Annual Report 2020



Microsoft

Dear shareholders, colleagues, customers, and partners:

While the start of a new decade typically brings hope, we quickly saw the world come to a near standstill in 2020, confronted by compounding crises: a public health and economic crisis, persistent issues of systemic racial injustice and inequity, and the devastating effects of climate change. It is easy to fall prey to pessimism, or the sense that we individually or as a company can't make a difference. But helplessness is corrosive to hope, and hope plus work is what is required. Amid this disruption, what's clear is that we have a once-in-a-generation opportunity to harness digital technology to define the world we want to live in. And for that, I am optimistic.

It is in times like these that our ability to stay true to Microsoft's mission and corporate purpose is of the utmost importance. As a company, we are steadfast in **our mission to empower every person and every organization on the planet to achieve more.** Our mission is enduring. It drives who we are and everything we do, emphasizing our passion to empower both people and the lasting institutions they build. And it means we must always use technology to help address the world's challenges, not create new ones.

I'm proud of how our ecosystem of customers and partners has stepped up over the past year to help people and organizations in every country use technology to be resilient and transform during the most trying of circumstances. We've acted as digital first responders to the world's first responders, supporting those on the front lines, from healthcare, to education, to public sector, to critical manufacturing, grocery, and retail. And we're helping organizations navigate the response, recovery, and reimagine phases of the crisis, equipping them not only to stay open for business but to innovate. We've witnessed years of digital transformation in mere months.

Amid this rapid change, we delivered strong results: Our commercial cloud surpassed $50 billion in revenue for the first time – up 36 percent year-over-year. All-up, we delivered $143 billion in revenue, $53 billion in operating income, and more than $60 billion in operating cash flow – and returned $35 billion to shareholders.

OUR OPPORTUNITY

Although this year has taught us that no business is 100 percent resilient, those fortified by digital technology are more resilient and more capable of transforming when faced with sweeping changes like those we are experiencing. The way people interact with businesses is fundamentally shifting, and there is no going back. Digital technology is the most malleable tool ever created, and we believe that businesses that use it to build their own digital capability will recover faster and emerge stronger. At Microsoft, we call this dynamic *tech intensity*: adopting best-in-class digital tools and platforms for the purpose of building new, proprietary products and services.

I've been inspired by the ingenuity and creativity of so many people and organizations in every industry around the world applying tech intensity to address big challenges, including those created by COVID-19:

- In healthcare, Dr. Amanda Randles at Duke University is using the power of Azure to conduct hundreds of millions of simulations required to help more patients have access to critical ventilators.
- In the public sector, the state of California built 90 percent of its COVID-19 infrastructure with GitHub and Azure DevOps, reducing the time it takes to stand up a new website from 18 months to just three hours.
- In telecom, two analysts at T-Mobile used Power Platform to build an app that helped the company keep retail associates employed and keep customers, including first responders, connected during the critical first weeks of the crisis.
- In retail, Patagonia is using Dynamics 365 to ship inventory directly from a store or from a warehouse, optimizing to send single shipments to customers, while reducing the load on all locations.
- In education, the University of Bologna in Italy moved 90 percent of courses for its 80,000 students online to Microsoft Teams within three days – a first in the university's 900-plus year history.
- And, in sports, the NBA is using our technology to reimagine the game experience so fans can feel like they're together from the safety of their homes and players can experience the energy of cheering fans – virtually – in the arena.

We are living in the era of the intelligent cloud and intelligent edge, which is being shaped by rapid advances in distributed computing, ambient intelligence, and multisense, multidevice experiences. This means the places we go and the things we interact with will increasingly become digitized, creating new opportunities and new breakthroughs: from precision medicine to precision agriculture, from personalized e-commerce to personalized education, and from connected manufacturing floors to connected homes.

Our collective opportunity is to channel this intelligent cloud and intelligent edge era into tech intensity for every organization on the planet. Our customer solution areas were built for this era. They enable people, organizations, and entire industries to not only thrive but reimagine the world. So organizations can empower their employees, fostering a new culture for hybrid work; engage customers intelligently and virtually; transform products with new business models; and optimize operations to keep customers and employees safe and secure.

Across our customer solution areas, we are expanding our opportunity to help every organization in every industry build their tech intensity – with a business model that is trusted and aligned with their success.

Applications and Infrastructure

More than ever, organizations are relying on Azure to stay up and running and support critical workloads, from healthcare triage with AI-assisted bots, to digital twins in manufacturing, to e-commerce in retail. Today, leaders in every industry – including 95 percent of the Fortune 500 – run on Azure. We are building Azure as the world's computer to support them, with more datacenter regions than any other provider – now 61.

Fifty billion devices will come online by 2030, and Azure is the only cloud that extends to the edge, with consistency across operating models, development models, and infrastructure stack. Azure Arc enables organizations to deploy Azure services anywhere and extend Azure management to any infrastructure. Azure Stack Edge brings rapid machine learning inferencing closer to where data is generated, including the harshest of conditions, like disaster response. Our acquisitions of Affirmed and Metaswitch, along with new Azure Edge Zones, expand our offerings for telecom operators as they move to 5G. And, with Azure Orbital, we're taking our infrastructure to space, enabling anyone to access satellite data and capabilities from Azure.

Data and AI

There will be 175 zettabytes of data by 2025, and processing this data in real time will be an imperative for every organization. At the data layer, Azure is the only cloud with limitless data and analytics capabilities. Azure Synapse brings together big data analytics and data warehousing, enabling data scientists to generate immediate insights from structured and unstructured data. And together with Azure SQL Hyperscale, Cosmos DB, and our other data services, we are able to deliver a cloud-native data estate for every organization.

In AI, we have the most comprehensive portfolio of tools, frameworks, and infrastructure. Azure Cognitive Services makes it easier to build applications that see, hear, speak, search, understand, and accelerate decision-making. Azure Machine Learning helps organizations build and deploy models faster, while ensuring they can do so responsibly and safely. And, we are pushing the bounds of how AI can generalize learning beyond narrow domains, collaborating with OpenAI on a supercomputing platform to train and run AI models of unprecedented scale. Their new GPT-3 model was trained on our Azure AI supercomputer and constitutes a new breakthrough in natural language understanding and generation, promising breakthrough scenarios within our products and those of our customers, when safely deployed.

Developer Tools

Today, the majority of job openings for developers are outside the tech sector, and developers will increasingly drive and influence every business process and function. We have the most used and loved developer tools to build any app for any platform. With the world's most popular code editing tools – Visual Studio and VS Code – developers are more productive than ever. With GitHub, more than 50 million developers across 3 million organizations, including

the majority of the Fortune 50, are able to collaborate and build software together. And, with Azure, they have best-in-class services to build cloud-native apps and modernize existing ones.

This year, we went further to give developers new tools to power remote development, productivity, and collaboration, wherever they are. Codespaces brings together the best of GitHub, Visual Studio, and Azure to help developers go from code to cloud in seconds. VS Live Share enables real-time collaboration between developers, regardless of their location. And with Azure Communications Services, any developer can integrate rich communications APIs into their applications across any device, on any platform, using the same reliable and secure infrastructure that powers Teams.

Power Platform

500 million apps will be created by 2023 to drive transformation and productivity for every organization. To accelerate this, we must enable a new category of developers – citizen developers – equipping domain experts with tools that are low-code or no-code to create solutions that solve their unique business needs and help them better collaborate with professional developers. With Power Platform, anyone can become a citizen developer, able to create an application, build a virtual agent, automate a workflow, and analyze data in hours or days, not weeks or months.

Power BI is the clear leader in business intelligence in the cloud. Power Virtual Agents enables anyone to build an intelligent bot with just a point and click. And Power Automate enables customers to automate manual business processes across both legacy and modern applications.

Modern Workplace

Microsoft 365 is empowering people and organizations to be productive and secure as they adapt to more fluid ways of working and learning. The PC has been mission-critical across work, school, and life to sustain productivity in a remote everything world. More than 1 billion active devices now run Windows 10, and Office 365 usage is higher than ever. New Microsoft Edge – with enterprise-class security – protects individuals' privacy online and makes it easier to find information at work. And with Surface, we are reimagining every layer of the stack – from how we infuse AI from the silicon up, to device form factors, to the role of operating systems – investing across form and function to create new device categories.

The past six months have served as the largest at-scale experiment we've ever seen for remote work. We've been studying this closely to understand the changing nature of productivity and are applying these learnings to inform how we build our products. We think about the future of work through three vectors. First, we are creating a system of collaboration for every organization. Work doesn't begin and end inside a meeting, and with Teams, we are focused on the entire workflow around a meeting – before, during, and after. It's the only solution with meetings, calls, chat, content collaboration with Office, and business process workflows, in a secure, integrated user experience. Second, learning in the flow of work will be increasingly important. A new Teams app will help organizations skill, reskill, and upskill employees, surfacing learning content from LinkedIn Learning and other content providers. Finally, prioritizing employee well-being is core to an organization's success. New capabilities like Together mode in Teams help reduce cognitive load, while a new "virtual commute" will provide much-needed structure for the remote workday.

Business Applications

Dynamics 365 is helping organizations in every industry digitize their business operations and make every part of their operations remote, from manufacturing, to supply-chain management, to sales and customer service, including new scenarios like contactless shopping. As much as 73 percent of the data in the world is still not being analyzed. And from Dynamics 365 Customer Insights for personalized customer experiences and Dynamics 365 Commerce for omnichannel retail, Dynamics 365 is the only AI-powered business cloud that gives customers a 360-degree view of their business to unify data and unlock insights. And the combination of LinkedIn Sales Navigator and Dynamics 365 gives sales professionals tools for more effective remote selling.

Amid a rapidly changing jobs market, LinkedIn's role in creating economic opportunity for every member of the global workforce has never been more acute. LinkedIn is where more than 706 million professionals around the world go to connect, learn, and plan for the future. People are turning to LinkedIn Learning more than ever to acquire new skills. And we are helping organizations attract, retain, and develop the best talent with our portfolio of Talent Solutions, Talent Insights, and Glint.

Security

Identity, security, management, and compliance underlie our entire tech stack. Cybercrime will cost businesses, governments, and individuals $1 trillion this year, and the shift to remote everything has only increased the need for a "Zero Trust" architecture that reduces both cost and complexity. We are the only company that offers integrated, end-to-end capabilities to protect people and organizations.

In identity, Azure Active Directory now provides identity and access management to more than 345 million monthly active users across more than 200,000 organizations. In security, Defender offers broad coverage, spanning identities, cloud apps, devices, IoT, and more. It complements Azure Sentinel, which analyzes security signals across the entire organization, using AI to detect, investigate, and automatically remediate threats. In device and data management, Microsoft Endpoint Manager monitors and manages an organization's devices in a unified management platform. And, in compliance, we provide tools to help organizations govern their data and comply with increasing regulatory requirements.

Gaming

Gaming is the most expansive category in the entertainment industry. Three billion people around the world look to gaming for entertainment, community, and achievement, and our ambition is to empower each of them, wherever they play. We saw record engagement and monetization this year, led by strength on and off console, as people everywhere turn to gaming to connect, socialize, and play with their friends during a time of social distancing.

Our Xbox Game Pass service now has more than 15 million subscribers. Quality differentiated content – from *Flight Simulator* to *Minecraft* – is the engine behind the service's growth, and our pending acquisition of ZeniMax Media, one of the world's largest, privately held game developers and publishers, will add iconic franchises to the more than 100 high-quality games already available. We're also transforming how games are distributed, played, and viewed, bringing cloud gaming to Game Pass, so subscribers can stream games to a phone or tablet and play along with nearly 100 million Xbox Live players.

OUR PURPOSE

As we pursue our mission, we also recognize our enormous responsibility to ensure the technology we build benefits everyone on the planet, including the planet itself. Our customers see this urgent need and are looking to us – in partnership with them – to take action. We're committed to working across the public and private sectors to foster partnerships and solutions that will have lasting impact and redefine what "achieve more" means for the world. For us, "achieve more" has four important attributes:

Support inclusive economic opportunity

First, we must ensure that the economic growth we drive is inclusive. This starts with protecting public health. COVID-19 has underscored that without a healthy society, we cannot sustain a healthy economy. That's why, through our AI for Health initiative, we're empowering those working to tackle some of the toughest challenges in global health, including those on the front lines of COVID-19 research.

It also requires that we equip everyone with the skills, technology, and opportunity to pursue the in-demand jobs of a changing economy. We're accelerating efforts to close the skills and broadband gaps, ensuring underrepresented and overlooked communities can compete on equal ground. COVID-19 has intensified the need for these efforts, forcing tens of millions of people out of work. That's why we're bringing together assets from across Microsoft, inclusive of LinkedIn and GitHub, to help 25 million job seekers gain digital skills for in-demand roles. We are also

working to expand broadband access to 40 million unserved and underserved people in rural areas globally, and to 3 million people in unserved and rural communities in the US by July 2022.

We also prioritize accessibility in our culture, products, and services, ensuring we use technology to design a more accessible world for the 1 billion-plus people around the world with disabilities. As we continue our own accessibility journey, we seek to inspire and enable others to advance theirs, including through our five-year investment in AI for Accessibility.

Nonprofits are on the front lines of solving some of the world's most pressing challenges. We make our technology affordable and accessible to nonprofit organizations around the world, enabling them to drive greater impact for the causes and communities they serve. This year, we provided $1.9 billion in donated or discounted products and services to help 243,000 nonprofits better serve their communities. And our employees donated an additional $221 million (including company match) through our employee giving program to the organizations and causes they care about.

Protect fundamental rights

Second, we unequivocally support the fundamental rights of all people, from defending democracy to addressing systemic racial injustice and inequity around the world. Recent events are shining a bright light on how much work there is still to do. Seeing injustice in the world calls us all to take action.

We're committed to addressing racial injustice and inequity for the Black and African American community in the United States and for vulnerable communities globally. This starts with our own culture at Microsoft, extends to how we engage our suppliers and partners to create change, and includes strengthening our communities. Our efforts include investing an additional $150 million to advance racial justice and includes work on our own cultural transformation, doubling the number of Black-owned suppliers in our ecosystem, doubling the percentage of our transaction volumes through Black-owned financial institutions, and accelerating our justice reform initiatives.

