	\$ 104.97	\$ 3,000
Third quarter	41,238	\$ 97.00	4,000
Second quarter	71,766	\$ 97.54	7,000
First quarter	25,984	\$ 115.45	3,000
Total open market common stock repurchases	167,567		\$ 17,000

#### Note 8 – Comprehensive Income

Comprehensive income consists of two components, net income and OCI. OCI refers to revenue, expenses, and gains and losses that under GAAP are recorded as an element of shareholders' equity but are excluded from net income. The Company's OCI consists of foreign currency translation adjustments from those subsidiaries not using the U.S. dollar as their functional currency, net deferred gains and losses on certain derivative instruments accounted for as cash flow hedges and unrealized gains and losses on marketable securities classified as available-for-sale.

The following table shows the pre-tax amounts reclassified from AOCI into the Condensed Consolidated Statements of Operations, and the associated financial statement line item, for the three- and six-month periods ended April 1, 2017 and March 26, 2016 (in millions):

Comprehensive Income Components	Financial Statement Line Item	Three Months Ended		Six Months Ended	
		April 1, 2017	March 26, 2016	April 1, 2017	March 26, 2016
Unrealized (gains)/losses on derivative instruments:					
Foreign exchange contracts	Revenue	\$ (408 )	\$ (325 )	\$(509)	\$(654 )
	Cost of sales	(570 )	(219 )	(557 )	(525 )
	Other income/(expense), net	(367 )	(131 )	237	(11 )
Interest rate contracts	Other income/(expense), net	2	3	3	7
		(1,343 )	(672 )	(826 )	(1,183 )
Unrealized (gains)/losses on marketable securities	Other income/(expense), net	(20 )	76	11	149
Total amounts reclassified from AOCI		\$(1,363 )	\$(596 )	\$(815)	\$(1,034 )

The following table shows the changes in AOCI by component for the six months ended April 1, 2017 (in millions):

	Cumulative Foreign Currency Translation	Unrealized Gains/Losses on Derivative Instruments	Unrealized Gains/Losses on Marketable Securities	Total
Balance at September 24, 2016	\$ (578 )	\$ 38	\$ 1,174	\$634
Other comprehensive income/(loss) before reclassifications	(193 )	1,421	(2,077 )	(849 )
Amounts reclassified from AOCI	—	(826 )	11	(815 )
Tax effect	32	(153 )	729	608
Other comprehensive income/(loss)	(161 )	442	(1,337 )	(1,056)
Balance at April 1, 2017	\$ (739 )	\$ 480	\$ (163 )	\$(422)

#### Note 9 – Benefit Plans

##### Stock Plans

The Company had 317.4 million shares reserved for future issuance under its stock plans as of April 1, 2017. RSUs granted generally vest over four years, based on continued employment, and are settled upon vesting in shares of the Company's common stock on a one-for-one basis. Each share issued with respect to RSUs granted under the Company's stock plans reduces the number of shares available for grant under the plan by two shares. RSUs cancelled and shares withheld to satisfy tax withholding obligations increase the number of shares available for grant under the plans utilizing a factor of two times the number of RSUs cancelled or shares withheld.

##### Rule 10b5-1 Trading Plans

During the three months ended April 1, 2017, Section 16 officers Angela Ahrendts, Timothy D. Cook, Luca Maestri, Daniel Riccio and Philip Schiller had equity trading plans in place in accordance with Rule 10b5-1(c)(1) under the Exchange Act. An equity trading plan is a written document that pre-establishes the amounts, prices and dates (or formula for determining the amounts, prices and dates) of future purchases or sales of the Company's stock, including shares acquired pursuant to the Company's employee and director equity plans.

## Restricted Stock Units

A summary of the Company's RSU activity and related information for the six months ended April 1, 2017 is as follows:

	Number of RSUs (in thousands)	Weighted-Average Grant Date Fair Value Per Share	Aggregate Fair Value (in millions)
Balance at September 24, 2016	99,089	\$ 97.54	
RSUs granted	45,313	\$ 118.36	
RSUs vested	(21,942 )	\$ 92.65	
RSUs cancelled	(3,227 )	\$ 105.68	
Balance at April 1, 2017	119,233	\$ 106.13	\$ 17,129

RSUs that vested during the three- and six-month periods ended April 1, 2017 had fair values of \$460 million and \$2.6 billion, respectively, as of the vesting date. RSUs that vested during the three- and six-month periods ended March 26, 2016 had fair values of \$450 million and \$2.5 billion, respectively, as of the vesting date.

## Share-Based Compensation

The following table shows a summary of the share-based compensation expense included in the Condensed Consolidated Statements of Operations for the three- and six-month periods ended April 1, 2017 and March 26, 2016 (in millions):

	Three Months Ended		Six Months Ended	
	April 1, 2017	March 26, 2016	April 1, 2017	March 26, 2016
Cost of sales	\$ 217	\$ 191	\$446	\$ 395
Research and development	575	468	1,164	934
Selling, general and administrative	425	389	863	797
Total share-based compensation expense	\$ 1,217	\$ 1,048	\$2,473	\$ 2,126

The income tax benefit related to share-based compensation expense was \$424 million and \$889 million for the three- and six-month periods ended April 1, 2017, respectively, and was \$347 million and \$760 million for the three- and six-month periods ended March 26, 2016, respectively. As of April 1, 2017, the total unrecognized compensation cost related to outstanding RSUs, restricted stock and stock options was \$10.0 billion, which the Company expects to recognize over a weighted-average period of 2.8 years.

## Note 10 – Commitments and Contingencies

## Accrued Warranty and Indemnification

The following table shows changes in the Company's accrued warranties and related costs for the three- and six-month periods ended April 1, 2017 and March 26, 2016 (in millions):

	Three Months Ended		Six Months Ended	
	April 1, 2017	March 26, 2016	April 1, 2017	March 26, 2016
Beginning accrued warranty and related costs	\$ 4,698	\$ 5,236	\$3,702	\$ 4,780
Cost of warranty claims	(1,031 )	(1,128 )	(2,368 )	(2,397 )
Accruals for product warranty	1,068	877	3,401	2,602
Ending accrued warranty and related costs	\$ 4,735	\$ 4,985	\$4,735	\$ 4,985

The Company generally does not indemnify end-users of its operating system and application software against legal claims that the software infringes third-party intellectual property rights. Other agreements entered into by the Company sometimes include indemnification provisions under which the Company could be subject to costs and/or damages in the event of an infringement claim against the Company or an indemnified third party. In the opinion of management, there was not at least a reasonable possibility the Company may have incurred a material loss with respect to indemnification of end-users of its operating system or application software for infringement of third-party intellectual property rights.



The Company offers an iPhone Upgrade Program, which is available to customers who purchase a qualifying iPhone in the U.S., the U.K. and mainland China. The iPhone Upgrade Program provides customers the right to trade in that iPhone for a specified amount when purchasing a new iPhone, provided certain conditions are met. The Company accounts for the trade-in right as a guarantee liability and recognizes arrangement revenue net of the fair value of such right with subsequent changes to the guarantee liability recognized within revenue.

The Company has entered into indemnification agreements with its directors and executive officers. Under these agreements, the Company has agreed to indemnify such individuals to the fullest extent permitted by law against liabilities that arise by reason of their status as directors or officers and to advance expenses incurred by such individuals in connection with related legal proceedings. It is not possible to determine the maximum potential amount of payments the Company could be required to make under these agreements due to the limited history of prior indemnification claims and the unique facts and circumstances involved in each claim. However, the Company maintains directors and officers liability insurance coverage to reduce its exposure to such obligations.

#### Concentrations in the Available Sources of Supply of Materials and Product

Although most components essential to the Company's business are generally available from multiple sources, a number of components are currently obtained from single or limited sources. In addition, the Company competes for various components with other participants in the markets for mobile communication and media devices and personal computers. Therefore, many components used by the Company, including those that are available from multiple sources, are at times subject to industry-wide shortage and significant pricing fluctuations that could materially adversely affect the Company's financial condition and operating results.

The Company uses some custom components that are not commonly used by its competitors, and new products introduced by the Company often utilize custom components available from only one source. When a component or product uses new technologies, initial capacity constraints may exist until the suppliers' yields have matured or manufacturing capacity has increased. If the Company's supply of components for a new or existing product were delayed or constrained, or if an outsourcing partner delayed shipments of completed products to the Company, the Company's financial condition and operating results could be materially adversely affected. The Company's business and financial performance could also be materially adversely affected depending on the time required to obtain sufficient quantities from the original source, or to identify and obtain sufficient quantities from an alternative source. Continued availability of these components at acceptable prices, or at all, may be affected if those suppliers decide to concentrate on the production of common components instead of components customized to meet the Company's requirements.

The Company has entered into agreements for the supply of many components; however, there can be no guarantee that the Company will be able to extend or renew these agreements on similar terms, or at all. Therefore, the Company remains subject to significant risks of supply shortages and price increases that could materially adversely affect its financial condition and operating results.

Substantially all of the Company's hardware products are manufactured by outsourcing partners that are located primarily in Asia. A significant concentration of this manufacturing is currently performed by a small number of outsourcing partners, often in single locations. Certain of these outsourcing partners are the sole-sourced suppliers of components and manufacturers for many of the Company's products. Although the Company works closely with its outsourcing partners on manufacturing schedules, the Company's operating results could be adversely affected if its outsourcing partners were unable to meet their production commitments. The Company's manufacturing purchase obligations typically cover its requirements for periods up to 150 days.

#### Other Off-Balance Sheet Commitments

##### Operating Leases

The Company leases various equipment and facilities, including retail space, under noncancelable operating lease arrangements. The Company does not currently utilize any other off-balance sheet financing arrangements. As of April 1, 2017, the Company's total future minimum lease payments under noncancelable operating leases were \$8.2 billion. The Company's retail store and other facility leases are typically for terms not exceeding 10 years and generally contain multi-year renewal options.

##### Contingencies

The Company is subject to various legal proceedings and claims that have arisen in the ordinary course of business and that have not been fully adjudicated, as further discussed in Part II, Item 1 of this Form 10-Q under the heading “Legal Proceedings” and in Part II, Item 1A of this Form 10-Q under the heading “Risk Factors.” In the opinion of management, there was not at least a reasonable possibility the Company may have incurred a material loss, or a material loss in excess of a recorded accrual, with respect to loss contingencies for asserted legal and other claims. However, the outcome of litigation is inherently uncertain. Therefore, although management considers the likelihood of such an outcome to be remote, if one or more of these legal matters were resolved against the Company in a reporting period for amounts in excess of management’s expectations, the Company’s consolidated financial statements for that reporting period could be materially adversely affected.

Apple Inc. v. Samsung Electronics Co., Ltd., et al.

On August 24, 2012, a jury returned a verdict awarding the Company \$1.05 billion in its lawsuit against Samsung Electronics Co., Ltd. and affiliated parties in the United States District Court, Northern District of California, San Jose Division. On March 6, 2014, the District Court entered final judgment in favor of the Company in the amount of approximately \$930 million. On May 18, 2015, the U.S. Court of Appeals for the Federal Circuit affirmed in part, and reversed in part, the decision of the District Court. As a result, the Court of Appeals ordered entry of final judgment on damages in the amount of approximately \$548 million, with the District Court to determine supplemental damages and interest, as well as damages owed for products subject to the reversal in part. Samsung paid \$548 million to the Company in December 2015, which was included in net sales in the Condensed Consolidated Statement of Operations. On December 6, 2016, the U.S. Supreme Court remanded the case to the U.S. Court of Appeals for the Federal Circuit for further proceedings related to the \$548 million in damages. On February 7, 2017, the U.S. Court of Appeals for the Federal Circuit remanded the case to the District Court to determine what additional proceedings, if any, are needed. Because the case remains subject to further proceedings, the Company has not recognized any further amounts in its results of operations.

Note 11 – Segment Information and Geographic Data

The Company reports segment information based on the “management” approach. The management approach designates the internal reporting used by management for making decisions and assessing performance as the source of the Company’s reportable operating segments.