But we can't stop there. Democracy itself is under attack. That's why we are helping protect the integrity of our democratic processes and institutions around the world through our Defending Democracy Program, which works with governments, NGOs, academics, and industry to explore technological solutions to preserve and protect electoral processes and to defend against disinformation.

Commit to a sustainable future

Third, we must protect our most finite resource – the planet – by working toward a more sustainable future. Over the past year, we've set ambitious climate goals and outlined detailed plans to achieve them, including to be carbon negative, zero waste, and water positive by 2030. We are also building a new planetary computing platform to help manage Earth's natural systems.

Addressing the climate crisis is good for the planet and good for Microsoft. That's why we're innovating and empowering customers, partners, NGOs, and governments around the world with technology to help them set and achieve their own climate goals, including the creation of a $1 billion Climate Innovation Fund to accelerate innovation.

Earn trust

Finally, we are committed to building trust in technology and its use. Without trust, none of our progress is possible. For Microsoft, trust is built on privacy, security, the responsible use of AI, and transparency.

Our approach to privacy and data protection is grounded in our belief that customers own their own data. Our privacy principles include a commitment to be transparent in our privacy practices, to offer meaningful privacy choices, and to responsibly manage the data we store and process. It's why we were early supporters of the European Union's General Data Protection Regulation (GDPR) and why we were the first major technology company

to expand GDPR's core rights to all our customers around the world. To date, more than 43 million people have visited these tools.

Security is a central challenge in the digital age. In an increasingly complex world, technology alone is not enough to combat increasing threats. It also requires partnerships, both with governments and industries. Our Digital Crimes Unit – an international team of technical, legal, and business experts – has coordinated with partners across countries to disrupt threats targeting governments, universities, human rights organizations, individuals, and more. This year, for example, they took control of domains being used to send COVID-19-themed phishing emails in 62 countries.

AI has proved itself to be a powerful tool for tackling the kinds of challenges that this year has highlighted. However, when we build AI, we must do so responsibly, taking a principled approach and asking difficult questions, like not what technology can do, but what should it do? Fairness, reliability and safety, privacy and security, inclusiveness, transparency, and accountability are the ethical principles that guide our work and advocacy. Our Office of Responsible AI helps ensure our products adhere to these principles. We've released guidelines, software development tools, and other resources to enable our developer community to do the same.

Finally, transparency is foundational to trust, so we provide clear information on how we run our business and how we work with customers and partners. We provide details on our CSR Reports Hub covering everything from law enforcement access to data, to environmental data, details on our political activities, workforce demographics, and human rights.

OUR CULTURE

Ultimately, we will only achieve our mission if we live our culture. It is at the root of every decision we make. We fundamentally believe that we need a culture founded in a growth mindset. It starts with a belief that everyone can grow and develop; that potential is nurtured, not predetermined; and that anyone can change their mindset. It's not by claiming a growth mindset but by knowing that we are imperfect but can learn and get better that we can close the gap between our espoused culture and the lived experience for every employee at the company.

Our success is dependent on our customers' success, and we need to obsess about them – listening and then innovating to meet their unmet and unarticulated needs. No customer of ours cares about our organizational boundaries, and we need to operate as One Microsoft to deliver the best solutions for them. Finally, we need to actively seek diversity and embrace inclusion to best serve our customers around the world and create a culture where everyone can do their best work. Diversity and inclusion continues to be a core priority for every employee at Microsoft as part of our annual performance and development approach. This past year, we expanded our global allyship program, adapting learning experiences for the work from home conditions of COVID-19. As we reflect on our opportunity to address racial injustice, we announced our aspiration to increase representation and strengthen our culture of inclusion, including a commitment to double the number of Black and African American and Hispanic and Latinx people managers, senior individual contributors, and senior leaders in the US by 2025.

If we commit to being customer obsessed, operating as One Microsoft, and becoming more diverse and inclusive, I believe there is no limit to what we can achieve.

The world is at an inflection point, and digital technology will be key to defining what comes next. Over the next decade, technology spending as a percentage of gross domestic product is projected to double. And, we are well positioned to not only participate in that growth but drive it by expanding our impact and building the key technologies that empower every person and every organization on the planet to achieve more.



Satya Nadella
Chief Executive Officer
October 13, 2020

FINANCIAL HIGHLIGHTS

(In millions, except per share amounts)

Year Ended June 30,	2020	2019 [a]	2018	2017 [d][e]	2016 [d]
Revenue	**$143,015**	$125,843	$110,360	$ 96,571	$ 91,154
Gross margin	**96,937**	82,933	72,007	62,310	58,374
Operating income	**52,959**	42,959	35,058	29,025 [f]	26,078 [g]
Net income	**44,281**	39,240 [b]	16,571 [c]	25,489 [f]	20,539 [g]
Diluted earnings per share	**5.76**	5.06 [b]	2.13 [c]	3.25 [f]	2.56 [g]
Cash dividends declared per common share	**2.04**	1.84	1.68	1.56	1.44
Cash, cash equivalents, and short-term investments	**136,527**	133,819	133,768	132,981	113,240
Total assets	**301,311**	286,556	258,848	250,312	202,897
Long-term obligations	**110,697**	114,806	117,642	106,856	66,705
Stockholders' equity	**118,304**	102,330	82,718	87,711	83,090

(a) *GitHub has been included in our consolidated results of operations starting on the October 25, 2018 acquisition date*.
(b) *Includes a $2.6 billion net income tax benefit related to intangible property transfers and a $157 million net charge related to the enactment of the Tax Cuts and Jobs Act ("TCJA"), which together increased net income and diluted earnings per share ("EPS") by $2.4 billion and $0.31, respectively. Refer to Note 12 – Income Taxes of the Notes to Financial Statements.*
(c) *Includes a $13.7 billion net charge related to the enactment of the TCJA, which decreased net income and diluted EPS by $13.7 billion and $1.75, respectively. Refer to Note 12 – Income Taxes of the Notes to Financial Statements.*
(d) *Reflects the impact of the adoption of new accounting standards in fiscal year 2018 related to revenue recognition and leases.*
(e) *LinkedIn has been included in our consolidated results of operations starting on the December 8, 2016 acquisition date.*
(f) *Includes $306 million of employee severance expenses primarily related to our sales and marketing restructuring plan, which decreased operating income, net income, and diluted EPS by $306 million, $243 million, and $0.04, respectively.*
(g) *Includes $630 million of asset impairment charges related to our Phone business and $480 million of restructuring charges associated with our Phone business restructuring plans, which together decreased operating income, net income, and diluted EPS by $1.1 billion, $895 million, and $0.11, respectively.*

ISSUER PURCHASES OF EQUITY SECURITIES, DIVIDENDS, AND STOCK PERFORMANCE

SHARE REPURCHASES AND DIVIDENDS

Share Repurchases

On September 20, 2016, our Board of Directors approved a share repurchase program authorizing up to $40.0 billion in share repurchases. This share repurchase program commenced in December 2016 and was completed in February 2020.

On September 18, 2019, our Board of Directors approved a share repurchase program authorizing up to $40.0 billion in share repurchases. This share repurchase program commenced in February 2020, following completion of the program approved on September 20, 2016, has no expiration date, and may be terminated at any time. As of June 30, 2020, $31.7 billion remained of this $40.0 billion share repurchase program.

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

(In millions)	Shares	Amount	Shares	Amount	Shares	Amount
Year Ended June 30,		2020		2019		2018
First Quarter	**29**	**$ 4,000**	24	$ 2,600	22	$ 1,600
Second Quarter	**32**	**4,600**	57	6,100	22	1,800
Third Quarter	**37**	**6,000**	36	3,899	34	3,100
Fourth Quarter	**28**	**5,088**	33	4,200	21	2,100
Total	**126**	**$ 19,688**	150	$ 16,799	99	$ 8,600

Shares repurchased during the fourth quarter of fiscal year 2020 were under the share repurchase program approved on September 18, 2019. Shares repurchased during the third quarter of fiscal year 2020 were under the share repurchase programs approved on both September 20, 2016 and September 18, 2019. All other shares repurchased were under the share repurchase program approved on September 20, 2016. The above table excludes shares repurchased to settle employee tax withholding related to the vesting of stock awards of $3.3 billion, $2.7 billion, and $2.1 billion for fiscal years 2020, 2019, and 2018, respectively. All share repurchases were made using cash resources.

Dividends

Our Board of Directors declared the following dividends:

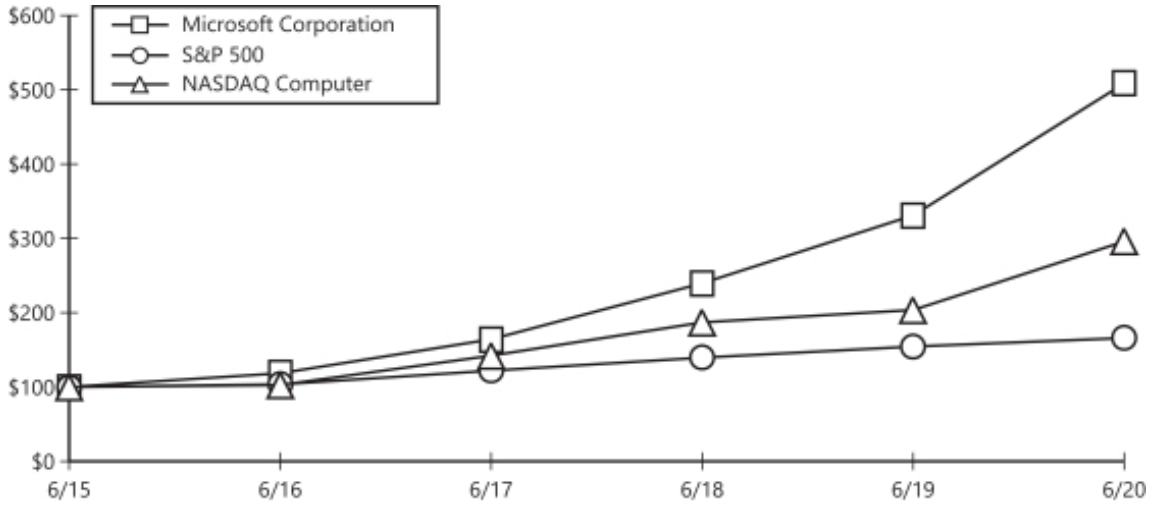
Declaration Date	Record Date	Payment Date	Dividend Per Share	Amount
Fiscal Year 2020				(In millions)
September 18, 2019	**November 21, 2019**	**December 12, 2019**	**$ 0.51**	**$ 3,886**
December 4, 2019	**February 20, 2020**	**March 12, 2020**	**0.51**	**3,876**
March 9, 2020	**May 21, 2020**	**June 11, 2020**	**0.51**	**3,865**
June 17, 2020	**August 20, 2020**	**September 10, 2020**	**0.51**	**3,861**
Total			**$ 2.04**	**$ 15,488**
Fiscal Year 2019				
September 18, 2018	November 15, 2018	December 13, 2018	$ 0.46	$ 3,544
November 28, 2018	February 21, 2019	March 14, 2019	0.46	3,526
March 11, 2019	May 16, 2019	June 13, 2019	0.46	3,521
June 12, 2019	August 15, 2019	September 12, 2019	0.46	3,510
Total			$ 1.84	$ 14,101

The dividend declared on June 17, 2020 was included in other current liabilities as of June 30, 2020.

STOCK PERFORMANCE

COMPARISON OF 5 YEAR CUMULATIVE TOTAL RETURN*

Among Microsoft Corporation, the S&P 500 Index
and the NASDAQ Computer Index



	6/15	6/16	6/17	6/18	6/19	6/20
Microsoft Corporation	**100.00**	**119.12**	**164.45**	**239.83**	**331.13**	**509.27**
S&P 500	**100.00**	**103.99**	**122.60**	**140.23**	**154.83**	**166.45**
NASDAQ Computer	**100.00**	**102.87**	**142.49**	**187.03**	**203.97**	**296.29**

* $100 invested on 6/30/15 in stock or index, including reinvestment of dividends.

Note About Forward-Looking Statements

This report includes estimates, projections, statements relating to our business plans, objectives, and expected operating results that are "forward-looking statements" within the meaning of the Private Securities Litigation Reform Act of 1995, Section 27A of the Securities Act of 1933, and Section 21E of the Securities Exchange Act of 1934. Forward-looking statements may appear throughout this report, including the following sections: "Business", and "Management's Discussion and Analysis of Financial Condition and Results of Operations". These forward-looking statements generally are identified by the words "believe," "project," "expect," "anticipate," "estimate," "intend," "strategy," "future," "opportunity," "plan," "may," "should," "will," "would," "will be," "will continue," "will likely result," and similar expressions. Forward-looking statements are based on current expectations and assumptions that are subject to risks and uncertainties that may cause actual results to differ materially. We describe risks and uncertainties that could cause actual results and events to differ materially in "Risk Factors," "Management's Discussion and Analysis of Financial Condition and Results of Operations," and "Quantitative and Qualitative Disclosures about Market Risk" in our fiscal year 2020 Form 10-K. Readers are cautioned not to place undue reliance on forward-looking statements, which speak only as of the date they are made. We undertake no obligation to update or revise publicly any forward-looking statements, whether because of new information, future events, or otherwise.

BUSINESS

GENERAL

Embracing Our Future

Microsoft is a technology company whose mission is to empower every person and every organization on the planet to achieve more. We strive to create local opportunity, growth, and impact in every country around the world. Our platforms and tools help drive small business productivity, large business competitiveness, and public-sector efficiency. They also support new startups, improve educational and health outcomes, and empower human ingenuity. As the world responds to the outbreak of a novel strain of the coronavirus ("COVID-19"), we are working to do our part by ensuring the safety of our employees, striving to protect the health and well-being of the communities in which we operate, and providing technology and resources to our customers to help them do their best work while remote.

We continue to transform our business to lead in the new era of the intelligent cloud and intelligent edge. We bring technology and products together into experiences and solutions that unlock value for our customers. Our unique role as a platform and tools provider allows us to connect the dots, bring together an ecosystem of partners, and enable organizations of all sizes to build the digital capability required to address these challenges.