The Company manages its business primarily on a geographic basis. The Company’s reportable operating segments consist of the Americas, Europe, Greater China, Japan and Rest of Asia Pacific. The Americas segment includes both North and South America. The Europe segment includes European countries, as well as India, the Middle East and Africa. The Greater China segment includes China, Hong Kong and Taiwan. The Rest of Asia Pacific segment includes Australia and those Asian countries not included in the Company’s other reportable operating segments. Although the reportable operating segments provide similar hardware and software products and similar services, each one is managed separately to better align with the location of the Company’s customers and distribution partners and the unique market dynamics of each geographic region. The accounting policies of the various segments are the same as those described in Note 1, “Summary of Significant Accounting Policies” of the Notes to Consolidated Financial Statements in Part II, Item 8 of the 2016 Form 10-K.

The Company evaluates the performance of its reportable operating segments based on net sales and operating income. Net sales for geographic segments are generally based on the location of customers and sales through the Company’s retail stores located in those geographic locations. Operating income for each segment includes net sales to third parties, related cost of sales and operating expenses directly attributable to the segment. Advertising expenses are generally included in the geographic segment in which the expenditures are incurred. Operating income for each segment excludes other income and expense and certain expenses managed outside the reportable operating segments. Costs excluded from segment operating income include various corporate expenses such as research and development, corporate marketing expenses, certain share-based compensation expenses, income taxes, various nonrecurring charges and other separately managed general and administrative costs. The Company does not include intercompany transfers between segments for management reporting purposes.



The following table shows information by reportable operating segment for the three- and six-month periods ended April 1, 2017 and March 26, 2016 (in millions):

	Three Months Ended		Six Months Ended	
	April 1, 2017	March 26, 2016	April 1, 2017	March 26, 2016
<b>Americas:</b>				
Net sales	\$21,157	\$ 19,096	\$53,125	\$ 48,421
Operating income	\$6,668	\$ 6,116	\$17,162	\$ 16,134
<b>Europe:</b>				
Net sales	\$12,733	\$ 11,535	\$31,254	\$ 29,467
Operating income	\$3,851	\$ 3,602	\$9,587	\$ 9,381
<b>Greater China:</b>				
Net sales	\$10,726	\$ 12,486	\$26,959	\$ 30,859
Operating income	\$4,224	\$ 4,818	\$10,400	\$ 12,394
<b>Japan:</b>				
Net sales	\$4,485	\$ 4,281	\$10,251	\$ 9,075
Operating income	\$2,037	\$ 1,930	\$4,710	\$ 4,170
<b>Rest of Asia Pacific:</b>				
Net sales	\$3,795	\$ 3,159	\$9,658	\$ 8,607
Operating income	\$1,309	\$ 1,095	\$3,538	\$ 3,127

A reconciliation of the Company's segment operating income to the Condensed Consolidated Statements of Operations for the three- and six-month periods ended April 1, 2017 and March 26, 2016 is as follows (in millions):

	Three Months Ended		Six Months Ended	
	April 1, 2017	March 26, 2016	April 1, 2017	March 26, 2016
Segment operating income	\$18,089	\$17,561	\$45,397	\$45,206
Research and development expense	(2,776 )	(2,511 )	(5,647 )	(4,915 )
Other corporate expenses, net	(1,216 )	(1,063 )	(2,294 )	(2,133 )
Total operating income	\$14,097	\$13,987	\$37,456	\$38,158

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

This section and other parts of this Quarterly Report on Form 10-Q contain forward-looking statements, within the meaning of the Private Securities Litigation Reform Act of 1995, that involve risks and uncertainties. Forward-looking statements provide current expectations of future events based on certain assumptions and include any statement that does not directly relate to any historical or current fact. Forward-looking statements can also be identified by words such as "future," "anticipates," "believes," "estimates," "expects," "intends," "plans," "predicts," "will," "would," "could," "can" or similar terms. Forward-looking statements are not guarantees of future performance and the Company's actual results may differ significantly from the results discussed in the forward-looking statements. Factors that might cause such differences include, but are not limited to, those discussed in Part II, Item 1A of this Form 10-Q under the heading "Risk Factors," which are incorporated herein by reference. The following discussion should be read in conjunction with the Company's Annual Report on Form 10-K for the year ended September 24, 2016 (the "2016 Form 10-K") filed with the U.S. Securities and Exchange Commission (the "SEC") and the condensed consolidated financial statements and notes thereto included elsewhere in this Form 10-Q. All information presented herein is based on the Company's fiscal calendar. Unless otherwise stated, references to particular years, quarters, months or periods refer to the Company's fiscal years ended in September and the associated quarters, months and periods of those fiscal years. Each of the terms the "Company" and "Apple" as used herein refers collectively to Apple Inc. and its wholly-owned subsidiaries, unless otherwise stated. The Company assumes no obligation to revise or update any forward-looking statements for any reason, except as required by law.

### Available Information

The Company's Annual Report on Form 10-K, Quarterly Reports on Form 10-Q, Current Reports on Form 8-K, and amendments to reports filed pursuant to Sections 13(a) and 15(d) of the Securities Exchange Act of 1934, as amended (the "Exchange Act"), are filed with the SEC. The Company is subject to the informational requirements of the Exchange Act and files or furnishes reports, proxy statements, and other information with the SEC. Such reports and other information filed by the Company with the SEC are available free of charge on the Company's website at [investor.apple.com/sec.cfm](http://investor.apple.com/sec.cfm) when such reports are available on the SEC's website. The public may read and copy any materials filed by the Company with the SEC at the SEC's Public Reference Room at 100 F Street, NE, Room 1580, Washington, DC 20549. The public may obtain information on the operation of the Public Reference Room by calling the SEC at 1-800-SEC-0330. The SEC maintains an internet site that contains reports, proxy and information statements and other information regarding issuers that file electronically with the SEC at [www.sec.gov](http://www.sec.gov). The contents of websites are not incorporated into this filing. Further, the Company's references to website URLs are intended to be inactive textual references only.

### Overview and Highlights

The Company designs, manufactures and markets mobile communication and media devices and personal computers, and sells a variety of related software, services, accessories, networking solutions and third-party digital content and applications. The Company's products and services include iPhone®, iPad®, Mac®, Apple Watch®, Apple TV®, a portfolio of consumer and professional software applications, iOS, macOS®, watchOS® and tvOS™ operating systems, iCloud®, Apple Pay® and a variety of accessory, service and support offerings. The Company sells and delivers digital content and applications through the iTunes Store®, App Store®, Mac App Store, TV App Store, iBooks Store™ and Apple Music® (collectively "Digital Content and Services"). The Company sells its products worldwide through its retail stores, online stores and direct sales force, as well as through third-party cellular network carriers, wholesalers, retailers and value-added resellers. In addition, the Company sells a variety of third-party Apple-compatible products, including application software and various accessories through its retail and online stores. The Company sells to consumers, small and mid-sized businesses and education, enterprise and government customers.

### Business Strategy

The Company is committed to bringing the best user experience to its customers through its innovative hardware, software and services. The Company's business strategy leverages its unique ability to design and develop its own operating systems, hardware, application software and services to provide its customers products and solutions with innovative design, superior ease-of-use and seamless integration. As part of its strategy, the Company continues to expand its platform for the discovery and delivery of digital content and applications through its Digital Content and Services, which allows customers to discover and download digital content, iOS, Mac, Apple Watch and Apple TV

applications, and books through either a Mac or Windows personal computer or through iPhone, iPad and iPod touch® devices (“iOS devices”), Apple TV and Apple Watch. The Company also supports a community for the development of third-party software and hardware products and digital content that complement the Company’s offerings. The Company believes a high-quality buying experience with knowledgeable salespersons who can convey the value of the Company’s products and services greatly enhances its ability to attract and retain customers. Therefore, the Company’s strategy also includes building and expanding its own retail and online stores and its third-party distribution network to effectively reach more customers and provide them with a high-quality sales and post-sales support experience. The Company believes ongoing investment in research and development (“R&D”), marketing and advertising is critical to the development and sale of innovative products and technologies.

### Business Seasonality and Product Introductions

The Company has historically experienced higher net sales in its first quarter compared to other quarters in its fiscal year due in part to seasonal holiday demand. Additionally, new product introductions can significantly impact net sales, product costs and operating expenses. Product introductions can also impact the Company's net sales to its indirect distribution channels as these channels are filled with new product inventory following a product introduction, and often, channel inventory of a particular product declines as the next related major product launch approaches. Net sales can also be affected when consumers and distributors anticipate a product introduction. However, neither historical seasonal patterns nor historical patterns of product introductions should be considered reliable indicators of the Company's future pattern of product introductions, future net sales or financial performance.

### Fiscal Period

The Company's fiscal year is the 52 or 53-week period that ends on the last Saturday of September. The Company's fiscal year 2017 will include 53 weeks and will end on September 30, 2017. A 14th week was included in the first quarter of 2017, as is done every five or six years, to realign the Company's fiscal quarters with calendar quarters.

### Second Quarter Fiscal 2017 Highlights

Net sales increased 5% or \$2.3 billion during the second quarter of 2017 compared to the same quarter in 2016, primarily driven by strong growth in Services, Mac and Other Products, partially offset by the effect of weakness in foreign currencies relative to the U.S. dollar. Net sales reflected year-over-year growth in each of the geographic operating segments, with the exception of Greater China. During the second quarter of 2017, the Company introduced a new 9.7-inch iPad, which became available at the end of the quarter.

The Company utilized \$7.0 billion to repurchase shares of its common stock and paid dividends and dividend equivalents of \$3.0 billion during the second quarter of 2017. Additionally, the Company issued \$11.0 billion of U.S. dollar-denominated long-term debt.

### Sales Data

The following table shows net sales by operating segment and net sales and unit sales by product for the three- and six-month periods ended April 1, 2017 and March 26, 2016 (dollars in millions and units in thousands):

	Three Months Ended			Six Months Ended		
	April 1, 2017	March 26, 2016	Change	April 1, 2017	March 26, 2016	Change
Net Sales by Operating Segment:						
Americas	\$21,157	\$ 19,096	11 %	\$53,125	\$48,421	10 %
Europe	12,733	11,535	10 %	31,254	29,467	6 %
Greater China	10,726	12,486	(14 )%	26,959	30,859	(13 )%
Japan	4,485	4,281	5 %	10,251	9,075	13 %
Rest of Asia Pacific	3,795	3,159	20 %	9,658	8,607	12 %
Total net sales	\$52,896	\$ 50,557	5 %	\$ 131,247	\$ 126,429	4 %

### Net Sales by Product:

iPhone <sup>(1)</sup>	\$33,249	\$ 32,857	1 %	\$87,627	\$84,492	4 %
iPad <sup>(1)</sup>	3,889	4,413	(12 )%	9,422	11,497	(18 )%
Mac <sup>(1)</sup>	5,844	5,107	14 %	13,088	11,853	10 %
Services <sup>(2)</sup>	7,041	5,991	18 %	14,213	12,047	18 %
Other Products <sup>(1)(3)</sup>	2,873	2,189	31 %	6,897	6,540	5 %
Total net sales	\$52,896	\$ 50,557	5 %	\$ 131,247	\$ 126,429	4 %

### Unit Sales by Product:

iPhone	50,763	51,193	(1 )%	129,053	125,972	2 %
iPad	8,922	10,251	(13 )%	22,003	26,373	(17 )%
Mac	4,199	4,034	4 %	9,573	9,346	2 %

(1)Includes deferrals and amortization of related software upgrade rights and non-software services.

(2)Includes revenue from Digital Content and Services, AppleCare®, Apple Pay, licensing and other services.

(3)Includes sales of Apple TV, Apple Watch, Beats® products, iPod and Apple-branded and third-party accessories.

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## Product Performance

## iPhone

The following table presents iPhone net sales and unit sales information for the three- and six-month periods ended April 1, 2017 and March 26, 2016 (dollars in millions and units in thousands):

	Three Months Ended			Six Months Ended		
	April 1, 2017	March 26, 2016	Change	April 1, 2017	March 26, 2016	Change
Net sales	\$33,249	\$32,857	1 %	\$87,627	\$84,492	4 %
Percentage of total net sales	63 %	65 %		67 %	67 %	
Unit sales	50,763	51,193	(1 )%	129,053	125,972	2 %

iPhone net sales increased during the second quarter of 2017 compared to the same period in 2016 due to higher iPhone average selling prices (“ASPs”), largely offset by the effect of weakness in foreign currencies relative to the U.S. dollar. The year-over-year increase in iPhone net sales during the first six months of 2017 was due primarily to higher iPhone unit sales and to a lesser extent higher iPhone ASPs, partially offset by the effect of weakness in foreign currencies relative to the U.S. dollar.

## iPad

The following table presents iPad net sales and unit sales information for the three- and six-month periods ended April 1, 2017 and March 26, 2016 (dollars in millions and units in thousands):

	Three Months Ended			Six Months Ended		
	April 1, 2017	March 26, 2016	Change	April 1, 2017	March 26, 2016	Change
Net sales	\$3,889	\$4,413	(12 )%	\$9,422	\$11,497	(18 )%
Percentage of total net sales	7 %	9 %		7 %	9 %	
Unit sales	8,922	10,251	(13 )%	22,003	26,373	(17 )%

iPad net sales decreased in the second quarter and first six months of 2017 compared to the same periods in 2016 due primarily to lower iPad unit sales in each of the geographic operating segments and to a lesser extent the effect of weakness in foreign currencies relative to the U.S. dollar.

## Mac

The following table presents Mac net sales and unit sales information for the three- and six-month periods ended April 1, 2017 and March 26, 2016 (dollars in millions and units in thousands):

	Three Months Ended			Six Months Ended		
	April 1, 2017	March 26, 2016	Change	April 1, 2017	March 26, 2016	Change
Net sales	\$5,844	\$5,107	14 %	\$13,088	\$11,853	10 %
Percentage of total net sales	11 %	10 %		10 %	9 %	
Unit sales	4,199	4,034	4 %	9,573	9,346	2 %

Mac net sales increased during the second quarter and first six months of 2017 compared to the same periods in 2016 due primarily to a different mix of Macs, including the new MacBook Pro introduced in the first quarter of 2017, and to a lesser extent higher Mac unit sales. The year-over-year increase in Mac net sales was partially offset by the effect of weakness in foreign currencies relative to the U.S. dollar.

## Services

The following table presents Services net sales information for the three- and six-month periods ended April 1, 2017 and March 26, 2016 (dollars in millions):

	Three Months Ended			Six Months Ended		
	April 1, 2017	March 26, 2016	Change	April 1, 2017	March 26, 2016	Change
Net sales	\$7,041	\$5,991	18 %	\$14,213	\$12,047	18 %
Percentage of total net sales	13 %	12 %		11 %	10 %	

The year-over-year increase in Services net sales in the second quarter and first six months of 2017 compared to the same periods in 2016 was due primarily to growth from the App Store and licensing sales. The year-over-year increase in Services net sales during the first six months of 2017 was partially offset by the non-recurrence of the \$548 million received from Samsung Electronics Co., Ltd. in the first quarter of 2016 related to patent infringement matters.

## Segment Operating Performance

The Company manages its business primarily on a geographic basis. The Company's reportable operating segments consist of the Americas, Europe, Greater China, Japan and Rest of Asia Pacific. The Americas segment includes both North and South America. The Europe segment includes European countries, as well as India, the Middle East and Africa. The Greater China segment includes China, Hong Kong and Taiwan. The Rest of Asia Pacific segment includes Australia and those Asian countries not included in the Company's other reportable operating segments. Although the reportable operating segments provide similar hardware and software products and similar services, each one is managed separately to better align with the location of the Company's customers and distribution partners and the unique market dynamics of each geographic region. Further information regarding the Company's reportable operating segments can be found in Part I, Item 1 of this Form 10-Q in the Notes to Condensed Consolidated Financial Statements, in Note 11, "Segment Information and Geographic Data."

## Americas

The following table presents Americas net sales information for the three- and six-month periods ended April 1, 2017 and March 26, 2016 (dollars in millions):

	Three Months Ended			Six Months Ended		
	April 1, 2017	March 26, 2016	Change	April 1, 2017	March 26, 2016	Change
Net sales	\$21,157	\$19,096	11 %	\$53,125	\$48,421	10 %
Percentage of total net sales	40 %	38 %		40 %	38 %	

Americas net sales increased during the second quarter of 2017 compared to the same period in 2016 due primarily to higher net sales of iPhone and Other Products. The year-over-year increase in Americas net sales during the first six months of 2017 was due primarily to higher net sales of iPhone and Mac, partially offset by lower net sales of iPad.

## Europe

The following table presents Europe net sales information for the three- and six-month periods ended April 1, 2017 and March 26, 2016 (dollars in millions):

	Three Months Ended			Six Months Ended		
	April 1, 2017	March 26, 2016	Change	April 1, 2017	March 26, 2016	Change
Net sales	\$12,733	\$11,535	10 %	\$31,254	\$29,467	6 %
Percentage of total net sales	24 %	23 %		24 %	23 %	

Europe net sales increased during the second quarter of 2017 compared to the same period in 2016 due primarily to higher net sales of iPhone and Mac, partially offset by the effect of weakness in foreign currencies relative to the U.S. dollar. The year-over-year increase in Europe net sales during the first six months of 2017 was due primarily to higher net sales of iPhone and Services, partially offset by the effect of weakness in foreign currencies relative to the U.S. dollar and to a lesser extent lower net sales of iPad.

## Greater China

The following table presents Greater China net sales information for the three- and six-month periods ended April 1, 2017 and March 26, 2016 (dollars in millions):

	Three Months Ended			Six Months Ended		
	April 1, 2017	March 26, 2016	Change	April 1, 2017	March 26, 2016	Change
Net sales	\$10,726	\$12,486	(14 )%	\$26,959	\$30,859	(13 )%
Percentage of total net sales	20	% 25	%	21	% 24	%

Greater China net sales decreased during the second quarter and first six months of 2017 compared to the same periods in 2016 due primarily to lower net sales of iPhone and the effect of weakness in foreign currencies relative to the U.S. dollar, partially offset by growth in net sales of Services.

## Japan

The following table presents Japan net sales information for the three- and six-month periods ended April 1, 2017 and March 26, 2016 (dollars in millions):

	Three Months Ended			Six Months Ended		
	April 1, 2017	March 26, 2016	Change	April 1, 2017	March 26, 2016	Change
Net sales	\$4,485	\$4,281	5 %	\$10,251	\$9,075	13 %
Percentage of total net sales	8	% 8	%	8	% 7	%

Japan net sales increased during the second quarter of 2017 compared to the same period in 2016 due primarily to higher net sales of Services and the effect of strength in the Japanese yen relative to the U.S. dollar. The year-over-year increase in Japan net sales during the first six months of 2017 was due primarily to the effect of strength in the Japanese yen relative to the U.S. dollar and growth in net sales of iPhone.

## Rest of Asia Pacific

The following table presents Rest of Asia Pacific net sales information for the three- and six-month periods ended April 1, 2017 and March 26, 2016 (dollars in millions):

	Three Months Ended			Six Months Ended		
	April 1, 2017	March 26, 2016	Change	April 1, 2017	March 26, 2016	Change
Net sales	\$3,795	\$3,159	20 %	\$9,658	\$8,607	12 %
Percentage of total net sales	7	% 6	%	7	% 7	%

Rest of Asia Pacific net sales increased during the second quarter of 2017 compared to the same period in 2016 due primarily to higher net sales of iPhone and Mac. The year-over-year increase in Rest of Asia Pacific net sales during the first six months of 2017 was due primarily to higher net sales of iPhone and the effect of strength in foreign currencies relative to the U.S. dollar.

## Gross Margin

Gross margin for the three- and six-month periods ended April 1, 2017 and March 26, 2016 was as follows (dollars in millions):

	Three Months Ended		Six Months Ended		
	April 1, 2017	March 26, 2016	April 1, 2017	March 26, 2016	
Net sales	\$52,896	\$50,557	\$131,247	\$126,429	
Cost of sales	32,305	30,636	80,480	76,085	
Gross margin	\$20,591	\$19,921	\$50,767	\$50,344	
Gross margin percentage	38.9	% 39.4	% 38.7	% 39.8	%

Gross margin decreased during the second quarter and first six months of 2017 compared to the same periods in 2016 due primarily to higher product cost structures and the effect of weakness in foreign currencies relative to the U.S. dollar, partially offset by a favorable mix of products and services.





The Company anticipates gross margin during the third quarter of 2017 to be between 37.5% and 38.5%. The foregoing statement regarding the Company's expected gross margin percentage in the third quarter of 2017 is forward-looking and could differ from actual results. The Company's future gross margins can be impacted by multiple factors including, but not limited to, those set forth in Part II, Item 1A of this Form 10-Q under the heading "Risk Factors" and those described in this paragraph. In general, the Company believes gross margins will remain under downward pressure due to a variety of factors, including continued industry-wide global product pricing pressures, increased competition, compressed product life cycles, product transitions, potential increases in the cost of components, and potential strengthening of the U.S. dollar, as well as potential increases in the costs of outside manufacturing services and a potential shift in the Company's sales mix towards products with lower gross margins. In response to competitive pressures, the Company expects it will continue to take product pricing actions, which would adversely affect gross margins. Gross margins could also be affected by the Company's ability to manage product quality and warranty costs effectively and to stimulate demand for certain of its products. Due to the Company's significant international operations, its financial condition and operating results, including gross margins, could be significantly affected by fluctuations in exchange rates.

#### Operating Expenses

Operating expenses for the three- and six-month periods ended April 1, 2017 and March 26, 2016 were as follows (dollars in millions):

	Three Months Ended		Six Months Ended	
	April 1, 2017	March 26, 2016	April 1, 2017	March 26, 2016
Research and development	\$2,776	\$2,511	\$5,647	\$4,915
Percentage of total net sales	5	% 5	% 4	% 4
Selling, general and administrative	\$3,718	\$3,423	\$7,664	\$7,271
Percentage of total net sales	7	% 7	% 6	% 6
Total operating expenses	\$6,494	\$5,934	\$13,311	\$12,186
Percentage of total net sales	12	% 12	% 10	% 10

#### Research and Development

The growth in R&D expense during the second quarter and first six months of 2017 compared to the same periods in 2016 was driven primarily by an increase in headcount and related expenses to support expanded R&D activities. The Company continues to believe that focused investments in R&D are critical to its future growth and competitive position in the marketplace, and to the development of new and updated products that are central to the Company's core business strategy.

#### Selling, General and Administrative

The growth in selling, general and administrative expense during the second quarter of 2017 compared to the same quarter in 2016 was driven primarily by an increase in headcount and related expenses and higher spending on marketing and advertising. The year-over-year growth in selling, general and administrative expense during the first six months of 2017 was driven primarily by an increase in headcount and related expenses and higher variable selling costs.

#### Other Income/(Expense), Net

Other income/(expense), net for the three- and six-month periods ended April 1, 2017 and March 26, 2016 was as follows (dollars in millions):

	Three Months Ended			Six Months Ended		
	April 1, 2017	March 26, 2016	Change	April 1, 2017	March 26, 2016	Change
Interest and dividend income	\$1,282	\$ 986		\$2,506	\$ 1,927	
Interest expense	(530 )	(321 )		(1,055 )	(597 )	
Other expense, net	(165 )	(510 )		(43 )	(773 )	
Total other income/(expense), net	\$587	\$ 155	279 %	\$1,408	\$ 557	153 %

The increase in other income/(expense), net during the second quarter and first six months of 2017 compared to the same periods in 2016 was due primarily to higher interest income and the favorable impact of foreign

exchange-related items, partially offset by higher interest expense on debt. The weighted-average interest rate earned by the Company on its cash, cash equivalents and marketable securities was 1.99% and 1.74% in the second quarter of 2017 and 2016, respectively, and 1.93% and 1.70% in the first six months of 2017 and 2016, respectively.