In this next phase of innovation, computing is more powerful and ubiquitous from the cloud to the edge. Artificial intelligence ("AI") capabilities are rapidly advancing, fueled by data and knowledge of the world. Physical and virtual worlds are coming together with the Internet of Things ("IoT") and mixed reality to create richer experiences that understand the context surrounding people, the things they use, the places they go, and their activities and relationships. A person's experience with technology spans a multitude of devices and has become increasingly more natural and multi-sensory with voice, ink, and gaze interactions.

What We Offer

Founded in 1975, we develop and support software, services, devices, and solutions that deliver new value for customers and help people and businesses realize their full potential.

We offer an array of services, including cloud-based solutions that provide customers with software, services, platforms, and content, and we provide solution support and consulting services. We also deliver relevant online advertising to a global audience.

Our products include operating systems; cross-device productivity applications; server applications; business solution applications; desktop and server management tools; software development tools; and video games. We also design, manufacture, and sell devices, including PCs, tablets, gaming and entertainment consoles, other intelligent devices, and related accessories.

The Ambitions That Drive Us

To achieve our vision, our research and development efforts focus on three interconnected ambitions:

- Reinvent productivity and business processes.
- Build the intelligent cloud and intelligent edge platform.
- Create more personal computing.

Reinvent Productivity and Business Processes

At Microsoft, we're providing technology and resources to help our customers navigate a remote environment. We're seeing our family of products play key roles in the ways the world is continuing to work, learn, and connect.

Our growth depends on securely delivering continuous innovation and advancing our leading productivity and collaboration tools and services, including Office, Dynamics, and LinkedIn. Microsoft 365 brings together Office 365, Windows 10, and Enterprise Mobility + Security to help organizations empower their employees with AI-backed tools that unlock creativity, increase teamwork, and fuel innovation, all the while enabling compliance coverage and data protection. Microsoft Teams is enabling rapid digital transformation by giving people a single tool to chat, call, meet, and collaborate. Microsoft Relationship Sales solution brings together LinkedIn Sales Navigator and Dynamics to transform business to business sales through social selling. Dynamics 365 for Talent with LinkedIn Recruiter and Learning gives human resource professionals a complete solution to compete for talent. Microsoft Power Platform empowers employees to build custom applications, automate workflow, and analyze data no matter their technical expertise.

These scenarios represent a move to unlock creativity and discover new habits, while simplifying security and management. Organizations of all sizes have digitized business-critical functions, redefining what they can expect from their business applications. This creates an opportunity to reach new customers and increase usage and engagement with existing customers.

Build the Intelligent Cloud and Intelligent Edge Platform

In the new remote world, companies have accelerated their own digital transformation to empower their employees, optimize their operations, engage customers, and in some cases, change the very core of their products and services. Partnering with organizations on their digital transformation during this period is one of our largest opportunities and we are uniquely positioned to become the strategic digital transformation platform and partner of choice; their success is our success.

Our strategy requires continued investment in datacenters and other hybrid and edge infrastructure to support our services. Azure is a trusted cloud with comprehensive compliance coverage and AI-based security built in.

Our cloud business benefits from three economies of scale: datacenters that deploy computational resources at significantly lower cost per unit than smaller ones; datacenters that coordinate and aggregate diverse customer, geographic, and application demand patterns, improving the utilization of computing, storage, and network resources; and multi-tenancy locations that lower application maintenance labor costs.

As one of the two largest providers of cloud computing at scale, we believe we work from a position of strength. Being a global-scale cloud, Azure uniquely offers hybrid consistency, developer productivity, AI capabilities, and

trusted security and compliance. We see more emerging use cases and needs for compute and security at the edge and are accelerating our innovation across the spectrum of intelligent edge devices, from IoT sensors to gateway devices and edge hardware to build, manage, and secure edge workloads. With Azure Stack, organizations can extend Azure into their own datacenters to create a consistent stack across the public cloud and the intelligent edge. Our hybrid infrastructure consistency spans identity, data, compute, management, and security, helping to support the real-world needs and evolving regulatory requirements of commercial customers and enterprises. We are accelerating our development of mixed reality solutions with new Azure services and devices. The opportunity to merge the physical and digital worlds, when combined with the power of Azure cloud services, unlocks the potential for entirely new workloads which we believe will shape the next era of computing.

The ability to convert data into AI drives our competitive advantage. Azure SQL Database makes it possible for customers to take SQL Server from their on-premises datacenter to a fully managed instance in the cloud to utilize built-in AI. We are accelerating adoption of AI innovations from research to products. Our innovation helps every developer be an AI developer, with approachable new tools from Azure Machine Learning Studio for creating simple machine learning models, to the powerful Azure Machine Learning Workbench for the most advanced AI modeling and data science.

Create More Personal Computing

We strive to make computing more personal by putting users at the core of the experience, enabling them to interact with technology in more intuitive, engaging, and dynamic ways. In support of this, we are bringing Office, Windows, and devices together for an enhanced and more cohesive customer experience.

Windows 10 serves the enterprise as the most secure and productive operating system. It empowers people with AI-first interfaces ranging from voice-activated commands through Cortana, inking, immersive 3D content storytelling, and mixed reality experiences. Our ambition for Windows 10 monetization opportunities includes gaming, services, subscriptions, and search advertising. Windows also plays a critical role in fueling our cloud business and Microsoft 365 strategy, and it powers the growing range of devices on the “intelligent edge.”

We are committed to designing and marketing first-party devices to help drive innovation, create new device categories, and stimulate demand in the Windows ecosystem. We recently added several new products and accessories into the Surface family, including Surface Book 3 and Surface Go 2. These new Surface products join Surface Pro 7, Surface Laptop 3, and Surface Pro X.

To expand usage and deepen engagement, we continue to invest in content, community, and cloud services as we pursue the expansive opportunity in the gaming industry. We are broadening our approach to how we think about gaming end-to-end, from the way games are created and distributed to how they are played and viewed across PC, console, and mobile. We have a strong position with our large and growing highly engaged community of gamers. Xbox Game Pass, with over 10 million members from 41 countries, is a community with access to a curated library of over 100 first- and third-party console and PC titles. Project xCloud is Microsoft’s game streaming technology that is complementary to our console hardware and will give fans the ultimate choice to play the games they want, with the people they want, on the devices they want.

Our Future Opportunity

In a time of great disruption and uncertainty, customers are looking to us to accelerate their own digital transformations as software and cloud computing play a huge role across every industry and around the world. We continue to develop complete, intelligent solutions for our customers that empower people to stay productive and collaborate, while safeguarding businesses and simplifying IT management. Our goal is to lead the industry in several distinct areas of technology over the long-term, which we expect will translate to sustained growth. We are investing significant resources in:

- Transforming the workplace to deliver new modern, modular business applications to improve how people communicate, collaborate, learn, work, play, and interact with one another.

- Building and running cloud-based services in ways that unleash new experiences and opportunities for businesses and individuals.
- Applying AI to drive insights and act on our customer's behalf by understanding and interpreting their needs using natural methods of communication.
- Using Windows to fuel our cloud business and Microsoft 365 strategy, and to develop new categories of devices – both our own and third-party – on the intelligent edge.
- Inventing new gaming experiences that bring people together around their shared love for games on any devices and pushing the boundaries of innovation with console and PC gaming by creating the next wave of entertainment.

Our future growth depends on our ability to transcend current product category definitions, business models, and sales motions. We have the opportunity to redefine what customers and partners can expect and are working to deliver new solutions that reflect the best of Microsoft.

COVID-19

In March 2020, the World Health Organization declared the outbreak of COVID-19 to be a pandemic. The COVID-19 pandemic is having widespread, rapidly evolving, and unpredictable impacts on global society, economies, financial markets, and business practices. Federal and state governments have implemented measures in an effort to contain the virus, including social distancing, travel restrictions, border closures, limitations on public gatherings, work from home, supply chain logistical changes, and closure of non-essential businesses. To protect the health and well-being of our employees, suppliers, and customers, we have made substantial modifications to employee travel policies, implemented office closures as employees are advised to work from home, and cancelled or shifted our conferences and other marketing events to virtual-only through fiscal year 2021. The COVID-19 pandemic has impacted and may continue to impact our business operations, including our employees, customers, partners, and communities, and there is substantial uncertainty in the nature and degree of its continued effects over time. Refer to Management's Discussion and Analysis of Financial Condition and Results of Operations for further discussion regarding the impact of COVID-19 on our fiscal year 2020 financial results.

The extent to which the COVID-19 pandemic impacts our business going forward will depend on numerous evolving factors we cannot reliably predict, including the duration and scope of the pandemic; governmental, business, and individuals' actions in response to the pandemic; and the impact on economic activity including the possibility of recession or financial market instability. These factors may adversely impact consumer, business, and government spending on technology as well as customers' ability to pay for our products and services on an ongoing basis. This uncertainty also affects management's accounting estimates and assumptions, which could result in greater variability in a variety of areas that depend on these estimates and assumptions, including investments, receivables, and forward-looking guidance. Refer to Risk Factors in our fiscal year 2020 Form 10-K for a discussion of these factors and other risks.

Commitment to Sustainability

We work to ensure that technology is inclusive, trusted, and increases sustainability. We're empowering our customers and partners with new technology to help them drive efficiencies, transform their businesses, and create their own solutions for sustainability. In January 2020, we announced a bold new environmental sustainability strategy focused on carbon, water, waste, and ecosystems. As part of our commitment, we are investing $1 billion over the next four years in new technologies and innovative climate solutions. We set an ambitious goal to reduce and ultimately remove Microsoft's carbon footprint. By 2030 Microsoft will be carbon negative, and by 2050 Microsoft will remove from the environment all the carbon the company has emitted directly or by electrical consumption since it was founded in 1975. We also launched a new initiative to use Microsoft technology to help our suppliers and customers around the world reduce their own carbon footprint.

The investments we make in sustainability carry through to our products, services, and devices. We design our devices, from Surface to Xbox, to minimize their impact on the environment. Our cloud and AI services help

businesses cut energy consumption, reduce physical footprints, and design sustainable products. We also pledged a $50 million investment in AI for Earth to accelerate innovation by putting AI in the hands of those working to directly address sustainability challenges. Lastly, this work is supported by using our voice to support policies we think can advance sustainability efforts.

Addressing Racial Injustice

Our future opportunity depends on reaching and empowering all communities, and we are committed to taking action to help address racial injustice and inequity. With significant input from employees and leaders who are members of the Black and African American community, our senior leadership team and board of directors has developed a set of actions to help improve the lived experience at Microsoft and drive change in the communities in which we live and work. These efforts include increasing our representation and culture of inclusion by doubling the number of Black and African American people managers, senior individual contributors, and senior leaders in the United States by 2025; engaging our ecosystem by using our balance sheet and engagement with suppliers and partners to extend the vision for societal change; and strengthening our communities by using the power of data, technology, and partnership to help improve the lives of Black and African American citizens across the United States.

Investing in Digital Skills

With a continued focus on digital transformation, Microsoft is making efforts to help ensure that no one is left behind, particularly as economies start to recover from the COVID-19 pandemic. We are expanding access to the digital skills that have become increasingly vital to many of the world's jobs, and especially to individuals hardest hit by recent job losses, including those with lower incomes, women, and underrepresented minorities. Our skills initiative brings together learning resources, certification opportunities, and job-seeker tools from LinkedIn, GitHub, and Microsoft Learn, and is built on data insights drawn from LinkedIn's Economic Graph. This is combined with $20 million we are investing in key non-profit partnerships through Microsoft Philanthropies.

OPERATING SEGMENTS

We operate our business and report our financial performance using three segments: Productivity and Business Processes, Intelligent Cloud, and More Personal Computing. Our segments provide management with a comprehensive financial view of our key businesses. The segments enable the alignment of strategies and objectives across the development, sales, marketing, and services organizations, and they provide a framework for timely and rational allocation of resources within businesses.

Additional information on our operating segments and geographic and product information is contained in Note 19 – Segment Information and Geographic Data of the Notes to Financial Statements.

Our reportable segments are described below.

Productivity and Business Processes

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

- Office Commercial, including Office 365 subscriptions, the Office portion of Microsoft 365 Commercial subscriptions, and Office licensed on-premises, comprising Office, Exchange, SharePoint, Microsoft Teams, Office 365 Security and Compliance, and Skype for Business, and related Client Access Licenses ("CALs").
- Office Consumer, including Microsoft 365 Consumer (formerly Office 365 Consumer) subscriptions and Office licensed on-premises, and Office Consumer Services, including Skype, Outlook.com, and OneDrive.

- LinkedIn, including Talent Solutions, Learning Solutions, Marketing Solutions, Sales Solutions, and Premium Subscriptions.
- Dynamics business solutions, including Dynamics 365, a set of cloud-based applications across ERP and CRM, Dynamics ERP on-premises, and Dynamics CRM on-premises.

Office Commercial

Office Commercial is designed to increase personal, team, and organizational productivity through a range of products and services. Growth depends on our ability to reach new users in new markets such as first-line workers, small and medium businesses, and growth markets, as well as add value to our core product and service offerings to span productivity categories such as communication, collaboration, analytics, security, and compliance. Office Commercial revenue is mainly affected by a combination of continued installed base growth and average revenue per user expansion, as well as the continued shift from Office licensed on-premises to Office 365. CALs provide certain Office Commercial products and services with access rights to our server products and CAL revenue is reported with the associated Office products and services.

Office Consumer

Office Consumer is designed to increase personal productivity through a range of products and services. Growth depends on our ability to reach new users, add value to our core product set, and continue to expand our product and service offerings into new markets. Office Consumer revenue is mainly affected by the percentage of customers that buy Office with their new devices and the continued shift from Office licensed on-premises to Microsoft 365 Consumer subscriptions. Office Consumer Services revenue is mainly affected by the demand for communication and storage through Skype, Outlook.com, and OneDrive, which is largely driven by subscriptions, advertising, and the sale of minutes.