#### Provision for Income Taxes

Provision for income taxes and effective tax rates for the three- and six-month periods ended April 1, 2017 and March 26, 2016 were as follows (dollars in millions):

	Three Months Ended		Six Months Ended	
	April 1, 2017	March 26, 2016	April 1, 2017	March 26, 2016
Provision for income taxes	\$ 3,655	\$ 3,626	\$ 9,944	\$ 9,838
Effective tax rate	24.9 %	25.6 %	25.6 %	25.4 %

The Company's effective tax rates during the second quarter of 2017 and 2016 differ from the statutory federal income tax rate of 35% due primarily to certain undistributed foreign earnings, a substantial portion of which was generated by subsidiaries organized in Ireland, for which no U.S. taxes are provided when such earnings are intended to be indefinitely reinvested outside the U.S. The lower effective tax rate during the second quarter of 2017 compared to the same quarter in 2016 was due primarily to a different geographic mix of earnings. The slightly higher effective tax rate in the first six months of 2017 compared to the same period in 2016 was due primarily to the retroactive reinstatement of the U.S. federal R&D tax credit during the first quarter of 2016.

The Company is subject to audits by federal, state, local and foreign tax authorities. Management believes that adequate provisions have been made for any adjustments that may result from tax examinations. However, the outcome of tax audits cannot be predicted with certainty. If any issues addressed in the Company's tax audits are resolved in a manner not consistent with management's expectations, the Company could be required to adjust its provision for income taxes in the period such resolution occurs.

On August 30, 2016, the European Commission announced its decision that Ireland granted state aid to the Company by providing tax opinions in 1991 and 2007 concerning the tax allocation of profits of the Irish branches of two subsidiaries of the Company (the "State Aid Decision"). The State Aid Decision orders Ireland to calculate and recover additional taxes from the Company for the period June 2003 through December 2014. Irish legislative changes, effective as of January 2015, eliminated the application of the tax opinions from that date forward. The Company believes the State Aid Decision to be without merit and appealed to the General Court of the Court of Justice of the European Union. Ireland has also appealed the State Aid Decision. While the European Commission announced a recovery amount of up to €13 billion, plus interest, the actual amount of additional taxes subject to recovery is to be calculated by Ireland in accordance with the European Commission's guidance. Once the recovery amount is computed by Ireland, the Company anticipates funding it, including interest, out of foreign cash into escrow, where it will remain pending conclusion of all appeals. The Company believes that any incremental Irish corporate income taxes potentially due related to the State Aid Decision would be creditable against U.S. taxes.

#### Recent Accounting Pronouncements

##### Restricted Cash

In November 2016, the Financial Accounting Standards Board ("FASB") issued Accounting Standards Update ("ASU") No. 2016-18, Statement of Cash Flows (Topic 230): Restricted Cash ("ASU 2016-18"), which enhances and clarifies the guidance on the classification and presentation of restricted cash in the statement of cash flows. The Company will adopt ASU 2016-18 in its first quarter of 2019 utilizing the retrospective adoption method. Currently, the Company's restricted cash balance is not significant.

##### Income Taxes

In October 2016, the FASB issued ASU No. 2016-16, Income Taxes (Topic 740): Intra-Entity Transfers of Assets Other Than Inventory ("ASU 2016-16"), which requires the recognition of the income tax consequences of an intra-entity transfer of an asset, other than inventory, when the transfer occurs. The Company will adopt ASU 2016-16 in its first quarter of 2019 utilizing the modified retrospective adoption method. Currently, the Company anticipates recording up to \$9 billion of net deferred tax assets on its Consolidated Balance Sheets. However, the ultimate impact of adopting ASU 2016-16 will depend on the balance of intellectual property transferred between its subsidiaries as of the adoption date. The Company will recognize incremental deferred income tax expense thereafter as these deferred tax assets are utilized.

### Stock Compensation

In March 2016, the FASB issued ASU No. 2016-09, Compensation – Stock Compensation (Topic 718): Improvements to Employee Share-Based Payment Accounting (“ASU 2016-09”), which modifies certain aspects of the accounting for share-based payment transactions, including income taxes, classification of awards, and classification in the statement of cash flows. The Company will adopt ASU 2016-09 in its first quarter of 2018. Currently, excess tax benefits or deficiencies from the Company's equity awards are recorded as additional paid-in capital in its Consolidated Balance Sheets. Upon adoption, the Company will record any excess tax benefits or deficiencies from its equity awards in its Consolidated Statements of Operations in the reporting periods in which vesting occurs. As a result, subsequent to adoption the Company's income tax expense and associated effective tax rate will be impacted by fluctuations in stock price between the grant dates and vesting dates of equity awards.

### Leases

In February 2016, the FASB issued ASU No. 2016-02, Leases (Topic 842) (“ASU 2016-02”), which modifies lease accounting for lessees to increase transparency and comparability by recording lease assets and liabilities for operating leases and disclosing key information about leasing arrangements. ASU 2016-02 will be effective for the Company beginning in its first quarter of 2020, and early adoption is permitted. The Company will use a modified retrospective adoption approach. While the Company is currently evaluating the timing and impact of adopting ASU 2016-02, currently the Company anticipates recording lease assets and liabilities in excess of \$8.2 billion on its Consolidated Balance Sheets, with no material impact to its Consolidated Statements of Operations. However, the ultimate impact of adopting ASU 2016-02 will depend on the Company's lease portfolio as of the adoption date.

### Financial Instruments

In January 2016, the FASB issued ASU No. 2016-01, Financial Instruments – Overall (Subtopic 825-10): Recognition and Measurement of Financial Assets and Financial Liabilities (“ASU 2016-01”), which updates certain aspects of recognition, measurement, presentation and disclosure of financial instruments. The Company will adopt ASU 2016-01 in its first quarter of 2019 utilizing the modified retrospective adoption method. Based on the composition of the Company's investment portfolio, the adoption of ASU 2016-01 is not expected to have a material impact on its consolidated financial statements.

In June 2016, the FASB issued ASU No. 2016-13, Financial Instruments – Credit Losses (Topic 326): Measurement of Credit Losses on Financial Instruments (“ASU 2016-13”), which modifies the measurement of expected credit losses of certain financial instruments. The Company will adopt ASU 2016-13 in its first quarter of 2021 utilizing the modified retrospective adoption method. Based on the composition of the Company's investment portfolio, current market conditions, and historical credit loss activity, the adoption of ASU 2016-13 is not expected to have a material impact on its consolidated financial statements.

### Revenue Recognition

In May 2014, the FASB issued ASU No. 2014-09, Revenue from Contracts with Customers (Topic 606) (“ASU 2014-09”), which amends the existing accounting standards for revenue recognition. ASU 2014-09 is based on principles that govern the recognition of revenue at an amount an entity expects to be entitled when products are transferred to customers.

Subsequently, the FASB has issued the following standards related to ASU 2014-09: ASU No. 2016-08, Revenue from Contracts with Customers (Topic 606): Principal versus Agent Considerations (“ASU 2016-08”); ASU No. 2016-10, Revenue from Contracts with Customers (Topic 606): Identifying Performance Obligations and Licensing (“ASU 2016-10”); ASU No. 2016-12, Revenue from Contracts with Customers (Topic 606): Narrow-Scope Improvements and Practical Expedients (“ASU 2016-12”); and ASU No. 2016-20, Technical Corrections and Improvements to Topic 606, Revenue from Contracts with Customers (“ASU 2016-20”). The Company must adopt ASU 2016-08, ASU 2016-10, ASU 2016-12 and ASU 2016-20 with ASU 2014-09 (collectively, the “new revenue standards”).

The new revenue standards may be applied retrospectively to each prior period presented or retrospectively with the cumulative effect recognized as of the date of adoption. The Company plans to adopt the new revenue standards in its first quarter of 2019 utilizing the full retrospective adoption method. The new revenue standards are not expected to have a material impact on the amount and timing of revenue recognized in the Company's consolidated financial statements.

### Liquidity and Capital Resources

The following tables present selected financial information and statistics as of April 1, 2017 and September 24, 2016 and for the first six months of 2017 and 2016 (in millions):

	April 1, 2017	September 24, 2016
Cash, cash equivalents and marketable securities	\$256,841	\$ 237,585
Property, plant and equipment, net	\$27,163	\$ 27,010
Commercial paper	\$9,992	\$ 8,105
Total term debt	\$88,530	\$ 78,927
Working capital	\$28,648	\$ 27,863

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	Six Months Ended	
	April 1, 2017	March 26, 2016
Cash generated by operating activities	\$39,579	\$39,064
Cash used in investing activities	\$(33,324)	\$(34,110)
Cash used in financing activities	\$(11,582)	\$(4,560 )

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The Company believes its existing balances of cash, cash equivalents and marketable securities will be sufficient to satisfy its working capital needs, capital asset purchases, outstanding commitments and other liquidity requirements associated with its existing operations over the next 12 months. The Company currently anticipates the cash used for future dividends, the share repurchase program and debt repayments will come from its current domestic cash, cash generated from ongoing U.S. operating activities and from borrowings.

As of April 1, 2017 and September 24, 2016, the Company's cash, cash equivalents and marketable securities held by foreign subsidiaries were \$239.6 billion and \$216.0 billion, respectively, and are generally based in U.S.

dollar-denominated holdings. Amounts held by foreign subsidiaries are generally subject to U.S. income taxation on repatriation to the U.S. In connection with the State Aid Decision, the European Commission announced a recovery amount of up to €13 billion, plus interest. The actual amount of additional taxes subject to recovery is to be calculated by Ireland in accordance with the European Commission's guidance. Once the recovery amount is computed by Ireland, the Company anticipates funding it, including interest, out of foreign cash into escrow, where it will remain pending conclusion of all appeals.

The Company's marketable securities investment portfolio is primarily invested in highly-rated securities, and its investment policy generally limits the amount of credit exposure to any one issuer. The policy generally requires investments to be investment grade, with the primary objective of minimizing the potential risk of principal loss. During the six months ended April 1, 2017, cash generated by operating activities of \$39.6 billion was a result of \$28.9 billion of net income, non-cash adjustments to net income of \$10.4 billion and an increase in the net change in operating assets and liabilities of \$0.3 billion. Cash used in investing activities of \$33.3 billion during the six months ended April 1, 2017 consisted primarily of cash used for purchases of marketable securities, net of sales and maturities, of \$26.9 billion and cash used to acquire property, plant and equipment of \$6.3 billion. Cash used in financing activities of \$11.6 billion during the six months ended April 1, 2017 consisted primarily of cash used to repurchase common stock of \$18.0 billion and cash used to pay dividends and dividend equivalents of \$6.1 billion, partially offset by proceeds from the issuance of term debt, net of \$11.0 billion and a net increase in commercial paper of \$1.9 billion.

During the six months ended March 26, 2016, cash generated by operating activities of \$39.1 billion was a result of \$28.9 billion of net income, non-cash adjustments to net income of \$11.0 billion and a decrease in the net change in operating assets and liabilities of \$0.8 billion. Cash used in investing activities of \$34.1 billion during the six months ended March 26, 2016 consisted primarily of cash used for purchases of marketable securities, net of sales and maturities, of \$27.0 billion and cash used to acquire property, plant and equipment of \$5.9 billion. Cash used in financing activities of \$4.6 billion during the six months ended March 26, 2016 consisted primarily of cash used to repurchase common stock of \$13.5 billion and cash used to pay dividends and dividend equivalents of \$5.9 billion, partially offset by proceeds from the issuance of term debt, net of \$15.6 billion.

#### Capital Assets

The Company's capital expenditures were \$4.5 billion during the first six months of 2017. The Company anticipates utilizing approximately \$16.0 billion for capital expenditures during 2017, which includes product tooling and manufacturing process equipment; data centers; corporate facilities and infrastructure, including information systems hardware, software and enhancements; and retail store facilities.

#### Debt

The Company issues unsecured short-term promissory notes ("Commercial Paper") pursuant to a commercial paper program. The Company uses the net proceeds from the commercial paper program for general corporate purposes, including dividends and share repurchases. As of April 1, 2017, the Company had \$10.0 billion of Commercial Paper outstanding, with a weighted-average interest rate of 0.80% and maturities generally less than nine months.