LinkedIn

LinkedIn connects the world's professionals to make them more productive and successful and transforms the way companies hire, market, sell, and learn. Our vision is to create economic opportunity for every member of the global workforce through the ongoing development of the world's first Economic Graph, a digital representation of the global economy. In addition to LinkedIn's free services, LinkedIn offers monetized solutions: Talent Solutions, Learning Solutions, Marketing Solutions, Sales Solutions, and Premium Subscriptions. Talent Solutions provide insights for workforce planning and tools to hire, nurture, and develop talent. Learning Solutions, including Glint, help businesses close critical skills gaps in times where companies are having to do more with existing talent. Marketing Solutions help companies grow relationships between businesses. Sales Solutions help companies strengthen customer relationships, empower teams with digital selling tools, and acquire new opportunities. Finally, Premium Subscriptions enables professionals to manage their professional identity, grow their network, and connect with talent through additional services like premium search. LinkedIn has over 700 million members and has offices around the globe. Growth will depend on our ability to increase the number of LinkedIn members and our ability to continue offering services that provide value for our members and increase their engagement. LinkedIn revenue is mainly affected by demand from enterprises and professional organizations for subscriptions to Talent Solutions, Learning Solutions, Sales Solutions, and Premium Subscriptions offerings, as well as member engagement and the quality of the sponsored content delivered to those members to drive Marketing Solutions.

Dynamics

Dynamics provides cloud-based and on-premises business solutions for financial management, enterprise resource planning ("ERP"), customer relationship management ("CRM"), supply chain management, and other application development platforms for small and medium businesses, large organizations, and divisions of global enterprises. Dynamics revenue is driven by the number of users licensed, expansion of average revenue per user, and the continued shift to Dynamics 365, a unified set of cloud-based intelligent business applications.

Competition

Competitors to Office include software and global application vendors, such as Apple, Cisco Systems, Facebook, Google, IBM, Okta, Proofpoint, Slack, Symantec, Zoom, and numerous web-based and mobile application competitors as well as local application developers. Apple distributes versions of its pre-installed application software, such as email and calendar products, through its PCs, tablets, and phones. Cisco Systems is using its position in enterprise communications equipment to grow its unified communications business. Google provides a hosted messaging and productivity suite. Slack provides teamwork and collaboration software. Zoom offers videoconferencing and cloud phone solutions. Skype for Business and Skype also compete with a variety of instant messaging, voice, and video communication providers, ranging from start-ups to established enterprises. Okta, Proofpoint, and Symantec provide security solutions across email security, information protection, identity, and governance. Web-based offerings competing with individual applications have also positioned themselves as alternatives to our products and services. We compete by providing powerful, flexible, secure, integrated industry-specific, and easy-to-use productivity and collaboration tools and services that create comprehensive solutions and work well with technologies our customers already have both on-premises or in the cloud.

LinkedIn faces competition from online professional networks, recruiting companies, talent management companies, and larger companies that are focusing on talent management and human resource services; job boards; traditional recruiting firms; and companies that provide learning and development products and services. Marketing Solutions competes with online and offline outlets that generate revenue from advertisers and marketers, and Sales Solutions competes with online and offline outlets for companies with lead generation and customer intelligence and insights.

Dynamics competes with vendors such as Oracle, Salesforce.com, and SAP to provide cloud-based and on-premises business solutions for small, medium, and large organizations.

Intelligent Cloud

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

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

Server Products and Cloud Services

Azure is a comprehensive set of cloud services that offer developers, IT professionals, and enterprises freedom to build, deploy, and manage applications on any platform or device. Customers can use Azure through our global network of datacenters for computing, networking, storage, mobile and web application services, AI, IoT, cognitive services, and machine learning. Azure enables customers to devote more resources to development and use of applications that benefit their organizations, rather than managing on-premises hardware and software. Azure revenue is mainly affected by infrastructure-as-a-service and platform-as-a-service consumption-based services, and per user-based services such as Enterprise Mobility + Security.

Our server products are designed to make IT professionals, developers, and their systems more productive and efficient. Server software is integrated server infrastructure and middleware designed to support software applications built on the Windows Server operating system. This includes the server platform, database, business intelligence, storage, management and operations, virtualization, service-oriented architecture platform, security, and identity software. We also license standalone and software development lifecycle tools for software architects, developers, testers, and project managers. GitHub provides a collaboration platform and code hosting service for developers. Server products revenue is mainly affected by purchases through volume licensing programs, licenses sold to original equipment manufacturers (“OEM”), and retail packaged products. CALs provide access rights to certain server products, including SQL Server and Windows Server, and revenue is reported along with the associated server product.

Enterprise Services

Enterprise Services, including Premier Support Services and Microsoft Consulting Services, assist customers in developing, deploying, and managing Microsoft server and desktop solutions and provide training and certification to developers and IT professionals on various Microsoft products.

Competition

Azure faces diverse competition from companies such as Amazon, Google, IBM, Oracle, VMware, and open source offerings. Our Enterprise Mobility + Security offerings also compete with products from a range of competitors including identity vendors, security solution vendors, and numerous other security point solution vendors. Azure's competitive advantage includes enabling a hybrid cloud, allowing deployment of existing datacenters with our public cloud into a single, cohesive infrastructure, and the ability to run at a scale that meets the needs of businesses of all sizes and complexities. We believe our cloud's global scale, coupled with our broad portfolio of identity and security solutions, allows us to effectively solve complex cybersecurity challenges for our customers and differentiates us from the competition.

Our server products face competition from a wide variety of server operating systems and applications offered by companies with a range of market approaches. Vertically integrated computer manufacturers such as Hewlett-Packard, IBM, and Oracle offer their own versions of the Unix operating system preinstalled on server hardware. Nearly all computer manufacturers offer server hardware for the Linux operating system and many contribute to Linux operating system development. The competitive position of Linux has also benefited from the large number of compatible applications now produced by many commercial and non-commercial software developers. A number of companies, such as Red Hat, supply versions of Linux.

We compete to provide enterprise-wide computing solutions and point solutions with numerous commercial software vendors that offer solutions and middleware technology platforms, software applications for connectivity (both Internet and intranet), security, hosting, database, and e-business servers. IBM and Oracle lead a group of companies focused on the Java Platform Enterprise Edition that competes with our enterprise-wide computing solutions. Commercial competitors for our server applications for PC-based distributed client-server environments include CA Technologies, IBM, and Oracle. Our web application platform software competes with open source software such as Apache, Linux, MySQL, and PHP. In middleware, we compete against Java vendors.

Our database, business intelligence, and data warehousing solutions offerings compete with products from IBM, Oracle, SAP, and other companies. Our system management solutions compete with server management and server virtualization platform providers, such as BMC, CA Technologies, Hewlett-Packard, IBM, and VMware. Our products for software developers compete against offerings from Adobe, IBM, Oracle, and other companies, and also against open-source projects, including Eclipse (sponsored by CA Technologies, IBM, Oracle, and SAP), PHP, and Ruby on Rails.

We believe our server products provide customers with advantages in performance, total costs of ownership, and productivity by delivering superior applications, development tools, compatibility with a broad base of hardware and software applications, security, and manageability.

Our Enterprise Services business competes with a wide range of companies that provide strategy and business planning, application development, and infrastructure services, including multinational consulting firms and small niche businesses focused on specific technologies.

More Personal Computing

Our More Personal Computing segment consists of products and services that put customers at the center of the experience with our technology. This segment primarily comprises:

- Windows, including Windows OEM licensing ("Windows OEM") and other non-volume licensing of the Windows operating system; Windows Commercial, comprising volume licensing of the Windows operating

system, Windows cloud services, and other Windows commercial offerings; patent licensing; Windows IoT; and MSN advertising.

- Devices, including Surface and PC accessories.
- Gaming, including Xbox hardware and Xbox content and services, comprising Xbox Live (transactions, subscriptions, cloud services, and advertising), video games, and third-party video game royalties.
- Search.

Windows

The Windows operating system is designed to deliver a more personal computing experience for users by enabling consistency of experience, applications, and information across their devices. Windows OEM revenue is impacted significantly by the number of Windows operating system licenses purchased by OEMs, which they pre-install on the devices they sell. In addition to computing device market volume, Windows OEM revenue is impacted by:

- The mix of computing devices based on form factor and screen size.
- Differences in device market demand between developed markets and growth markets.
- Attachment of Windows to devices shipped.
- Customer mix between consumer, small and medium businesses, and large enterprises.
- Changes in inventory levels in the OEM channel.
- Pricing changes and promotions, pricing variation that occurs when the mix of devices manufactured shifts from local and regional system builders to large multinational OEMs, and different pricing of Windows versions licensed.
- Constraints in the supply chain of device components.
- Piracy.

Windows Commercial revenue, which includes volume licensing of the Windows operating system and Windows cloud services such as Microsoft Defender Advanced Threat Protection, is affected mainly by the demand from commercial customers for volume licensing and Software Assurance (“SA”), as well as advanced security offerings. Windows Commercial revenue often reflects the number of information workers in a licensed enterprise and is relatively independent of the number of PCs sold in a given year.

Patent licensing includes our programs to license patents we own for use across a broad array of technology areas, including mobile devices and cloud offerings.

Windows IoT extends the power of Windows and the cloud to intelligent systems by delivering specialized operating systems, tools, and services for use in embedded devices.

MSN advertising includes both native and display ads.

Devices

We design, manufacture, and sell devices, including Surface and PC accessories. Our devices are designed to enable people and organizations to connect to the people and content that matter most using Windows and integrated Microsoft products and services. Surface is designed to help organizations, students, and consumers be more productive. Growth in Devices is dependent on total PC shipments, the ability to attract new customers, our product roadmap, and expanding into new categories.

Gaming

Our gaming platform is designed to provide a variety of entertainment through a unique combination of content, community, and cloud. Our exclusive game content is created through Xbox Game Studios, a collection of first-party

studios creating iconic and differentiated gaming experiences. We continue to invest in new gaming studios and content to expand our IP roadmap and leverage new content creators. These unique gaming experiences are the cornerstone of Xbox Game Pass, a subscription service and gaming community with access to a curated library of over 100 first- and third-party console and PC titles.

The gamer remains at the heart of the Xbox ecosystem. We continue to open new opportunities for gamers to engage both on- and off-console with both the launch of Project xCloud, our game streaming service, and continued investment in gaming hardware. Project xCloud utilizes Microsoft's Azure cloud technology to allow direct and on-demand streaming of games to PCs, consoles, and mobile devices, enabling gamers to take their favorites games with them and play on the device most convenient to them. Project xCloud will provide players with more choice over how and where they play.

Xbox Live enables people to connect and share online gaming experiences and is accessible on Xbox consoles, Windows-enabled devices, and other devices. Xbox Live is designed to benefit users by providing access to a network of certified applications and services and to benefit our developer and partner ecosystems by providing access to a large customer base. Xbox revenue is mainly affected by subscriptions and sales of first- and third-party content, as well as advertising. Growth of our Gaming business is determined by the overall active user base through Xbox enabled content, availability of games, providing exclusive game content that gamers seek, the computational power and reliability of the devices used to access our content and services, and the ability to create new experiences through first-party content creators.

Search

Our Search business, including Bing and Microsoft Advertising, is designed to deliver relevant online advertising to a global audience. We have several partnerships with other companies, including Verizon Media Group, through which we provide and monetize search queries. Growth depends on our ability to attract new users, understand intent, and match intent with relevant content and advertiser offerings.

Competition

Windows faces competition from various software products and from alternative platforms and devices, mainly from Apple and Google. We believe Windows competes effectively by giving customers choice, value, flexibility, security, an easy-to-use interface, and compatibility with a broad range of hardware and software applications, including those that enable productivity.

Devices face competition from various computer, tablet, and hardware manufacturers who offer a unique combination of high-quality industrial design and innovative technologies across various price points. These manufacturers, many of which are also current or potential partners and customers, include Apple and our Windows OEMs.

Xbox Live and our cloud gaming services face competition from various online gaming ecosystems and game streaming services, including those operated by Amazon, Apple, Facebook, Google, and Tencent. We also compete with other providers of entertainment services such as Netflix and Hulu. Our gaming platform competes with console platforms from Nintendo and Sony, both of which have a large, established base of customers. We believe our gaming platform is effectively positioned against, and uniquely differentiated from, competitive products and services based on significant innovation in hardware architecture, user interface, developer tools, online gaming and entertainment services, and continued strong exclusive content from our own first-party game franchises as well as other digital content offerings.

Our search business competes with Google and a wide array of websites, social platforms like Facebook, and portals that provide content and online offerings to end users.

OPERATIONS

We have operations centers that support operations in their regions, including customer contract and order processing, credit and collections, information processing, and vendor management and logistics. The regional center in Ireland supports the European, Middle Eastern, and African region; the center in Singapore supports the Japan, India, Greater China, and Asia-Pacific region; and the centers in Fargo, North Dakota, Fort Lauderdale, Florida, Puerto Rico, Redmond, Washington, and Reno, Nevada support Latin America and North America. In addition to the operations centers, we also operate datacenters throughout the Americas, Europe, Australia, and Asia, as well as in the Middle East and Africa.

To serve the needs of customers around the world and to improve the quality and usability of products in international markets, we localize many of our products to reflect local languages and conventions. Localizing a product may require modifying the user interface, altering dialog boxes, and translating text.

Our devices are primarily manufactured by third-party contract manufacturers. We generally have the ability to use other manufacturers if a current vendor becomes unavailable or unable to meet our requirements. The majority of our hardware products contain components for which there is only one qualified supplier. Extended disruptions at these suppliers could lead to a similar disruption in our ability to manufacture devices.

RESEARCH AND DEVELOPMENT

Product and Service Development, and Intellectual Property

We develop most of our products and services internally through the following engineering groups.

- *Cloud and AI*, focuses on making IT professionals, developers, and their systems more productive and efficient through development of cloud infrastructure, server, database, CRM, ERP, management and development tools, AI cognitive services, and other business process applications and services for enterprises.
- *Experiences and Devices*, focuses on instilling a unifying product ethos across our end-user experiences and devices, including Office, Windows, Enterprise Mobility + Security, and Surface.
- *AI and Research*, focuses on our AI innovations and other forward-looking research and development efforts spanning infrastructure, services, applications, and search.
- *LinkedIn*, focuses on our services that transform the way customers hire, market, sell, and learn.
- *Gaming*, focuses on developing hardware, content, and services across a large range of platforms to help grow our user base through game experiences and social interaction.

Internal development allows us to maintain competitive advantages that come from product differentiation and closer technical control over our products and services. It also gives us the freedom to decide which modifications and enhancements are most important and when they should be implemented. We strive to obtain information as early as possible about changing usage patterns and hardware advances that may affect software and hardware design. Before releasing new software platforms, and as we make significant modifications to existing platforms, we provide application vendors with a range of resources and guidelines for development, training, and testing. Generally, we also create product documentation internally.