As of April 1, 2017, the Company had outstanding floating- and fixed-rate notes with varying maturities for an aggregate principal amount of \$88.9 billion (collectively the "Notes"). The Company has entered, and in the future may enter, into interest rate swaps to manage interest rate risk on the Notes. In addition, the Company has entered, and in the future may enter, into currency swaps to manage foreign currency risk on the Notes.

Further information regarding the Company's debt issuances and related hedging activity can be found in Part I, Item 1 of this Form 10-Q in the Notes to Condensed Consolidated Financial Statements, in Note 2, "Financial Instruments" and Note 6, "Debt."

Capital Return Program

As of April 1, 2017, the Company had an authorized capital return program of \$250 billion, which included a share repurchase program of \$175 billion of the Company's common stock. As of April 1, 2017, \$151 billion of the share repurchase program had been utilized. The Company's share repurchase program does not obligate it to acquire any specific number of shares. Under the program, shares may be repurchased in privately negotiated or open market transactions, including under plans complying with Rule 10b5-1 under the Exchange Act.



The following table presents the Company's dividends, dividend equivalents, share repurchases and net share settlement activity from the start of the capital return program in August 2012 through April 1, 2017 (in millions):

	Dividends and Dividend Equivalents Paid	Accelerated Share Repurchases	Open Market Share Repurchases	Taxes Related to Settlement of Equity Awards	Total
Q2 2017	\$ 3,004	\$ 3,000	\$ 4,001	\$ 159	\$10,164
Q1 2017	3,130	6,000	5,000	629	14,759
2016	12,150	12,000	17,000	1,570	42,720
2015	11,561	6,000	30,026	1,499	49,086
2014	11,126	21,000	24,000	1,158	57,284
2013	10,564	13,950	9,000	1,082	34,596
2012	2,488	—	—	56	2,544
Total	\$ 54,023	\$ 61,950	\$ 89,027	\$ 6,153	\$211,153

On May 2, 2017, the Company announced that the Board of Directors increased the total capital return program from \$250 billion to \$300 billion, which includes an increase in the share repurchase authorization from \$175 billion to \$210 billion. Additionally, the Company announced that the Board of Directors raised the Company's quarterly cash dividend by 10.5% from \$0.57 to \$0.63 per share, beginning with the dividend to be paid during the third quarter of 2017. The Company intends to increase its dividend on an annual basis subject to declaration by the Board of Directors.

The Company expects to execute its capital return program by the end of March 2019 by paying dividends and dividend equivalents, repurchasing shares and remitting withheld taxes related to net share settlement of restricted stock units. The Company plans to continue to access the domestic and international debt markets to assist in funding its capital return program.

#### Off-Balance Sheet Arrangements and Contractual Obligations

The Company has not entered into any transactions with unconsolidated entities whereby the Company has financial guarantees, subordinated retained interests, derivative instruments, or other contingent arrangements that expose the Company to material continuing risks, contingent liabilities, or any other obligation under a variable interest in an unconsolidated entity that provides financing, liquidity, market risk, or credit risk support to the Company, or engages in leasing, hedging, or R&D services with the Company.

#### Operating Leases

As of April 1, 2017, the Company's total future minimum lease payments under noncancelable operating leases were \$8.2 billion. The Company's retail store and other facility leases are typically for terms not exceeding 10 years and generally contain multi-year renewal options.

#### Manufacturing Purchase Obligations

The Company utilizes several outsourcing partners to manufacture sub-assemblies for the Company's products and to perform final assembly and testing of finished products. These outsourcing partners acquire components and build product based on demand information supplied by the Company, which typically covers periods up to 150 days. The Company also obtains individual components for its products from a wide variety of individual suppliers. Consistent with industry practice, the Company acquires components through a combination of purchase orders, supplier contracts, and open orders based on projected demand information. As of April 1, 2017, the Company had manufacturing purchase obligations of \$21.7 billion.

#### Other Purchase Obligations

The Company's other purchase obligations were comprised of commitments to acquire capital assets, including product tooling and manufacturing process equipment, and commitments related to advertising, licensing, R&D, internet and telecommunications services and other obligations. As of April 1, 2017, the Company had other purchase obligations of \$5.9 billion.

The Company's other non-current liabilities in the Condensed Consolidated Balance Sheets consist primarily of deferred tax liabilities, gross unrecognized tax benefits and the related gross interest and penalties. As of April 1, 2017, the Company had non-current deferred tax liabilities of \$28.2 billion, gross unrecognized tax benefits of \$8.8

billion and an additional \$1.3 billion for gross interest and penalties.

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#### Indemnification

The Company generally does not indemnify end-users of its operating system and application software against legal claims that the software infringes third-party intellectual property rights. Other agreements entered into by the Company sometimes include indemnification provisions under which the Company could be subject to costs and/or damages in the event of an infringement claim against the Company or an indemnified third party. In the opinion of management, there was not at least a reasonable possibility the Company may have incurred a material loss with respect to indemnification of end-users of its operating system or application software for infringement of third-party intellectual property rights.

The Company offers an iPhone Upgrade Program, which is available to customers who purchase a qualifying iPhone in the U.S., the U.K. and mainland China. The iPhone Upgrade Program provides customers the right to trade in that iPhone for a specified amount when purchasing a new iPhone, provided certain conditions are met. The Company accounts for the trade-in right as a guarantee liability and recognizes arrangement revenue net of the fair value of such right with subsequent changes to the guarantee liability recognized within revenue.

The Company has entered into indemnification agreements with its directors and executive officers. Under these agreements, the Company has agreed to indemnify such individuals to the fullest extent permitted by law against liabilities that arise by reason of their status as directors or officers and to advance expenses incurred by such individuals in connection with related legal proceedings. It is not possible to determine the maximum potential amount of payments the Company could be required to make under these agreements due to the limited history of prior indemnification claims and the unique facts and circumstances involved in each claim. However, the Company maintains directors and officers liability insurance coverage to reduce its exposure to such obligations.

#### Critical Accounting Policies and Estimates

The preparation of financial statements and related disclosures in conformity with U.S. generally accepted accounting principles and the Company's discussion and analysis of its financial condition and operating results require the Company's management to make judgments, assumptions and estimates that affect the amounts reported in its condensed consolidated financial statements and accompanying notes. Management bases its estimates on historical experience and on various other assumptions it believes to be reasonable under the circumstances, the results of which form the basis for making judgments about the carrying values of assets and liabilities. Actual results may differ from these estimates, and such differences may be material.

Note 1, "Summary of Significant Accounting Policies" in Part I, Item 1 of this Form 10-Q and in the Notes to Consolidated Financial Statements in Part II, Item 8 of the 2016 Form 10-K, and "Critical Accounting Policies and Estimates" in Part II, Item 7 of the 2016 Form 10-K describe the significant accounting policies and methods used in the preparation of the Company's condensed consolidated financial statements. There have been no material changes to the Company's critical accounting policies and estimates since the 2016 Form 10-K.

#### Item 3. Quantitative and Qualitative Disclosures About Market Risk

There have been no material changes to the Company's market risk during the first six months of 2017. For a discussion of the Company's exposure to market risk, refer to the Company's market risk disclosures set forth in Part II, Item 7A, "Quantitative and Qualitative Disclosures About Market Risk" of the 2016 Form 10-K.

#### Item 4. Controls and Procedures

##### Evaluation of Disclosure Controls and Procedures

Based on an evaluation under the supervision and with the participation of the Company's management, the Company's principal executive officer and principal financial officer have concluded that the Company's disclosure controls and procedures as defined in Rules 13a-15(e) and 15d-15(e) under the Exchange Act were effective as of April 1, 2017 to ensure that information required to be disclosed by the Company in reports that it files or submits under the Exchange Act is (i) recorded, processed, summarized and reported within the time periods specified in the SEC rules and forms and (ii) accumulated and communicated to the Company's management, including its principal executive officer and principal financial officer, as appropriate to allow timely decisions regarding required disclosure.

##### Changes in Internal Control Over Financial Reporting

There were no changes in the Company's internal control over financial reporting during the second quarter of 2017, which were identified in connection with management's evaluation required by paragraph (d) of Rules 13a-15 and

15d-15 under the Exchange Act, that have materially affected, or are reasonably likely to materially affect, the Company's internal control over financial reporting.

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## PART II — OTHER INFORMATION

### Item 1. Legal Proceedings

The Company is subject to legal proceedings and claims that have not been fully resolved and that have arisen in the ordinary course of business. In the opinion of management, there was not at least a reasonable possibility the Company may have incurred a material loss, or a material loss in excess of a recorded accrual, with respect to loss contingencies for asserted legal and other claims. However, the outcome of legal proceedings and claims brought against the Company is subject to significant uncertainty. Therefore, although management considers the likelihood of such an outcome to be remote, if one or more of these legal matters were resolved against the Company in a reporting period for amounts in excess of management's expectations, the Company's consolidated financial statements for that reporting period could be materially adversely affected. See the risk factor "The Company could be impacted by unfavorable results of legal proceedings, such as being found to have infringed on intellectual property rights" in Part II, Item 1A of this Form 10-Q under the heading "Risk Factors." The Company settled certain matters during the second quarter of 2017 that did not individually or in the aggregate have a material impact on the Company's financial condition or operating results.

### Item 1A. Risk Factors

The following description of risk factors includes any material changes to, and supersedes the description of, risk factors associated with the Company's business previously disclosed in Part I, Item 1A of the 2016 Form 10-K and in Part II, Item 1A of the Form 10-Q for the quarter ended December 31, 2016, in each case under the heading "Risk Factors." The business, financial condition and operating results of the Company can be affected by a number of factors, whether currently known or unknown, including but not limited to those described below, any one or more of which could, directly or indirectly, cause the Company's actual financial condition and operating results to vary materially from past, or from anticipated future, financial condition and operating results. Any of these factors, in whole or in part, could materially and adversely affect the Company's business, financial condition, operating results and stock price.

The following discussion of risk factors contains forward-looking statements. These risk factors may be important to understanding other statements in this Form 10-Q. The following information should be read in conjunction with the condensed consolidated financial statements and related notes in Part I, Item 1, "Financial Statements" and Part I, Item 2, "Management's Discussion and Analysis of Financial Condition and Results of Operations" of this Form 10-Q. Because of the following factors, as well as other factors affecting the Company's financial condition and operating results, past financial performance should not be considered to be a reliable indicator of future performance, and investors should not use historical trends to anticipate results or trends in future periods.

Global and regional economic conditions could materially adversely affect the Company.

The Company's operations and performance depend significantly on global and regional economic conditions. Uncertainty about global and regional economic conditions poses a risk as consumers and businesses may postpone spending in response to tighter credit, higher unemployment, financial market volatility, government austerity programs, negative financial news, declines in income or asset values and/or other factors. These worldwide and regional economic conditions could have a material adverse effect on demand for the Company's products and services. Demand also could differ materially from the Company's expectations as a result of currency fluctuations because the Company generally raises prices on goods and services sold outside the U.S. to correspond with the effect of a strengthening of the U.S. dollar. Other factors that could influence worldwide or regional demand include changes in fuel and other energy costs, conditions in the real estate and mortgage markets, unemployment, labor and healthcare costs, access to credit, consumer confidence and other macroeconomic factors affecting consumer spending behavior. These and other economic factors could materially adversely affect demand for the Company's products and services.

In the event of financial turmoil affecting the banking system and financial markets, additional consolidation of the financial services industry, or significant financial service institution failures, there could be tightening in the credit markets, low liquidity and extreme volatility in fixed income, credit, currency and equity markets. This could have a number of effects on the Company's business, including the insolvency or financial instability of outsourcing partners or suppliers or their inability to obtain credit to finance development and/or manufacture products resulting in product delays; inability of customers, including channel partners, to obtain credit to finance purchases of the

Company's products; failure of derivative counterparties and other financial institutions; and restrictions on the Company's ability to issue new debt. Other income and expense also could vary materially from expectations depending on gains or losses realized on the sale or exchange of financial instruments; impairment charges resulting from revaluations of debt and equity securities and other investments; changes in interest rates; increases or decreases in cash balances; volatility in foreign exchange rates; and changes in fair value of derivative instruments. Increased volatility in the financial markets and overall economic uncertainty would increase the risk of the actual amounts realized in the future on the Company's financial instruments differing significantly from the fair values currently assigned to them.