We protect our intellectual property investments in a variety of ways. We work actively in the U.S. and internationally to ensure the enforcement of copyright, trademark, trade secret, and other protections that apply to our software and hardware products, services, business plans, and branding. We are a leader among technology companies in pursuing patents and currently have a portfolio of over 63,000 U.S. and international patents issued and over 24,500 pending worldwide. While we employ much of our internally-developed intellectual property exclusively in our products and services, we also engage in outbound licensing of specific patented technologies that are incorporated into licensees' products. From time to time, we enter into broader cross-license agreements with other technology

companies covering entire groups of patents. We also purchase or license technology that we incorporate into our products and services. At times, we make select intellectual property broadly available at no or low cost to achieve a strategic objective, such as promoting industry standards, advancing interoperability, or attracting and enabling our external development community. Our increasing engagement with open source software will also cause us to license our intellectual property rights broadly in certain situations.

While it may be necessary in the future to seek or renew licenses relating to various aspects of our products, services, and business methods, we believe, based upon past experience and industry practice, such licenses generally can be obtained on commercially reasonable terms. We believe our continuing research and product development are not materially dependent on any single license or other agreement with a third party relating to the development of our products.

Investing in the Future

Our success is based on our ability to create new and compelling products, services, and experiences for our users, to initiate and embrace disruptive technology trends, to enter new geographic and product markets, and to drive broad adoption of our products and services. We invest in a range of emerging technology trends and breakthroughs that we believe offer significant opportunities to deliver value to our customers and growth for the Company. Based on our assessment of key technology trends, we maintain our long-term commitment to research and development across a wide spectrum of technologies, tools, and platforms spanning digital work and life experiences, cloud computing, AI, devices, and operating systems.

While our main product research and development facilities are located in Redmond, Washington, we also operate research and development facilities in other parts of the U.S. and around the world, including Canada, China, Czech Republic, India, Ireland, Israel, and the United Kingdom. This global approach helps us remain competitive in local markets and enables us to continue to attract top talent from across the world.

In addition to our main research and development operations, we also operate Microsoft Research. Microsoft Research is one of the world's largest corporate research organizations and works in close collaboration with top universities around the world to advance the state-of-the-art in computer science and a broad range of other disciplines, providing us a unique perspective on future trends and contributing to our innovation.

We generally fund research at the corporate level to ensure that we are looking beyond immediate product considerations to opportunities further in the future. We also fund research and development activities at the operating segment level. Much of our segment level research and development is coordinated with other segments and leveraged across the Company. We plan to continue to make significant investments in a broad range of research and development efforts.

DISTRIBUTION, SALES, AND MARKETING

We market and distribute our products and services through the following channels: OEMs, direct, and distributors and resellers. Our sales force performs a variety of functions, including working directly with commercial enterprises and public-sector organizations worldwide to identify and meet their technology and digital transformation requirements; managing OEM relationships; and supporting system integrators, independent software vendors, and other partners who engage directly with our customers to perform sales, consulting, and fulfillment functions for our products and services.

OEMs

We distribute our products and services through OEMs that pre-install our software on new devices and servers they sell. The largest component of the OEM business is the Windows operating system pre-installed on devices. OEMs also sell devices pre-installed with other Microsoft products and services, including applications such as Office and the capability to subscribe to Office 365.

There are two broad categories of OEMs. The largest category of OEMs are direct OEMs as our relationship with them is managed through a direct agreement between Microsoft and the OEM. We have distribution agreements covering one or more of our products with virtually all the multinational OEMs, including Acer, ASUS, Dell, Fujitsu, Hewlett-Packard, Lenovo, Samsung, Sharp, Toshiba, and with many regional and local OEMs. The second broad category of OEMs are system builders consisting of lower-volume PC manufacturers, which source Microsoft software for pre-installation and local redistribution primarily through the Microsoft distributor channel rather than through a direct agreement or relationship with Microsoft.

Direct

Many organizations that license our products and services transact directly with us through Enterprise Agreements and Enterprise Services contracts, with sales support from system integrators, independent software vendors, web agencies, and partners that advise organizations on licensing our products and services ("Enterprise Agreement Software Advisors" or "ESA"). Microsoft offers direct sales programs targeted to reach small, medium, and corporate customers, in addition to those offered through the reseller channel. A large network of partner advisors support many of these sales.

We also sell commercial and consumer products and services directly to customers, such as cloud services, search, and gaming, through our digital marketplaces and online stores. In June 2020, we announced a strategic change in our retail operations, including closing our Microsoft Store physical locations.

Distributors and Resellers

Organizations also license our products and services indirectly, primarily through licensing solution partners ("LSP"), distributors, value-added resellers ("VAR"), and retailers. Although each type of reselling partner may reach organizations of all sizes, LSPs are primarily engaged with large organizations, distributors resell primarily to VARs, and VARs typically reach small and medium organizations. ESAs are also typically authorized as LSPs and operate as resellers for our other volume licensing programs. Microsoft Cloud Solution Provider is our main partner program for reselling cloud services.

We distribute our retail packaged products primarily through independent non-exclusive distributors, authorized replicators, resellers, and retail outlets. Individual consumers obtain these products primarily through retail outlets. We distribute our devices through third-party retailers. We have a network of field sales representatives and field support personnel that solicit orders from distributors and resellers, and provide product training and sales support.

Our Dynamics business solutions are also licensed to enterprises through a global network of channel partners providing vertical solutions and specialized services.

LICENSING OPTIONS

We offer options for organizations that want to purchase our cloud services, on-premises software, and Software Assurance. We license software to organizations under volume licensing agreements to allow the customer to acquire multiple licenses of products and services instead of having to acquire separate licenses through retail channels. We use different programs designed to provide flexibility for organizations of various sizes. While these programs may differ in various parts of the world, generally they include those discussed below.

SA conveys rights to new software and upgrades for perpetual licenses released over the contract period. It also provides support, tools, training, and other licensing benefits to help customers deploy and use software efficiently. SA is included with certain volume licensing agreements and is an optional purchase with others.

Volume Licensing Programs

Enterprise Agreement

Enterprise Agreements offer large organizations a manageable volume licensing program that gives them the flexibility to buy cloud services and software licenses under one agreement. Enterprise Agreements are designed for medium or large organizations that want to license cloud services and on-premises software organization-wide over a three-year period. Organizations can elect to purchase perpetual licenses or subscribe to licenses. SA is included.

Microsoft Product and Services Agreement

Microsoft Product and Services Agreements are designed for medium and large organizations that want to license cloud services and on-premises software as needed, with no organization-wide commitment, under a single, non-expiring agreement. Organizations purchase perpetual licenses or subscribe to licenses. SA is optional for customers that purchase perpetual licenses.

Open

Open agreements are a simple, cost-effective way to acquire the latest Microsoft technology. Open agreements are designed for small and medium organizations that want to license cloud services and on-premises software over a one- to three-year period. Under the Open agreements, organizations purchase perpetual licenses and SA is optional. Under Open Value agreements, organizations can elect to purchase perpetual licenses or subscribe to licenses and SA is included.

Select Plus

Select Plus agreements are designed for government and academic organizations to acquire on-premises licenses at any affiliate or department level, while realizing advantages as one organization. Organizations purchase perpetual licenses and SA is optional.

Microsoft Online Subscription Agreement

Microsoft Online Subscription Agreements are designed for small and medium organizations that want to subscribe to, activate, provision, and maintain cloud services seamlessly and directly via the web. The agreement allows customers to acquire monthly or annual subscriptions for cloud-based services.

Partner Programs

The Microsoft Cloud Solution Provider program offers customers an easy way to license the cloud services they need in combination with the value-added services offered by their systems integrator, managed services provider, or cloud reseller partner. Partners in this program can easily package their own products and services to directly provision, manage, and support their customer subscriptions.

The Microsoft Services Provider License Agreement allows hosting service providers and independent software vendors who want to license eligible Microsoft software products to provide software services and hosted applications to their end customers. Partners license software over a three-year period and are billed monthly based on consumption.

The Independent Software Vendor Royalty program enables partners to integrate Microsoft products into other applications and then license the unified business solution to their end users.

CUSTOMERS

Our customers include individual consumers, small and medium organizations, large global enterprises, public-sector institutions, Internet service providers, application developers, and OEMs. Our practice is to ship our products promptly upon receipt of purchase orders from customers; consequently, backlog is not significant.

EMPLOYEES

As of June 30, 2020, we employed approximately 163,000 people on a full-time basis, 96,000 in the U.S. and 67,000 internationally. Of the total employed people, 56,000 were in operations, including manufacturing, distribution, product support, and consulting services; 55,000 were in product research and development; 40,000 were in sales and marketing; and 12,000 were in general and administration. Certain of our employees are subject to collective bargaining agreements.

AVAILABLE INFORMATION

Our Internet address is www.microsoft.com. At our Investor Relations website, www.microsoft.com/investor, we make available free of charge a variety of information for investors. Our goal is to maintain the Investor Relations website as a portal through which investors can easily find or navigate to pertinent information about us, including:

- Our annual report on Form 10-K, quarterly reports on Form 10-Q, current reports on Form 8-K, and any amendments to those reports, as soon as reasonably practicable after we electronically file that material with or furnish it to the Securities and Exchange Commission ("SEC") at www.sec.gov.
- Information on our business strategies, financial results, and metrics for investors.
- Announcements of investor conferences, speeches, and events at which our executives talk about our product, service, and competitive strategies. Archives of these events are also available.
- Press releases on quarterly earnings, product and service announcements, legal developments, and international news.
- Corporate governance information including our articles of incorporation, bylaws, governance guidelines, committee charters, codes of conduct and ethics, global corporate social responsibility initiatives, and other governance-related policies.
- Other news and announcements that we may post from time to time that investors might find useful or interesting.
- Opportunities to sign up for email alerts to have information pushed in real time.

The information found on our website is not part of this or any other report we file with, or furnish to, the SEC. In addition to these channels, we use social media to communicate to the public. It is possible that the information we post on social media could be deemed to be material to investors. We encourage investors, the media, and others interested in Microsoft to review the information we post on the social media channels listed on our Investor Relations website.

MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

The following Management's Discussion and Analysis of Financial Condition and Results of Operations ("MD&A") is intended to help the reader understand the results of operations and financial condition of Microsoft Corporation. MD&A is provided as a supplement to, and should be read in conjunction with, our consolidated financial statements and the accompanying Notes to Financial Statements.

OVERVIEW

Microsoft is a technology company whose mission is to empower every person and every organization on the planet to achieve more. We strive to create local opportunity, growth, and impact in every country around the world. Our platforms and tools help drive small business productivity, large business competitiveness, and public-sector efficiency. They also support new startups, improve educational and health outcomes, and empower human ingenuity.

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

As the world responds to the outbreak of a novel strain of the coronavirus ("COVID-19"), we are working to do our part by ensuring the safety of our employees, striving to protect the health and well-being of the communities in which we operate, and providing technology and resources to our customers to help them do their best work while remote.

Highlights from fiscal year 2020 compared with fiscal year 2019 included:

- Commercial cloud revenue increased 36% to $51.7 billion.
- Office Commercial products and cloud services revenue increased 12%, driven by Office 365 Commercial growth of 24%.
- Office Consumer products and cloud services revenue increased 11%, with continued growth in Office 365 Consumer subscribers to 42.7 million.
- LinkedIn revenue increased 20%.
- Dynamics products and cloud services revenue increased 14%, driven by Dynamics 365 growth of 42%.
- Server products and cloud services revenue increased 27%, driven by Azure growth of 56%.
- Enterprise Services revenue increased 5%.
- Windows Commercial products and cloud services revenue increased 18%.
- Windows original equipment manufacturer licensing ("Windows OEM") revenue increased 9%.
- Surface revenue increased 8%.
- Xbox content and services revenue increased 11%.
- Search advertising revenue, excluding traffic acquisition costs, was relatively unchanged.

Industry Trends

Our industry is dynamic and highly competitive, with frequent changes in both technologies and business models. Each industry shift is an opportunity to conceive new products, new technologies, or new ideas that can further

transform the industry and our business. At Microsoft, we push the boundaries of what is possible through a broad range of research and development activities that seek to identify and address the changing demands of customers and users, industry trends, and competitive forces.

Economic Conditions, Challenges, and Risks

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

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

Our international operations provide a significant portion of our total revenue and expenses. Many of these revenue and expenses are denominated in currencies other than the U.S. dollar. As a result, changes in foreign exchange rates may significantly affect revenue and expenses. Strengthening of the U.S. dollar relative to certain foreign currencies did not significantly impact reported revenue or expenses from our international operations in the first and second quarters of fiscal year 2019, and reduced reported revenue and expenses from our international operations in the third and fourth quarters of fiscal year 2019. Strengthening of the U.S. dollar relative to certain foreign currencies reduced reported revenue and expenses from our international operations in fiscal year 2020.

Refer to Risk Factors in our fiscal year 2020 Form 10-K for a discussion of these factors and other risks.

COVID-19

In fiscal year 2020, the COVID-19 pandemic impacted our business operations, including our employees, customers, partners, and communities, and we saw the following trends in our financial operating results. In the Productivity and Business Processes and Intelligent Cloud segments, cloud usage and demand increased as customers shifted to work and learn from home. We also experienced a slowdown in transactional licensing, particularly in small and medium businesses, and LinkedIn was negatively impacted by the weak job market and reductions in advertising spend. In the More Personal Computing segment, Windows OEM, Surface, and Gaming benefited from increased demand to support remote work-, play-, and learn-from-home scenarios, while Search was negatively impacted by reductions in advertising spend. The COVID-19 pandemic may continue to impact our business operations and financial operating results, and there is substantial uncertainty in the nature and degree of its continued effects over time.

The extent to which the COVID-19 pandemic impacts our business going forward will depend on numerous evolving factors we cannot reliably predict, including the duration and scope of the pandemic; governmental, business, and individuals' actions in response to the pandemic; and the impact on economic activity including the possibility of recession or financial market instability. These factors may adversely impact consumer, business, and government spending on technology as well as customers' ability to pay for our products and services on an ongoing basis. This uncertainty also affects management's accounting estimates and assumptions, which could result in greater variability in a variety of areas that depend on these estimates and assumptions, including investments, receivables, and forward-looking guidance. Refer to Risk Factors in our fiscal year 2020 Form 10-K for a discussion of these factors and other risks.