Global markets for the Company's products and services are highly competitive and subject to rapid technological change, and the Company may be unable to compete effectively in these markets.

The Company's products and services compete in highly competitive global markets characterized by aggressive price cutting and resulting downward pressure on gross margins, frequent introduction of new products, short product life cycles, evolving industry standards, continual improvement in product price/performance characteristics, rapid adoption of technological and product advancements by competitors and price sensitivity on the part of consumers. The Company's ability to compete successfully depends heavily on its ability to ensure a continuing and timely introduction of innovative new products, services and technologies to the marketplace. The Company believes it is unique in that it designs and develops nearly the entire solution for its products, including the hardware, operating system, numerous software applications and related services. As a result, the Company must make significant investments in R&D. The Company currently holds a significant number of patents and copyrights and has registered and/or has applied to register numerous patents, trademarks and service marks. In contrast, many of the Company's competitors seek to compete primarily through aggressive pricing and very low cost structures, and emulating the Company's products and infringing on its intellectual property. If the Company is unable to continue to develop and sell innovative new products with attractive margins or if competitors infringe on the Company's intellectual property, the Company's ability to maintain a competitive advantage could be adversely affected.

The Company markets certain mobile communication and media devices based on the iOS mobile operating system and also markets related services, including third-party digital content and applications. The Company faces substantial competition in these markets from companies that have significant technical, marketing, distribution and other resources, as well as established hardware, software and digital content supplier relationships; and the Company has a minority market share in the global smartphone market. Additionally, the Company faces significant price competition as competitors reduce their selling prices and attempt to imitate the Company's product features and applications within their own products or, alternatively, collaborate with each other to offer solutions that are more competitive than those they currently offer. The Company competes with business models that provide content to users for free. The Company also competes with illegitimate means to obtain third-party digital content and applications. Some of the Company's competitors have greater experience, product breadth and distribution channels than the Company. Because some current and potential competitors have substantial resources and/or experience and a lower cost structure, they may be able to provide products and services at little or no profit or even at a loss. The Company also expects competition to intensify as competitors attempt to imitate the Company's approach to providing components seamlessly within their individual offerings or work collaboratively to offer integrated solutions. The Company's financial condition and operating results depend substantially on the Company's ability to continually improve iOS and iOS devices in order to maintain their functional and design advantages.

The Company is the only authorized maker of hardware using macOS, which has a minority market share in the personal computer market. This market has been contracting and is dominated by computer makers using competing operating systems, most notably Windows. In the market for personal computers and accessories, the Company faces a significant number of competitors, many of which have broader product lines, lower-priced products and a larger installed customer base. Historically, consolidation in this market has resulted in larger competitors. Price competition has been particularly intense as competitors have aggressively cut prices and lowered product margins. An increasing number of internet-enabled devices that include software applications and are smaller and simpler than traditional personal computers compete for market share with the Company's existing products. The Company's financial condition and operating results also depend on its ability to continually improve the Mac platform to maintain its functional and design advantages.

There can be no assurance the Company will be able to continue to provide products and services that compete effectively.

To remain competitive and stimulate customer demand, the Company must successfully manage frequent product introductions and transitions.

Due to the highly volatile and competitive nature of the industries in which the Company competes, the Company must continually introduce new products, services and technologies, enhance existing products and services, effectively stimulate customer demand for new and upgraded products and successfully manage the transition to these new and upgraded products. The success of new product introductions depends on a number of factors including, but

not limited to, timely and successful product development, market acceptance, the Company's ability to manage the risks associated with new product production ramp-up issues, the availability of application software for new products, the effective management of purchase commitments and inventory levels in line with anticipated product demand, the availability of products in appropriate quantities and at expected costs to meet anticipated demand and the risk that new products may have quality or other defects or deficiencies in the early stages of introduction. Accordingly, the Company cannot determine in advance the ultimate effect of new product introductions and transitions.



The Company depends on the performance of distributors, carriers and other resellers.

The Company distributes its products through cellular network carriers, wholesalers, national and regional retailers and value-added resellers, many of whom distribute products from competing manufacturers. The Company also sells its products and third-party products in most of its major markets directly to education, enterprise and government customers and consumers and small and mid-sized businesses through its retail and online stores.

Some carriers providing cellular network service for iPhone subsidize users' purchases of the device. There is no assurance that such subsidies will be continued at all or in the same amounts upon renewal of the Company's agreements with these carriers or in agreements the Company enters into with new carriers.

The Company has invested and will continue to invest in programs to enhance reseller sales, including staffing selected resellers' stores with Company employees and contractors, and improving product placement displays. These programs could require a substantial investment while providing no assurance of return or incremental revenue. The financial condition of these resellers could weaken, these resellers could stop distributing the Company's products, or uncertainty regarding demand for some or all of the Company's products could cause resellers to reduce their ordering and marketing of the Company's products.

The Company faces substantial inventory and other asset risk in addition to purchase commitment cancellation risk. The Company records a write-down for product and component inventories that have become obsolete or exceed anticipated demand or net realizable value and accrues necessary cancellation fee reserves for orders of excess products and components. The Company also reviews its long-lived assets, including capital assets held at its suppliers' facilities and inventory prepayments, for impairment whenever events or circumstances indicate the carrying amount of an asset may not be recoverable. If the Company determines that impairment has occurred, it records a write-down equal to the amount by which the carrying value of the assets exceeds its fair value. Although the Company believes its provisions related to inventory, capital assets, inventory prepayments and other assets and purchase commitments are currently adequate, no assurance can be given that the Company will not incur additional related charges given the rapid and unpredictable pace of product obsolescence in the industries in which the Company competes.

The Company must order components for its products and build inventory in advance of product announcements and shipments. Consistent with industry practice, components are normally acquired through a combination of purchase orders, supplier contracts and open orders, in each case based on projected demand. Manufacturing purchase obligations typically cover forecasted component and manufacturing requirements for periods up to 150 days. Because the Company's markets are volatile, competitive and subject to rapid technology and price changes, there is a risk the Company will forecast incorrectly and order or produce excess or insufficient amounts of components or products, or not fully utilize firm purchase commitments.

Future operating results depend upon the Company's ability to obtain components in sufficient quantities on commercially reasonable terms.

Because the Company currently obtains components from single or limited sources, the Company is subject to significant supply and pricing risks. Many components, including those that are available from multiple sources, are at times subject to industry-wide shortages and significant commodity pricing fluctuations. While the Company has entered into agreements for the supply of many components, there can be no assurance that the Company will be able to extend or renew these agreements on similar terms, or at all. A number of suppliers of components may suffer from poor financial conditions, which can lead to business failure for the supplier or consolidation within a particular industry, further limiting the Company's ability to obtain sufficient quantities of components on commercially reasonable terms. The effects of global or regional economic conditions on the Company's suppliers, described in "Global and regional economic conditions could materially adversely affect the Company" above, also could affect the Company's ability to obtain components. Therefore, the Company remains subject to significant risks of supply shortages and price increases.

The Company's new products often utilize custom components available from only one source. When a component or product uses new technologies, initial capacity constraints may exist until the suppliers' yields have matured or manufacturing capacity has increased. Continued availability of these components at acceptable prices, or at all, may be affected for any number of reasons, including if those suppliers decide to concentrate on the production of common components instead of components customized to meet the Company's requirements. The supply of components for a

new or existing product could be delayed or constrained, or a key manufacturing vendor could delay shipments of completed products to the Company.

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The Company depends on component and product manufacturing and logistical services provided by outsourcing partners, many of which are located outside of the U.S.

Substantially all of the Company's manufacturing is performed in whole or in part by a few outsourcing partners located primarily in Asia. The Company has also outsourced much of its transportation and logistics management. While these arrangements may lower operating costs, they also reduce the Company's direct control over production and distribution. It is uncertain what effect such diminished control will have on the quality or quantity of products or services, or the Company's flexibility to respond to changing conditions. Although arrangements with these partners may contain provisions for warranty expense reimbursement, the Company may remain responsible to the consumer for warranty service in the event of product defects and could experience an unanticipated product defect or warranty liability. While the Company relies on its partners to adhere to its supplier code of conduct, material violations of the supplier code of conduct could occur.

The Company relies on sole-sourced outsourcing partners in the U.S., Asia and Europe to supply and manufacture many critical components, and on outsourcing partners primarily located in Asia, for final assembly of substantially all of the Company's hardware products. Any failure of these partners to perform may have a negative impact on the Company's cost or supply of components or finished goods. In addition, manufacturing or logistics in these locations or transit to final destinations may be disrupted for a variety of reasons including, but not limited to, natural and man-made disasters, information technology system failures, commercial disputes, military actions or economic, business, labor, environmental, public health, or political issues.

The Company has invested in manufacturing process equipment, much of which is held at certain of its outsourcing partners, and has made prepayments to certain of its suppliers associated with long-term supply agreements. While these arrangements help ensure the supply of components and finished goods, if these outsourcing partners or suppliers experience severe financial problems or other disruptions in their business, such continued supply could be reduced or terminated and the net realizable value of these assets could be negatively impacted.

The Company's products and services may experience quality problems from time to time that can result in decreased sales and operating margin and harm to the Company's reputation.

The Company sells complex hardware and software products and services that can contain design and manufacturing defects. Sophisticated operating system software and applications, such as those sold by the Company, often contain "bugs" that can unexpectedly interfere with the software's intended operation. The Company's online services may from time to time experience outages, service slowdowns, or errors. Defects may also occur in components and products the Company purchases from third parties. There can be no assurance the Company will be able to detect and fix all defects in the hardware, software and services it sells. Failure to do so could result in lost revenue, significant warranty and other expenses and harm to the Company's reputation.

The Company relies on access to third-party digital content, which may not be available to the Company on commercially reasonable terms or at all.

The Company contracts with numerous third parties to offer their digital content to customers. This includes the right to sell currently available music, movies, TV shows and books. The licensing or other distribution arrangements with these third parties are for relatively short terms and do not guarantee the continuation or renewal of these arrangements on reasonable terms, if at all. Some third-party content providers and distributors currently or in the future may offer competing products and services, and could take action to make it more difficult or impossible for the Company to license or otherwise distribute their content in the future. Other content owners, providers or distributors may seek to limit the Company's access to, or increase the cost of, such content. The Company may be unable to continue to offer a wide variety of content at reasonable prices with acceptable usage rules, or continue to expand its geographic reach. Failure to obtain the right to make available third-party digital content, or to make available such content on commercially reasonable terms, could have a material adverse impact on the Company's financial condition and operating results.

Some third-party digital content providers require the Company to provide digital rights management and other security solutions. If requirements change, the Company may have to develop or license new technology to provide these solutions. There is no assurance the Company will be able to develop or license such solutions at a reasonable cost and in a timely manner. In addition, certain countries have passed or may propose and adopt legislation that would force the Company to license its digital rights management, which could lessen the protection of content and

subject it to piracy and also could negatively affect arrangements with the Company's content providers.

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The Company's future performance depends in part on support from third-party software developers. The Company believes decisions by customers to purchase its hardware products depend in part on the availability of third party software applications and services. There is no assurance that third-party developers will continue to develop and maintain software applications and services for the Company's products. If third-party software applications and services cease to be developed and maintained for the Company's products, customers may choose not to buy the Company's products.

With respect to its Mac products, the Company believes the availability of third party software applications and services depends in part on the developers' perception and analysis of the relative benefits of developing, maintaining and upgrading such software for the Company's products compared to Windows-based products. This analysis may be based on factors such as the market position of the Company and its products, the anticipated revenue that may be generated, expected future growth of Mac sales and the costs of developing such applications and services. If the Company's minority share of the global personal computer market causes developers to question the Mac's prospects, developers could be less inclined to develop or upgrade software for the Company's Mac products and more inclined to devote their resources to developing and upgrading software for the larger Windows market.

With respect to iOS devices, the Company relies on the continued availability and development of compelling and innovative software applications, including applications distributed through the App Store. iOS devices are subject to rapid technological change, and, if third-party developers are unable to or choose not to keep up with this pace of change, third-party applications might not successfully operate and may result in dissatisfied customers. As with applications for the Company's Mac products, the availability and development of these applications also depend on developers' perceptions and analysis of the relative benefits of developing, maintaining or upgrading software for the Company's iOS devices rather than its competitors' platforms, such as Android. If developers focus their efforts on these competing platforms, the availability and quality of applications for the Company's iOS devices may suffer. The Company relies on access to third-party intellectual property, which may not be available to the Company on commercially reasonable terms or at all.

Many of the Company's products include third-party intellectual property, which requires licenses from those third parties. Based on past experience and industry practice, the Company believes such licenses generally can be obtained on reasonable terms. There is, however, no assurance that the necessary licenses can be obtained on acceptable terms or at all. Failure to obtain the right to use third-party intellectual property, or to use such intellectual property on commercially reasonable terms, could preclude the Company from selling certain products or otherwise have a material adverse impact on the Company's financial condition and operating results.

The Company could be impacted by unfavorable results of legal proceedings, such as being found to have infringed on intellectual property rights.

The Company is subject to various legal proceedings and claims that have not yet been fully resolved and that have arisen in the ordinary course of business, and additional claims may arise in the future.

For example, technology companies, including many of the Company's competitors, frequently enter into litigation based on allegations of patent infringement or other violations of intellectual property rights. In addition, patent holding companies seek to monetize patents they have purchased or otherwise obtained. The intellectual property rights claims against the Company have generally increased over time and may continue to increase. In particular, the Company's cellular-enabled products compete with products from mobile communication and media device companies that hold significant patent portfolios, and the Company has faced a significant number of patent claims against it. The Company is vigorously defending infringement actions in courts in a number of U.S. jurisdictions and before the U.S. International Trade Commission, as well as internationally in various countries. The plaintiffs in these actions frequently seek injunctions and substantial damages.

Regardless of the scope or validity of such patents or other intellectual property rights, or the merits of any claims by potential or actual litigants, the Company may have to engage in protracted litigation. If the Company is found to infringe one or more patents or other intellectual property rights, regardless of whether it can develop non-infringing technology, it may be required to pay substantial damages or royalties to a third party, or it may be subject to a temporary or permanent injunction prohibiting the Company from marketing or selling certain products.

In certain cases, the Company may consider the desirability of entering into licensing agreements, although no assurance can be given that such licenses can be obtained on acceptable terms or that litigation will not occur. These

licenses may also significantly increase the Company's operating expenses.

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Regardless of the merit of particular claims, litigation may be expensive, time-consuming, disruptive to the Company's operations and distracting to management. In recognition of these considerations, the Company may enter into arrangements to settle litigation.

In management's opinion, there is not at least a reasonable possibility the Company may have incurred a material loss, or a material loss in excess of a recorded accrual, with respect to loss contingencies, including matters related to infringement of intellectual property rights. However, the outcome of litigation is inherently uncertain.

Although management considers the likelihood of such an outcome to be remote, if one or more legal matters were resolved against the Company in a reporting period for amounts in excess of management's expectations, the Company's consolidated financial statements for that reporting period could be materially adversely affected. Further, such an outcome could result in significant compensatory, punitive or trebled monetary damages, disgorgement of revenue or profits, remedial corporate measures or injunctive relief against the Company that could materially adversely affect its financial condition and operating results.

The Company is subject to laws and regulations worldwide, changes to which could increase the Company's costs and individually or in the aggregate adversely affect the Company's business.

The Company is subject to laws and regulations affecting its domestic and international operations in a number of areas. These U.S. and foreign laws and regulations affect the Company's activities including, but not limited to, in areas of labor, advertising, digital content, consumer protection, real estate, billing, e-commerce, promotions, quality of services, telecommunications, mobile communications and media, television, intellectual property ownership and infringement, tax, import and export requirements, anti-corruption, foreign exchange controls and cash repatriation restrictions, data privacy requirements, anti-competition, environmental, health and safety.

By way of example, laws and regulations related to mobile communications and media devices in the many jurisdictions in which the Company operates are extensive and subject to change. Such changes could include, among others, restrictions on the production, manufacture, distribution and use of devices, locking devices to a carrier's network, or mandating the use of devices on more than one carrier's network. These devices are also subject to certification and regulation by governmental and standardization bodies, as well as by cellular network carriers for use on their networks. These certification processes are extensive and time consuming, and could result in additional testing requirements, product modifications, or delays in product shipment dates, or could preclude the Company from selling certain products.

Compliance with these laws, regulations and similar requirements may be onerous and expensive, and they may be inconsistent from jurisdiction to jurisdiction, further increasing the cost of compliance and doing business. Any such costs, which may rise in the future as a result of changes in these laws and regulations or in their interpretation, could individually or in the aggregate make the Company's products and services less attractive to the Company's customers, delay the introduction of new products in one or more regions, or cause the Company to change or limit its business practices. The Company has implemented policies and procedures designed to ensure compliance with applicable laws and regulations, but there can be no assurance that the Company's employees, contractors, or agents will not violate such laws and regulations or the Company's policies and procedures.

The Company's business is subject to the risks of international operations.

The Company derives a significant portion of its revenue and earnings from its international operations. Compliance with applicable U.S. and foreign laws and regulations, such as import and export requirements, anti-corruption laws, tax laws, foreign exchange controls and cash repatriation restrictions, data privacy requirements, environmental laws, labor laws and anti-competition regulations, increases the costs of doing business in foreign jurisdictions. Although the Company has implemented policies and procedures to comply with these laws and regulations, a violation by the Company's employees, contractors, or agents could nevertheless occur. In some cases, compliance with the laws and regulations of one country could violate the laws and regulations of another country. Violations of these laws and regulations could materially adversely affect the Company's brand, international growth efforts and business.

The Company also could be significantly affected by other risks associated with international activities including, but not limited to, economic and labor conditions, increased duties, taxes and other costs and political instability. Margins on sales of the Company's products in foreign countries, and on sales of products that include components obtained from foreign suppliers, could be materially adversely affected by international trade regulations, including duties, tariffs and antidumping penalties. The Company is also exposed to credit and collectability risk on its trade

receivables with customers in certain international markets. There can be no assurance the Company can effectively limit its credit risk and avoid losses.

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The Company's retail stores have required and will continue to require a substantial investment and commitment of resources and are subject to numerous risks and uncertainties.

The Company's retail stores have required substantial investment in equipment and leasehold improvements, information systems, inventory and personnel. The Company also has entered into substantial operating lease commitments for retail space. Certain stores have been designed and built to serve as high-profile venues to promote brand awareness and serve as vehicles for corporate sales and marketing activities. Because of their unique design elements, locations and size, these stores require substantially more investment than the Company's more typical retail stores. Due to the high cost structure associated with the Company's retail stores, a decline in sales or the closure or poor performance of individual or multiple stores could result in significant lease termination costs, write-offs of equipment and leasehold improvements and severance costs.

Many factors unique to retail operations, some of which are beyond the Company's control, pose risks and uncertainties. These risks and uncertainties include, but are not limited to, macro-economic factors that could have an adverse effect on general retail activity, as well as the Company's inability to manage costs associated with store construction and operation, the Company's failure to manage relationships with its existing retail partners, more challenging environments in managing retail operations outside the U.S., costs associated with unanticipated fluctuations in the value of retail inventory, and the Company's inability to obtain and renew leases in quality retail locations at a reasonable cost.

Investment in new business strategies and acquisitions could disrupt the Company's ongoing business and present risks not originally contemplated.

The Company has invested, and in the future may invest, in new business strategies or acquisitions. Such endeavors may involve significant risks and uncertainties, including distraction of management from current operations, greater than expected liabilities and expenses, inadequate return of capital and unidentified issues not discovered in the Company's due diligence. These new ventures are inherently risky and may not be successful.

The Company's business and reputation may be impacted by information technology system failures or network disruptions.

The Company may be subject to information technology system failures and network disruptions. These may be caused by natural disasters, accidents, power disruptions, telecommunications failures, acts of terrorism or war, computer viruses, physical or electronic break-ins, or other events or disruptions. System redundancy may be ineffective or inadequate, and the Company's disaster recovery planning may not be sufficient for all eventualities. Such failures or disruptions could, among other things, prevent access to the Company's online stores and services, preclude retail store transactions, compromise Company or customer data, and result in delayed or cancelled orders. System failures and disruptions could also impede the manufacturing and shipping of products, delivery of online services, transactions processing and financial reporting.

There may be breaches of the Company's information technology systems that materially damage business partner and customer relationships, curtail or otherwise adversely impact access to online stores and services, or subject the Company to significant reputational, financial, legal and operational consequences.

The Company's business requires it to use and store customer, employee and business partner personally identifiable information ("PII"). This may include, among other information, names, addresses, phone numbers, email addresses, contact preferences, tax identification numbers and payment account information. Although malicious attacks to gain access to PII affect many companies across various industries, the Company is at a relatively greater risk of being targeted because of its high profile and the amount of PII it manages.

The Company requires user names and passwords in order to access its information technology systems. The Company also uses encryption and authentication technologies designed to secure the transmission and storage of data and prevent access to Company data or accounts. As with all companies, these security measures are subject to third-party security breaches, employee error, malfeasance, faulty password management or other irregularities. For example, third parties may attempt to fraudulently induce employees or customers into disclosing user names, passwords or other sensitive information, which may in turn be used to access the Company's information technology systems. To help protect customers and the Company, the Company monitors accounts and systems for unusual activity and may freeze accounts under suspicious circumstances, which may result in the delay or loss of customer orders.



The Company devotes significant resources to network security, data encryption and other security measures to protect its systems and data, but these security measures cannot provide absolute security. To the extent the Company was to experience a breach of its systems and was unable to protect sensitive data, such a breach could materially damage business partner and customer relationships, and curtail or otherwise adversely impact access to online stores and services. Moreover, if a computer security breach affects the Company's systems or results in the unauthorized release of PII, the Company's reputation and brand could be materially damaged, use of the Company's products and services could decrease, and the Company could be exposed to a risk of loss or litigation and possible liability. While the Company maintains insurance coverage that, subject to policy terms and conditions and subject to a significant self-insured retention, is designed to address certain aspects of cyber risks, such insurance coverage may be insufficient to cover all losses or all types of claims that may arise in the continually evolving area of cyber risk. The Company is also subject to payment card association rules and obligations under its contracts with payment card processors. Under these rules and obligations, if information is compromised, the Company could be liable to payment card issuers for associated expenses and penalties. In addition, if the Company fails to follow payment card industry security standards, even if no customer information is compromised, the Company could incur significant fines or experience a significant increase in payment card transaction costs.

The Company's business is subject to a variety of U.S. and international laws, rules, policies and other obligations regarding data protection.

The Company is subject to federal, state and international laws relating to the collection, use, retention, security and transfer of PII. In many cases, these laws apply not only to third-party transactions, but also may restrict transfers of PII among the Company and its international subsidiaries. Several jurisdictions have passed laws in this area, and other jurisdictions are considering imposing additional restrictions. These laws continue to develop and may be inconsistent from jurisdiction to jurisdiction. Complying with emerging and changing international requirements may cause the Company to incur substantial costs or require the Company to change its business practices. Noncompliance could result in significant penalties or legal liability.

The Company makes statements about its use and disclosure of PII through its privacy policy, information provided on its website and press statements. Any failure by the Company to comply with these public statements or with other federal, state or international privacy-related or data protection laws and regulations could result in proceedings against the Company by governmental entities or others. Penalties could include ongoing audit requirements or significant legal liability.

The Company's success depends largely on the continued service and availability of key personnel.