Seasonality

Our revenue fluctuates quarterly and is generally higher in the second and fourth quarters of our fiscal year. Second quarter revenue is driven by corporate year-end spending trends in our major markets and holiday season spending

by consumers, and fourth quarter revenue is driven by the volume of multi-year on-premises contracts executed during the period.

Reportable Segments

We report our financial performance based on the following segments: Productivity and Business Processes, Intelligent Cloud, and More Personal Computing. The segment amounts included in MD&A are presented on a basis consistent with our internal management reporting. All differences between our internal management reporting basis and accounting principles generally accepted in the United States of America ("GAAP"), along with certain corporate-level and other activity, are included in Corporate and Other.

Additional information on our reportable segments is contained in Note 19 – Segment Information and Geographic Data of the Notes to Financial Statements.

Metrics

We use metrics in assessing the performance of our business and to make informed decisions regarding the allocation of resources. We disclose metrics to enable investors to evaluate progress against our ambitions, provide transparency into performance trends, and reflect the continued evolution of our products and services. Our commercial and other business metrics are fundamentally connected based on how customers use our products and services. The metrics are disclosed in the MD&A or the Notes to Financial Statements. Financial metrics are calculated based on GAAP results and growth comparisons relate to the corresponding period of last fiscal year.

Commercial

Our commercial business primarily consists of Server products and cloud services, Office Commercial, Windows Commercial, the commercial portion of LinkedIn, Enterprise Services, and Dynamics. Our commercial metrics allow management and investors to assess the overall health of our commercial business and include leading indicators of future performance.

Commercial remaining performance obligation	Commercial portion of revenue allocated to remaining performance obligations, which includes unearned revenue and amounts that will be invoiced and recognized as revenue in future periods
Commercial cloud revenue	Revenue from our commercial cloud business, which includes Office 365 Commercial, Azure, the commercial portion of LinkedIn, Dynamics 365, and other commercial cloud properties
Commercial cloud gross margin percentage	Gross margin percentage for our commercial cloud business

Productivity and Business Processes and Intelligent Cloud

Metrics related to our Productivity and Business Processes and Intelligent Cloud segments assess the health of our core businesses within these segments. The metrics reflect our cloud and on-premises product strategies and trends.

Office Commercial products and cloud services revenue growth	Revenue from Office Commercial products and cloud services, including Office 365 subscriptions, the Office 365 portion of Microsoft 365 Commercial subscriptions, and Office licensed on-premises, comprising Office, Exchange, SharePoint, Microsoft Teams, Office 365 Security and Compliance, and Skype for Business, and related Client Access Licenses ("CALs")
Office Consumer products and cloud services revenue growth	Revenue from Office Consumer products and cloud services, including Microsoft 365 Consumer (formerly Office 365 Consumer) subscriptions and Office licensed on-premises

Office 365 Commercial seat growth	The number of Office 365 Commercial seats at end of period where seats are paid users covered by an Office 365 Commercial subscription
Office 365 Consumer subscribers	The number of Office 365 Consumer subscribers at end of period
Dynamics products and cloud services revenue growth	Revenue from Dynamics products and cloud services, including Dynamics 365, a set of cloud-based applications across ERP and CRM, Dynamics ERP on-premises, and Dynamics CRM on-premises
LinkedIn revenue growth	Revenue from LinkedIn, including Talent Solutions, Learning Solutions, Marketing Solutions, Sales Solutions, and Premium Subscriptions
Server products and cloud services revenue growth	Revenue from Server products and cloud services, including Azure; SQL Server, Windows Server, Visual Studio, System Center, and related CALs; and GitHub
Enterprise Services revenue growth	Revenue from Enterprise Services, including Premier Support Services and Microsoft Consulting Services

More Personal Computing

Metrics related to our More Personal Computing segment assess the performance of key lines of business within this segment. These metrics provide strategic product insights which allow us to assess the performance across our commercial and consumer businesses. As we have diversity of target audiences and sales motions within the Windows business, we monitor metrics that are reflective of those varying motions.

Windows OEM Pro revenue growth	Revenue from sales of Windows Pro licenses sold through the OEM channel, which primarily addresses demand in the commercial market
Windows OEM non-Pro revenue growth	Revenue from sales of Windows non-Pro licenses sold through the OEM channel, which primarily addresses demand in the consumer market
Windows Commercial products and cloud services revenue growth	Revenue from Windows Commercial products and cloud services, comprising volume licensing of the Windows operating system, Windows cloud services, and other Windows commercial offerings
Surface revenue	Revenue from Surface devices and accessories
Xbox content and services revenue growth	Revenue from Xbox content and services, comprising Xbox Live (transactions, subscriptions, cloud services, and advertising), video games, and third-party video game royalties
Search advertising revenue, excluding TAC, growth	Revenue from search advertising excluding traffic acquisition costs ("TAC") paid to Bing Ads network publishers

SUMMARY RESULTS OF OPERATIONS

(In millions, except percentages and per share amounts)	2020	2019	2018	Percentage Change 2020 Versus 2019	Percentage Change 2019 Versus 2018
Revenue	**$ 143,015**	$ 125,843	$ 110,360	14%	14%
Gross margin	**96,937**	82,933	72,007	17%	15%
Operating income	**52,959**	42,959	35,058	23%	23%
Net income	**44,281**	39,240	16,571	13%	137%
Diluted earnings per share	**5.76**	5.06	2.13	14%	138%
Non-GAAP net income	**44,281**	36,830	30,267	20%	22%
Non-GAAP diluted earnings per share	**5.76**	4.75	3.88	21%	22%

Non-GAAP net income and diluted earnings per share ("EPS") exclude the net tax impact of transfer of intangible properties in fiscal year 2019 and the net tax impact of the Tax Cuts and Jobs Act ("TCJA") in fiscal years 2019 and 2018. Refer to the Non-GAAP Financial Measures section below for a reconciliation of our financial results reported in accordance with GAAP to non-GAAP financial results.

Fiscal Year 2020 Compared with Fiscal Year 2019

Revenue increased $17.2 billion or 14%, driven by growth across each of our segments. Intelligent Cloud revenue increased, driven by server products and cloud services. Productivity and Business Processes revenue increased, driven by Office Commercial and LinkedIn. More Personal Computing revenue increased, driven by Windows and Surface.

Gross margin increased $14.0 billion or 17%, driven by growth across each of our segments. Gross margin percentage increased, driven by sales mix shift to higher margin businesses. Commercial cloud gross margin percentage increased 4 points to 67%, primarily driven by improvement in Azure.

Operating income increased $10.0 billion or 23%, driven by growth across each of our segments.

Key changes in expenses were:

- Cost of revenue increased $3.2 billion or 7%, driven by growth in commercial cloud.
- Research and development expenses increased $2.4 billion or 14%, driven by investments in cloud engineering, LinkedIn, Devices, and Gaming.
- Sales and marketing expenses increased $1.4 billion or 8%, driven by investments in LinkedIn and commercial sales, and an increase in bad debt expense.
- General and administrative expenses increased $226 million or 5%, driven by charges associated with the closing of our Microsoft Store physical locations, offset in part by a reduction in business taxes and legal expenses.

Gross margin and operating income included an unfavorable foreign currency impact of 2% and 4%, respectively.

Prior year net income included a $2.6 billion net income tax benefit related to intangible property transfers and a $157 million net charge related to the enactment of the TCJA, which together resulted in an increase to net income and diluted EPS of $2.4 billion and $0.31, respectively.

Fiscal Year 2019 Compared with Fiscal Year 2018

Revenue increased $15.5 billion or 14%, driven by growth across each of our segments. Intelligent Cloud revenue increased, driven by server products and cloud services. Productivity and Business Processes revenue increased, driven by Office and LinkedIn. More Personal Computing revenue increased, driven by Surface, Gaming, and Windows.

Gross margin increased $10.9 billion or 15%, driven by growth across each of our segments. Gross margin percentage increased slightly, due to gross margin percentage improvement across each of our segments and favorable segment sales mix. Gross margin included a 5 percentage point improvement in commercial cloud, primarily from Azure.

Operating income increased $7.9 billion or 23%, driven by growth across each of our segments.

Key changes in expenses were:

- Cost of revenue increased $4.6 billion or 12%, driven by growth in commercial cloud, Surface, and Gaming.
- Research and development expenses increased $2.2 billion or 15%, driven by investments in cloud and artificial intelligence ("AI") engineering, Gaming, LinkedIn, and GitHub.

- Sales and marketing expenses increased $744 million or 4%, driven by investments in commercial sales capacity, LinkedIn, and GitHub, offset in part by a decrease in marketing. Sales and marketing expenses included a favorable foreign currency impact of 2%.

Fiscal year 2019 net income included a $2.6 billion net income tax benefit related to intangible property transfers and a $157 million net charge related to the enactment of the TCJA, which together resulted in an increase to net income and diluted EPS of $2.4 billion and $0.31, respectively. Fiscal year 2018 net income and diluted EPS were negatively impacted by the net charge related to the enactment of the TCJA, which resulted in a decrease to net income and diluted EPS of $13.7 billion and $1.75, respectively.

SEGMENT RESULTS OF OPERATIONS

(In millions, except percentages)	2020	2019	2018	Percentage Change 2020 Versus 2019	Percentage Change 2019 Versus 2018
Revenue					
Productivity and Business Processes	**$ 46,398**	$ 41,160	$ 35,865	13%	15%
Intelligent Cloud	**48,366**	38,985	32,219	24%	21%
More Personal Computing	**48,251**	45,698	42,276	6%	8%
Total	**$ 143,015**	$ 125,843	$ 110,360	14%	14%
Operating Income					
Productivity and Business Processes	**$ 18,724**	$ 16,219	$ 12,924	15%	25%
Intelligent Cloud	**18,324**	13,920	11,524	32%	21%
More Personal Computing	**15,911**	12,820	10,610	24%	21%
Total	**$ 52,959**	$ 42,959	$ 35,058	23%	23%

Reportable Segments

Fiscal Year 2020 Compared with Fiscal Year 2019

Productivity and Business Processes

Revenue increased $5.2 billion or 13%.

- Office Commercial products and cloud services revenue increased $3.1 billion or 12%, driven by Office 365 Commercial, offset in part by lower revenue from products licensed on-premises, reflecting a continued shift to cloud offerings. Office 365 Commercial revenue grew 24%, due to seat growth and higher revenue per user.
- Office Consumer products and cloud services revenue increased $458 million or 11%, driven by Microsoft 365 Consumer subscription revenue and transactional strength in Japan. Office 365 Consumer subscribers increased 23% to 42.7 million with increased demand from remote work and learn scenarios.
- LinkedIn revenue increased $1.3 billion or 20%, driven by growth across all businesses.
- Dynamics products and cloud services revenue increased 14%, driven by Dynamics 365 growth of 42%.

Operating income increased $2.5 billion or 15%.

- Gross margin increased $4.1 billion or 13%, driven by growth in Office Commercial and LinkedIn. Gross margin percentage was relatively unchanged, due to gross margin percentage improvement in LinkedIn, offset in part by an increased mix of cloud offerings.
- Operating expenses increased $1.6 billion or 11%, driven by investments in LinkedIn and cloud engineering.

Revenue, gross margin, and operating income included an unfavorable foreign currency impact of 2%, 2%, and 4%, respectively.

Intelligent Cloud

Revenue increased $9.4 billion or 24%.

- Server products and cloud services revenue increased $8.8 billion or 27%, driven by Azure. Azure revenue grew 56%, due to growth in our consumption-based services. Server products revenue increased 8%, due to hybrid and premium solutions, as well as demand related to SQL Server 2008 and Windows Server 2008 end of support.
- Enterprise Services revenue increased $285 million or 5%, driven by growth in Premier Support Services.

Operating income increased $4.4 billion or 32%.

- Gross margin increased $6.9 billion or 26%, driven by growth in server products and cloud services revenue and cloud services scale and efficiencies. Gross margin percentage increased slightly, due to gross margin percentage improvement in Azure, offset in part by an increased mix of cloud offerings.
- Operating expenses increased $2.5 billion or 19%, driven by investments in Azure.

Revenue, gross margin, and operating income included an unfavorable foreign currency impact of 2%, 2%, and 4%, respectively.

More Personal Computing

Revenue increased $2.6 billion or 6%.

- Windows revenue increased $1.9 billion or 9%, driven by growth in Windows Commercial and Windows OEM. Windows Commercial products and cloud services revenue increased 18%, driven by increased demand for Microsoft 365. Windows OEM revenue increased 9%, ahead of PC market growth. Windows OEM Pro revenue grew 11%, driven by Windows 7 end of support and healthy Windows 10 demand, offset in part by weakness in small and medium businesses. Windows OEM non-Pro revenue grew 5%, driven by consumer demand from remote work and learn scenarios.
- Surface revenue increased $457 million or 8%, driven by increased demand from remote work and learn scenarios.
- Gaming revenue increased $189 million or 2%, driven by an increase in Xbox content and services, offset in part by a decrease in Xbox hardware. Xbox content and services revenue increased $943 million or 11% on a strong prior year comparable, driven by growth in Minecraft, third-party titles, and subscriptions, accelerated by higher engagement during stay-at-home guidelines. Xbox hardware revenue declined 31%, primarily due to a decrease in volume and price of consoles sold.
- Search advertising revenue increased $112 million or 1%. Search advertising revenue, excluding traffic acquisition costs, was relatively unchanged.

Operating income increased $3.1 billion or 24%.

- Gross margin increased $3.0 billion or 12%, driven by growth in Windows, Gaming, and Surface. Gross margin percentage increased, due to sales mix shift to higher margin businesses and gross margin percentage improvement in Gaming.
- Operating expenses decreased $119 million or 1%, driven by the redeployment of engineering resources, offset in part by charges associated with the closing of our Microsoft Store physical locations and investments in Gaming.

Gross margin and operating income included an unfavorable foreign currency impact of 2% and 3%, respectively.

Fiscal Year 2019 Compared with Fiscal Year 2018

Productivity and Business Processes

Revenue increased $5.3 billion or 15%.