Much of the Company's future success depends on the continued availability and service of key personnel, including its Chief Executive Officer, executive team and other highly skilled employees. Experienced personnel in the technology industry are in high demand and competition for their talents is intense, especially in Silicon Valley, where most of the Company's key personnel are located.

The Company's business may be impacted by political events, war, terrorism, public health issues, natural disasters and other business interruptions.

War, terrorism, geopolitical uncertainties, public health issues and other business interruptions have caused and could cause damage or disruption to international commerce and the global economy, and thus could have a material adverse effect on the Company, its suppliers, logistics providers, manufacturing vendors and customers, including channel partners. The Company's business operations are subject to interruption by, among others, natural disasters, whether as a result of climate change or otherwise, fire, power shortages, nuclear power plant accidents and other industrial accidents, terrorist attacks and other hostile acts, labor disputes, public health issues and other events beyond its control. Such events could decrease demand for the Company's products, make it difficult or impossible for the Company to make and deliver products to its customers, including channel partners, or to receive components from its suppliers, and create delays and inefficiencies in the Company's supply chain. While the Company's suppliers are required to maintain safe working environments and operations, an industrial accident could occur and could result in disruption to the Company's business and harm to the Company's reputation. Should major public health issues, including pandemics, arise, the Company could be adversely affected by more stringent employee travel restrictions, additional limitations in freight services, governmental actions limiting the movement of products between regions, delays in production ramps of new products and disruptions in the operations of the Company's manufacturing vendors

and component suppliers. The majority of the Company's R&D activities, its corporate headquarters, information technology systems and other critical business operations, including certain component suppliers and manufacturing vendors, are in locations that could be affected by natural disasters. In the event of a natural disaster, the Company could incur significant losses, require substantial recovery time and experience significant expenditures in order to resume operations.

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The Company expects its quarterly revenue and operating results to fluctuate.

The Company's profit margins vary across its products and distribution channels. The Company's software, accessories, and service and support contracts generally have higher gross margins than certain of the Company's other products. Gross margins on the Company's hardware products vary across product lines and can change over time as a result of product transitions, pricing and configuration changes, and component, warranty, and other cost fluctuations. The Company's direct sales generally have higher associated gross margins than its indirect sales through its channel partners. In addition, the Company's gross margin and operating margin percentages, as well as overall profitability, may be materially adversely impacted as a result of a shift in product, geographic or channel mix, component cost increases, the strengthening U.S. dollar, price competition, or the introduction of new products, including those that have higher cost structures with flat or reduced pricing.

The Company has typically experienced higher net sales in its first quarter compared to other quarters due in part to seasonal holiday demand. Additionally, new product introductions can significantly impact net sales, product costs and operating expenses. Further, the Company generates a majority of its net sales from a single product and a decline in demand for that product could significantly impact quarterly net sales. The Company could also be subject to unexpected developments late in a quarter, such as lower-than-anticipated demand for the Company's products, issues with new product introductions, an internal systems failure, or failure of one of the Company's logistics, components supply, or manufacturing partners.

The Company's stock price is subject to volatility.

The Company's stock price has experienced substantial price volatility in the past and may continue to do so in the future. Additionally, the Company, the technology industry and the stock market as a whole have experienced extreme stock price and volume fluctuations that have affected stock prices in ways that may have been unrelated to these companies' operating performance. Price volatility over a given period may cause the average price at which the Company repurchases its own stock to exceed the stock's price at a given point in time. The Company believes its stock price should reflect expectations of future growth and profitability. The Company also believes its stock price should reflect expectations that its cash dividend will continue at current levels or grow and that its current share repurchase program will be fully consummated. Future dividends are subject to declaration by the Company's Board of Directors, and the Company's share repurchase program does not obligate it to acquire any specific number of shares. If the Company fails to meet expectations related to future growth, profitability, dividends, share repurchases or other market expectations, its stock price may decline significantly, which could have a material adverse impact on investor confidence and employee retention.

The Company's financial performance is subject to risks associated with changes in the value of the U.S. dollar versus local currencies.

The Company's primary exposure to movements in foreign currency exchange rates relates to non-U.S. dollar-denominated sales and operating expenses worldwide. Weakening of foreign currencies relative to the U.S. dollar adversely affects the U.S. dollar value of the Company's foreign currency-denominated sales and earnings, and generally leads the Company to raise international pricing, potentially reducing demand for the Company's products. Margins on sales of the Company's products in foreign countries and on sales of products that include components obtained from foreign suppliers, could be materially adversely affected by foreign currency exchange rate fluctuations. In some circumstances, for competitive or other reasons, the Company may decide not to raise local prices to fully offset the dollar's strengthening, or at all, which would adversely affect the U.S. dollar value of the Company's foreign currency-denominated sales and earnings. Conversely, a strengthening of foreign currencies relative to the U.S. dollar, while generally beneficial to the Company's foreign currency-denominated sales and earnings, could cause the Company to reduce international pricing and incur losses on its foreign currency derivative instruments, thereby limiting the benefit. Additionally, strengthening of foreign currencies may also increase the Company's cost of product components denominated in those currencies, thus adversely affecting gross margins.

The Company uses derivative instruments, such as foreign currency forward and option contracts, to hedge certain exposures to fluctuations in foreign currency exchange rates. The use of such hedging activities may not offset any, or more than a portion, of the adverse financial effects of unfavorable movements in foreign exchange rates over the limited time the hedges are in place.

The Company is exposed to credit risk and fluctuations in the market values of its investment portfolio.

Given the global nature of its business, the Company has both domestic and international investments. Credit ratings and pricing of the Company's investments can be negatively affected by liquidity, credit deterioration, financial results, economic risk, political risk, sovereign risk or other factors. As a result, the value and liquidity of the Company's cash, cash equivalents and marketable securities may fluctuate substantially. Therefore, although the Company has not realized any significant losses on its cash, cash equivalents and marketable securities, future fluctuations in their value could result in a significant realized loss.

The Company is exposed to credit risk on its trade accounts receivable, vendor non-trade receivables and prepayments related to long-term supply agreements, and this risk is heightened during periods when economic conditions worsen. The Company distributes its products through third-party cellular network carriers, wholesalers, retailers and value-added resellers. The Company also sells its products directly to small and mid-sized businesses and education, enterprise and government customers. A substantial majority of the Company's outstanding trade receivables are not covered by collateral, third-party financing arrangements or credit insurance. The Company's exposure to credit and collectability risk on its trade receivables is higher in certain international markets and its ability to mitigate such risks may be limited. The Company also has unsecured vendor non-trade receivables resulting from purchases of components by outsourcing partners and other vendors that manufacture sub-assemblies or assemble final products for the Company. In addition, the Company has made prepayments associated with long-term supply agreements to secure supply of inventory components. As of April 1, 2017, a significant portion of the Company's trade receivables was concentrated within cellular network carriers, and its vendor non-trade receivables and prepayments related to long-term supply agreements were concentrated among a few individual vendors located primarily in Asia. While the Company has procedures to monitor and limit exposure to credit risk on its trade and vendor non-trade receivables, as well as long-term prepayments, there can be no assurance such procedures will effectively limit its credit risk and avoid losses.

The Company could be subject to changes in its tax rates, the adoption of new U.S. or international tax legislation or exposure to additional tax liabilities.

The Company is subject to taxes in the U.S. and numerous foreign jurisdictions, including Ireland, where a number of the Company's subsidiaries are organized. Due to economic and political conditions, tax rates in various jurisdictions may be subject to significant change. The Company's effective tax rates could be affected by changes in the mix of earnings in countries with differing statutory tax rates, changes in the valuation of deferred tax assets and liabilities, or changes in tax laws or their interpretation, including in the U.S. and Ireland.

The Company is also subject to the examination of its tax returns and other tax matters by the U.S. Internal Revenue Service and other tax authorities and governmental bodies. The Company regularly assesses the likelihood of an adverse outcome resulting from these examinations to determine the adequacy of its provision for taxes. There can be no assurance as to the outcome of these examinations. If the Company's effective tax rates were to increase, particularly in the U.S. or Ireland, or if the ultimate determination of the Company's taxes owed is for an amount in excess of amounts previously accrued, the Company's financial condition, operating results and cash flows could be adversely affected.

## Item 2. Unregistered Sales of Equity Securities and Use of Proceeds

## Purchases of Equity Securities by the Issuer and Affiliated Purchasers

Share repurchase activity during the three months ended April 1, 2017 was as follows (in millions, except number of shares, which are reflected in thousands, and per share amounts):

Periods	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 <sup>(1)</sup>
January 1, 2017 to February 4, 2017:				
Open market and privately negotiated purchases	14,505	\$ 119.74	14,505	
February 5, 2017 to March 4, 2017:				
November 2016 ASR	6,343	(2)	6,343	
February 2017 ASR	17,527	(3) (3)	17,527	(3)
Open market and privately negotiated purchases	10,386	\$ 134.19	10,386	
March 5, 2017 to April 1, 2017:				
Open market and privately negotiated purchases	6,179	\$ 140.72	6,179	
Total	54,940			\$ 24,023

(1) As of April 1, 2017, the Company had an authorized share repurchase program of \$175 billion of the Company's common stock, of which \$151 billion had been utilized. The remaining \$24 billion in the table represents the amount available to repurchase shares under the authorized repurchase program as of April 1, 2017. The Company's share repurchase program does not obligate it to acquire any specific number of shares. Under the program, shares may be repurchased in privately negotiated and/or open market transactions, including under plans complying with Rule 10b5-1 under the Exchange Act.

(2) In November 2016, the Company entered into an accelerated share repurchase arrangement ("ASR") to purchase up to \$6.0 billion of the Company's common stock. In February 2017, the purchase period for this ASR ended and an additional 6.3 million shares were delivered and retired. In total, 51.2 million shares were delivered under this ASR at an average repurchase price of \$117.29.

(3) In February 2017, the Company entered into a new ASR to purchase up to \$3.0 billion of the Company's common stock. In exchange for an up-front payment of \$3.0 billion, the financial institution party to the arrangement committed to deliver shares to the Company during the ASR's purchase period, which will end in May 2017. The total number of shares ultimately delivered, and therefore the average price paid per share, will be determined at the end of the applicable purchase period based on the volume-weighted average price of the Company's common stock during that period.

## Item 3. Defaults Upon Senior Securities

None.

## Item 4. Mine Safety Disclosures

Not applicable.

## Item 5. Other Information

None.



Item 6. Exhibits  
Exhibit Index

Exhibit Number	Exhibit Description	Incorporated by Reference		
		Form	Exhibit	Filing Date/ Period End Date
4.1	<u>Officer's Certificate of the Registrant, dated as of February 9, 2017, including forms of global notes representing the Floating Rate Notes due 2019, Floating Rate Notes due 2020, Floating Rate Notes due 2022, 1.550% Notes due 2019, 1.900% Notes due 2020, 2.500% Notes due 2022, 3.000% Notes due 2024, 3.350% Notes due 2027 and 4.250% Notes due 2047.</u>	8-K	4.1	2/9/17
4.2	<u>Officer's Certificate of the Registrant, dated as of March 3, 2017, including form of global note representing 4.300% Notes due 2047.</u>	8-K	4.1	3/3/17
31.1*	<u>Rule 13a-14(a) / 15d-14(a) Certification of Chief Executive Officer.</u>			
31.2*	<u>Rule 13a-14(a) / 15d-14(a) Certification of Chief Financial Officer.</u>			
32.1**	<u>Section 1350 Certifications of Chief Executive Officer and Chief Financial Officer.</u>			
101.INS*	XBRL Instance Document.			
101.SCH*	XBRL Taxonomy Extension Schema Document.			
101.CAL*	XBRL Taxonomy Extension Calculation Linkbase Document.			
101.DEF*	XBRL Taxonomy Extension Definition Linkbase Document.			
101.LAB*	XBRL Taxonomy Extension Label Linkbase Document.			
101.PRE*	XBRL Taxonomy Extension Presentation Linkbase Document.			

\* Filed herewith.  
\*\* Furnished herewith.

**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.

May 3, 2017 Apple Inc.

By: /s/ Luca Maestri  
Luca Maestri  
Senior Vice President,  
Chief Financial Officer