- Office Commercial products and cloud services revenue increased $3.2 billion or 13%, driven by Office 365 Commercial, offset in part by lower revenue from products licensed on-premises, reflecting a continued shift to cloud offerings. Office 365 Commercial grew 33%, due to growth in seats and higher average revenue per user.
- Office Consumer products and cloud services revenue increased $286 million or 7%, driven by Microsoft 365 Consumer, due to recurring subscription revenue and transactional strength in Japan.
- LinkedIn revenue increased $1.5 billion or 28%, driven by growth across each line of business.
- Dynamics products and cloud services revenue increased 15%, driven by Dynamics 365 growth.

Operating income increased $3.3 billion or 25%, including an unfavorable foreign currency impact of 2%.

- Gross margin increased $4.1 billion or 15%, driven by growth in Office Commercial and LinkedIn. Gross margin percentage increased slightly, due to gross margin percentage improvement in LinkedIn and Office 365 Commercial, offset in part by an increased mix of cloud offerings.
- Operating expenses increased $806 million or 6%, driven by investments in LinkedIn and cloud engineering, offset in part by a decrease in marketing.

Intelligent Cloud

Revenue increased $6.8 billion or 21%.

- Server products and cloud services revenue, including GitHub, increased $6.5 billion or 25%, driven by Azure. Azure revenue growth was 72%, due to higher infrastructure-as-a-service and platform-as-a-service consumption-based and per user-based services. Server products revenue increased 6%, due to continued demand for premium versions and hybrid solutions, GitHub, and demand ahead of end-of-support for SQL Server 2008 and Windows Server 2008.
- Enterprise Services revenue increased $278 million or 5%, driven by growth in Premier Support Services and Microsoft Consulting Services.

Operating income increased $2.4 billion or 21%.

- Gross margin increased $4.8 billion or 22%, driven by growth in server products and cloud services revenue and cloud services scale and efficiencies. Gross margin percentage increased slightly, due to gross margin percentage improvement in Azure, offset in part by an increased mix of cloud offerings.
- Operating expenses increased $2.4 billion or 22%, driven by investments in cloud and AI engineering, GitHub, and commercial sales capacity.

More Personal Computing

Revenue increased $3.4 billion or 8%.

- Windows revenue increased $877 million or 4%, driven by growth in Windows Commercial and Windows OEM, offset in part by a decline in patent licensing. Windows Commercial products and cloud services revenue increased 14%, driven by an increased mix of multi-year agreements that carry higher in-quarter revenue recognition. Windows OEM revenue increased 4%. Windows OEM Pro revenue grew 10%, ahead of the commercial PC market, driven by healthy Windows 10 demand. Windows OEM non-Pro revenue declined 7%, below the consumer PC market, driven by continued pressure in the entry level category.
- Surface revenue increased $1.1 billion or 23%, with strong growth across commercial and consumer.

- Gaming revenue increased $1.0 billion or 10%, driven by Xbox software and services growth of 19%, primarily due to third-party title strength and subscriptions growth, offset in part by a decline in Xbox hardware of 13% primarily due to a decrease in volume of consoles sold.
- Search advertising revenue increased $616 million or 9%. Search advertising revenue, excluding traffic acquisition costs, increased 13%, driven by higher revenue per search.

Operating income increased $2.2 billion or 21%, including an unfavorable foreign currency impact of 2%.

- Gross margin increased $2.0 billion or 9%, driven by growth in Windows, Gaming, and Search. Gross margin percentage increased slightly, due to sales mix shift to higher gross margin businesses in Windows and Gaming.
- Operating expenses decreased $172 million or 1%.

OPERATING EXPENSES

Research and Development

(In millions, except percentages)	2020	2019	2018	Percentage Change 2020 Versus 2019	Percentage Change 2019 Versus 2018
Research and development	**$ 19,269**	$ 16,876	$ 14,726	14%	15%
As a percent of revenue	**13%**	13%	13%	0ppt	0ppt

Research and development expenses include payroll, employee benefits, stock-based compensation expense, and other headcount-related expenses associated with product development. Research and development expenses also include third-party development and programming costs, localization costs incurred to translate software for international markets, and the amortization of purchased software code and services content.

Fiscal Year 2020 Compared with Fiscal Year 2019

Research and development expenses increased $2.4 billion or 14%, driven by investments in cloud engineering, LinkedIn, Devices, and Gaming.

Fiscal Year 2019 Compared with Fiscal Year 2018

Research and development expenses increased $2.2 billion or 15%, driven by investments in cloud and AI engineering, Gaming, LinkedIn, and GitHub.

Sales and Marketing

(In millions, except percentages)	2020	2019	2018	Percentage Change 2020 Versus 2019	Percentage Change 2019 Versus 2018
Sales and marketing	**$ 19,598**	$ 18,213	$ 17,469	8%	4%
As a percent of revenue	**14%**	14%	16%	0ppt	(2)ppt

Sales and marketing expenses include payroll, employee benefits, stock-based compensation expense, and other headcount-related expenses associated with sales and marketing personnel, and the costs of advertising, promotions, trade shows, seminars, and other programs.

Fiscal Year 2020 Compared with Fiscal Year 2019

Sales and marketing expenses increased $1.4 billion or 8%, driven by investments in LinkedIn and commercial sales, and an increase in bad debt expense.

Fiscal Year 2019 Compared with Fiscal Year 2018

Sales and marketing expenses increased $744 million or 4%, driven by investments in commercial sales capacity, LinkedIn, and GitHub, offset in part by a decrease in marketing. Expenses included a favorable foreign currency impact of 2%.

General and Administrative

(In millions, except percentages)	2020	2019	2018	Percentage Change 2020 Versus 2019	Percentage Change 2019 Versus 2018
General and administrative	**$ 5,111**	$ 4,885	$ 4,754	5%	3%
As a percent of revenue	**4%**	4%	4%	0ppt	0ppt

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

Fiscal Year 2020 Compared with Fiscal Year 2019

General and administrative expenses increased $226 million or 5%, driven by charges associated with the closing of our Microsoft Store physical locations, offset in part by a reduction in business taxes and legal expenses.

Fiscal Year 2019 Compared with Fiscal Year 2018

General and administrative expenses increased $131 million or 3%.

OTHER INCOME (EXPENSE), NET

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

(In millions) Year Ended June 30,	2020	2019	2018
Interest and dividends income	**$ 2,680**	$ 2,762	$ 2,214
Interest expense	**(2,591)**	(2,686)	(2,733)
Net recognized gains on investments	**32**	648	2,399
Net gains (losses) on derivatives	**187**	144	(187)
Net losses on foreign currency remeasurements	**(191)**	(82)	(218)
Other, net	**(40)**	(57)	(59)
Total	**$ 77**	$ 729	$ 1,416

We use derivative instruments to: manage risks related to foreign currencies, equity prices, interest rates, and credit; enhance investment returns; and facilitate portfolio diversification. Gains and losses from changes in fair values of derivatives that are not designated as hedging instruments are primarily recognized in other income (expense), net.

Fiscal Year 2020 Compared with Fiscal Year 2019

Interest and dividends income decreased due to lower yields, offset in part by higher average portfolio balances on fixed-income securities. Interest expense decreased due to capitalization of interest expense and a decrease in outstanding long-term debt due to debt maturities, offset in part by debt exchange transaction fees and higher finance lease expense. Net recognized gains on investments decreased due to lower gains and higher other-than-

temporary impairments on equity investments, offset in part by gains on fixed income securities in the current period compared to losses in the prior period. Net gains on derivatives increased due to higher gains on foreign exchange and equity derivatives.

Fiscal Year 2019 Compared with Fiscal Year 2018

Interest and dividends income increased primarily due to higher yields on fixed-income securities. Interest expense decreased primarily driven by a decrease in outstanding long-term debt due to debt maturities, offset in part by higher finance lease expense. Net recognized gains on investments decreased primarily due to lower gains on sales of equity investments. Net gains on derivatives includes gains on foreign exchange and interest rate derivatives in the current period as compared to losses in the prior period.

INCOME TAXES

Effective Tax Rate

Fiscal Year 2020 Compared with Fiscal Year 2019

Our effective tax rate for fiscal years 2020 and 2019 was 17% and 10%, respectively. The increase in our effective tax rate for fiscal year 2020 compared to fiscal year 2019 was primarily due to a $2.6 billion net income tax benefit in the fourth quarter of fiscal year 2019 related to intangible property transfers. Our effective tax rate was lower than the U.S. federal statutory rate, primarily due to earnings taxed at lower rates in foreign jurisdictions resulting from producing and distributing our products and services through our foreign regional operations centers in Ireland and Puerto Rico, and tax benefits relating to stock-based compensation.

The mix of income before income taxes between the U.S. and foreign countries impacted our effective tax rate as a result of the geographic distribution of, and customer demand for, our products and services. In fiscal year 2020, our U.S. income before income taxes was $24.1 billion and our foreign income before income taxes was $28.9 billion. In fiscal year 2019, our U.S. income before income taxes was $15.8 billion and our foreign income before income taxes was $27.9 billion.

Fiscal Year 2019 Compared with Fiscal Year 2018

Our effective tax rate for fiscal years 2019 and 2018 was 10% and 55%, respectively. The decrease in our effective tax rate for fiscal year 2019 compared to fiscal year 2018 was primarily due to the net charge related to the enactment of the TCJA in the second quarter of fiscal year 2018 and a $2.6 billion net income tax benefit in the fourth quarter of fiscal year 2019 related to intangible property transfers. Our effective tax rate was lower than the U.S. federal statutory rate, primarily due to the tax benefit related to intangible property transfers, and earnings taxed at lower rates in foreign jurisdictions resulting from producing and distributing our products and services through our foreign regional operations centers in Ireland, Singapore, and Puerto Rico.

The mix of income before income taxes between the U.S. and foreign countries impacted our effective tax rate as a result of the geographic distribution of, and customer demand for, our products and services. In fiscal year 2019, our U.S. income before income taxes was $15.8 billion and our foreign income before income taxes was $27.9 billion. In fiscal year 2018, our U.S. income before income taxes was $11.5 billion and our foreign income before income taxes was $24.9 billion.

Tax Cuts and Jobs Act

On December 22, 2017, the TCJA was enacted into law, which significantly changed existing U.S. tax law and included numerous provisions that affect our business. We recorded a provisional net charge of $13.7 billion related to the enactment of the TCJA in fiscal year 2018, and adjusted the provisional net charge by recording additional tax expense of $157 million in fiscal year 2019 pursuant to Securities and Exchange Commission Staff Accounting Bulletin No. 118.

In fiscal year 2019, in response to the TCJA and recently issued regulations, we transferred certain intangible properties held by our foreign subsidiaries to the U.S. and Ireland. The transfers of intangible properties resulted in a $2.6 billion net income tax benefit recorded in the fourth quarter of fiscal year 2019, as the value of future tax deductions exceeded the current tax liability from foreign jurisdictions and U.S. global intangible low-taxed income tax.

Refer to Note 12 – Income Taxes of the Notes to Financial Statements for further discussion.

Uncertain Tax Positions

We settled a portion of the Internal Revenue Service ("IRS") audit for tax years 2004 to 2006 in fiscal year 2011. In February 2012, the IRS withdrew its 2011 Revenue Agents Report related to unresolved issues for tax years 2004 to 2006 and reopened the audit phase of the examination. We also settled a portion of the IRS audit for tax years 2007 to 2009 in fiscal year 2016, and a portion of the IRS audit for tax years 2010 to 2013 in fiscal year 2018. We remain under audit for tax years 2004 to 2013. In April 2020, the IRS commenced the audit for tax years 2014 to 2017.

As of June 30, 2020, the primary unresolved issues for the IRS audits relate to transfer pricing, which could have a material impact in our consolidated financial statements when the matters are resolved. We believe our allowances for income tax contingencies are adequate. We have not received a proposed assessment for the unresolved issues and do not expect a final resolution of these issues in the next 12 months. Based on the information currently available, we do not anticipate a significant increase or decrease to our tax contingencies for these issues within the next 12 months.

We are subject to income tax in many jurisdictions outside the U.S. Our operations in certain jurisdictions remain subject to examination for tax years 1996 to 2019, some of which are currently under audit by local tax authorities. The resolution of each of these audits is not expected to be material to our consolidated financial statements.

NON-GAAP FINANCIAL MEASURES

Non-GAAP net income and diluted EPS are non-GAAP financial measures which exclude the net tax impact of transfer of intangible properties in fiscal year 2019 and the net tax impact of the TCJA in fiscal years 2019 and 2018. We believe these non-GAAP measures aid investors by providing additional insight into our operational performance and help clarify trends affecting our business. For comparability of reporting, management considers non-GAAP measures in conjunction with GAAP financial results in evaluating business performance. These non-GAAP financial measures presented should not be considered a substitute for, or superior to, the measures of financial performance prepared in accordance with GAAP.

The following table reconciles our financial results reported in accordance with GAAP to non-GAAP financial results:

(In millions, except percentages and per share amounts)	2020	2019	2018	Percentage Change 2020 Versus 2019	Percentage Change 2019 Versus 2018
Net income	**$ 44,281**	$ 39,240	$ 16,571	13%	137%
Net tax impact of transfer of intangible properties	**0**	(2,567)	0	*	*
Net tax impact of the TCJA	**0**	157	13,696	*	*
Non-GAAP net income	**$ 44,281**	$ 36,830	$ 30,267	20%	22%
Diluted earnings per share	**$ 5.76**	$ 5.06	$ 2.13	14%	138%
Net tax impact of transfer of intangible properties	**0**	(0.33)	0	*	*
Net tax impact of the TCJA	**0**	0.02	1.75	*	*
Non-GAAP diluted earnings per share	**$ 5.76**	$ 4.75	$ 3.88	21%	22%

* *Not meaningful.*

FINANCIAL CONDITION

Cash, Cash Equivalents, and Investments

Cash, cash equivalents, and short-term investments totaled $136.5 billion and $133.8 billion as of June 30, 2020 and 2019. Equity investments were $3.0 billion and $2.6 billion as of June 30, 2020 and 2019, respectively. Our short-term investments are primarily intended to facilitate liquidity and capital preservation. They consist predominantly of highly liquid investment-grade fixed-income securities, diversified among industries and individual issuers. The investments are predominantly U.S. dollar-denominated securities, but also include foreign currency-denominated securities to diversify risk. Our fixed-income investments are exposed to interest rate risk and credit risk. The credit risk and average maturity of our fixed-income portfolio are managed to achieve economic returns that correlate to certain fixed-income indices. The settlement risk related to these investments is insignificant given that the short-term investments held are primarily highly liquid investment-grade fixed-income securities.

Valuation

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

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

Cash Flows

Fiscal Year 2020 Compared with Fiscal Year 2019

Cash from operations increased $8.5 billion to $60.7 billion for fiscal year 2020, mainly due to an increase in cash from customers, offset in part by an increase in cash used to pay income taxes, suppliers, and employees. Cash used in financing increased $9.1 billion to $46.0 billion for fiscal year 2020, mainly due to a $3.4 billion cash premium on our debt exchange, a $3.4 billion increase in common stock repurchases, a $1.5 billion increase in repayments of debt, and a $1.3 billion increase in dividends paid. Cash used in investing decreased $3.6 billion to $12.2 billion for fiscal year 2020, mainly due to a $6.4 billion increase in cash from net investment purchases, sales, and maturities, offset in part by a $1.5 billion increase in additions to property and equipment and $1.2 billion in other investing to facilitate the purchase of components.

Fiscal Year 2019 Compared with Fiscal Year 2018

Cash from operations increased $8.3 billion to $52.2 billion for fiscal year 2019, mainly due to an increase in cash received from customers, offset in part by an increase in cash paid to suppliers and employees and an increase in

cash paid for income taxes. Cash used in financing increased $3.3 billion to $36.9 billion for fiscal year 2019, mainly due to an $8.8 billion increase in common stock repurchases and a $1.1 billion increase in dividends paid, offset in part by a $6.2 billion decrease in repayments of debt, net of proceeds from issuance of debt. Cash used in investing increased $9.7 billion to $15.8 billion for fiscal year 2019, mainly due to a $6.0 billion decrease in cash from net investment purchases, sales, and maturities, a $2.3 billion increase in additions to property and equipment, and a $1.5 billion increase in cash used for acquisitions of companies, net of cash acquired, and purchases of intangible and other assets.

Debt

We issue debt to take advantage of favorable pricing and liquidity in the debt markets, reflecting our credit rating and the low interest rate environment. The proceeds of these issuances were or will be used for general corporate purposes, which may include, among other things, funding for working capital, capital expenditures, repurchases of capital stock, acquisitions, and repayment of existing debt. In June 2020, we exchanged a portion of our existing debt at premium for cash and new debt with longer maturities to take advantage of favorable financing rates in the debt markets, reflecting our credit rating and the low interest rate environment. Refer to Note 11 – Debt of the Notes to Financial Statements for further discussion.

Unearned Revenue

Unearned revenue comprises mainly unearned revenue related to volume licensing programs, which may include Software Assurance ("SA") and cloud services. Unearned revenue is generally invoiced annually at the beginning of each contract period for multi-year agreements and recognized ratably over the coverage period. Unearned revenue also includes payments for other offerings for which we have been paid in advance and earn the revenue when we transfer control of the product or service. Refer to Note 1 – Accounting Policies of the Notes to Financial Statements for further discussion.

The following table outlines the expected future recognition of unearned revenue as of June 30, 2020:

(In millions)	
Three Months Ending	
September 30, 2020	**$ 13,884**
December 31, 2020	**10,950**
March 31, 2021	**7,476**
June 30, 2021	**3,690**
Thereafter	**3,180**
Total	**$ 39,180**

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

Share Repurchases

For fiscal years 2020, 2019, and 2018, we repurchased 126 million shares, 150 million shares, and 99 million shares of our common stock for $19.7 billion, $16.8 billion, and $8.6 billion, respectively, through our share repurchase programs. All repurchases were made using cash resources. Refer to Note 16 – Stockholders' Equity of the Notes to Financial Statements for further discussion.

Dividends

Refer to Note 16 – Stockholders' Equity of the Notes to Financial Statements for further discussion.

Off-Balance Sheet Arrangements

We provide indemnifications of varying scope and size to certain customers against claims of intellectual property infringement made by third parties arising from the use of our products and certain other matters. Additionally, we have agreed to cover damages resulting from breaches of certain security and privacy commitments in our cloud business. In evaluating estimated losses on these obligations, we consider factors such as the degree of probability of an unfavorable outcome and our ability to make a reasonable estimate of the amount of loss. These obligations did not have a material impact in our consolidated financial statements during the periods presented.

Contractual Obligations

The following table summarizes the payments due by fiscal year for our outstanding contractual obligations as of June 30, 2020:

(In millions)	2021	2022-2023	2024-2025	Thereafter	Total
Long-term debt: [a]					
Principal payments	$ 3,750	$ 10,716	$ 7,500	$ 45,441	$ 67,407
Interest payments	2,028	3,736	3,293	25,265	34,322
Construction commitments [b]	4,761	280	0	0	5,041
Operating leases, including imputed interest [c]	2,420	3,986	2,929	4,409	13,744
Finance leases, including imputed interest [c]	992	2,243	2,676	9,611	15,522
Transition tax [d]	1,450	2,899	6,343	4,531	15,223
Purchase commitments [e]	25,059	1,324	369	272	27,024
Other long-term liabilities [f]	0	294	32	356	682
Total	$ 40,460	$ 25,478	$ 23,142	$ 89,885	$ 178,965

(a) *Refer to Note 11 – Debt of the Notes to Financial Statements.*
(b) *Refer to Note 7 – Property and Equipment of the Notes to Financial Statements.*
(c) *Refer to Note 14 – Leases of the Notes to Financial Statements.*
(d) *Refer to Note 12 – Income Taxes of the Notes to Financial Statements.*
(e) *Amounts represent purchase commitments, including open purchase orders and take-or-pay contracts that are not presented as construction commitments above.*
(f) *We have excluded long-term tax contingencies, other tax liabilities, and deferred income taxes of $15.2 billion from the amounts presented as the timing of these obligations is uncertain. We have also excluded unearned revenue and non-cash items.*

Other Planned Uses of Capital

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

Liquidity

As a result of the TCJA, we are required to pay a one-time transition tax on deferred foreign income not previously subject to U.S. income tax. Under the TCJA, the transition tax is payable in interest-free installments over eight years, with 8% due in each of the first five years, 15% in year six, 20% in year seven, and 25% in year eight. We have paid

transition tax of $3.2 billion, which included $1.2 billion for fiscal year 2020. The remaining transition tax of $15.2 billion is payable over the next six years with a final payment in fiscal year 2026. During fiscal year 2020, we also paid $3.7 billion related to the transfer of intangible properties that occurred in the fourth quarter of fiscal year 2019.

We expect existing cash, cash equivalents, short-term investments, cash flows from operations, and access to capital markets to continue to be sufficient to fund our operating activities and cash commitments for investing and financing activities, such as dividends, share repurchases, debt maturities, material capital expenditures, and the transition tax related to the TCJA, for at least the next 12 months and thereafter for the foreseeable future.

RECENT ACCOUNTING GUIDANCE

Refer to Note 1 – Accounting Policies of the Notes to Financial Statements for further discussion.

APPLICATION OF CRITICAL ACCOUNTING POLICIES

Our consolidated financial statements and accompanying notes are prepared in accordance with GAAP. Preparing consolidated financial statements requires management to make estimates and assumptions that affect the reported amounts of assets, liabilities, revenue, and expenses. These estimates and assumptions are affected by management's application of accounting policies, as well as uncertainty in the current economic environment due to the recent outbreak of COVID-19. Critical accounting policies for us include revenue recognition, impairment of investment securities, goodwill, research and development costs, contingencies, income taxes, and inventories.

Revenue Recognition

Our contracts with customers often include promises to transfer multiple products and services to a customer. Determining whether products and services are considered distinct performance obligations that should be accounted for separately versus together may require significant judgment. When a cloud-based service includes both on-premises software licenses and cloud services, judgment is required to determine whether the software license is considered distinct and accounted for separately, or not distinct and accounted for together with the cloud service and recognized over time. Certain cloud services, primarily Office 365, depend on a significant level of integration, interdependency, and interrelation between the desktop applications and cloud services, and are accounted for together as one performance obligation. Revenue from Office 365 is recognized ratably over the period in which the cloud services are provided.

Judgment is required to determine the stand-alone selling price ("SSP") for each distinct performance obligation. We use a single amount to estimate SSP for items that are not sold separately, including on-premises licenses sold with SA or software updates provided at no additional charge. We use a range of amounts to estimate SSP when we sell each of the products and services separately and need to determine whether there is a discount to be allocated based on the relative SSP of the various products and services.

In instances where SSP is not directly observable, such as when we do not sell the product or service separately, we determine the SSP using information that may include market conditions and other observable inputs. We typically have more than one SSP for individual products and services due to the stratification of those products and services by customers and circumstances. In these instances, we may use information such as the size of the customer and geographic region in determining the SSP.

Due to the various benefits from and the nature of our SA program, judgment is required to assess the pattern of delivery, including the exercise pattern of certain benefits across our portfolio of customers.

Our products are generally sold with a right of return, we may provide other credits or incentives, and in certain instances we estimate customer usage of our products and services, which are accounted for as variable consideration when determining the amount of revenue to recognize. Returns and credits are estimated at contract inception and updated at the end of each reporting period if additional information becomes available. Changes to our estimated variable consideration were not material for the periods presented.

Impairment of Investment Securities

We review debt investments quarterly for indicators of other-than-temporary impairment. This determination requires significant judgment. In making this judgment, we employ a systematic methodology quarterly that considers available quantitative and qualitative evidence in evaluating potential impairment of our investments. If the cost of an investment exceeds its fair value, we evaluate, among other factors, general market conditions, credit quality of debt instrument issuers, and the duration and extent to which the fair value is less than cost. We also evaluate whether we have plans to sell the security or it is more likely than not that we will be required to sell the security before recovery. In addition, we consider specific adverse conditions related to the financial health of and business outlook for the investee, including industry and sector performance, changes in technology, and operational and financing cash flow factors. Once a decline in fair value is determined to be other-than-temporary, an impairment charge is recorded in other income (expense), net and a new cost basis in the investment is established. If market, industry, and/or investee conditions deteriorate, we may incur future impairments.

Equity investments without readily determinable fair values are written down to fair value if a qualitative assessment indicates that the investment is impaired and the fair value of the investment is less than carrying value. We perform a qualitative assessment on a quarterly basis. We are required to estimate the fair value of the investment to determine the amount of the impairment loss. Once an investment is determined to be impaired, an impairment charge is recorded in other income (expense), net.

Goodwill

We allocate goodwill to reporting units based on the reporting unit expected to benefit from the business combination. We evaluate our reporting units on an annual basis and, if necessary, reassign goodwill using a relative fair value allocation approach. Goodwill is tested for impairment at the reporting unit level (operating segment or one level below an operating segment) on an annual basis (May 1 for us) and between annual tests if an event occurs or circumstances change that would more likely than not reduce the fair value of a reporting unit below its carrying value. These events or circumstances could include a significant change in the business climate, legal factors, operating performance indicators, competition, or sale or disposition of a significant portion of a reporting unit.

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

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

Research and Development Costs

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

Legal and Other Contingencies

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

Income Taxes

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

The TCJA significantly changes existing U.S. tax law and includes numerous provisions that affect our business. Refer to Note 12 – Income Taxes of the Notes to Financial Statements for further discussion.

Inventories

Inventories are stated at average cost, subject to the lower of cost or net realizable value. Cost includes materials, labor, and manufacturing overhead related to the purchase and production of inventories. Net realizable value is the estimated selling price less estimated costs of completion, disposal, and transportation. We regularly review inventory quantities on hand, future purchase commitments with our suppliers, and the estimated utility of our inventory. These reviews include analysis of demand forecasts, product life cycle status, product development plans, current sales levels, pricing strategy, and component cost trends. If our review indicates a reduction in utility below carrying value, we reduce our inventory to a new cost basis through a charge to cost of revenue.

CHANGE IN ACCOUNTING ESTIMATE

In July 2020, we completed an assessment of the useful lives of our server and network equipment and determined we should increase the estimated useful life of server equipment from three years to four years and increase the estimated useful life of network equipment from two years to four years. This change in accounting estimate will be effective beginning fiscal year 2021. Based on the carrying amount of server and network equipment included in "Property and equipment, net" as of June 30, 2020, it is estimated this change will increase our fiscal year 2021 operating income by $2.7 billion.

STATEMENT OF MANAGEMENT'S RESPONSIBILITY FOR FINANCIAL STATEMENTS

Management is responsible for the preparation of the consolidated financial statements and related information that are presented in this report. The consolidated financial statements, which include amounts based on management's estimates and judgments, have been prepared in conformity with accounting principles generally accepted in the United States of America.

The Company designs and maintains accounting and internal control systems to provide reasonable assurance at reasonable cost that assets are safeguarded against loss from unauthorized use or disposition, and that the financial records are reliable for preparing consolidated financial statements and maintaining accountability for assets. These systems are augmented by written policies, an organizational structure providing division of responsibilities, careful selection and training of qualified personnel, and a program of internal audits.

The Company engaged Deloitte & Touche LLP, an independent registered public accounting firm, to audit and render an opinion on the consolidated financial statements and internal control over financial reporting in accordance with the standards of the Public Company Accounting Oversight Board (United States).

The Board of Directors, through its Audit Committee, consisting solely of independent directors of the Company, meets periodically with management, internal auditors, and our independent registered public accounting firm to ensure that each is meeting its responsibilities and to discuss matters concerning internal controls and financial reporting. Deloitte & Touche LLP and the internal auditors each have full and free access to the Audit Committee.

Satya Nadella
Chief Executive Officer

Amy E. Hood
Executive Vice President and Chief Financial Officer

Frank H. Brod
Corporate Vice President, Finance and Administration;
Chief Accounting Officer

QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

RISKS

We are exposed to economic risk from foreign exchange rates, interest rates, credit risk, and equity prices. We use derivatives instruments to manage these risks, however, they may still impact our consolidated financial statements.

Foreign Currencies

Certain forecasted transactions, assets, and liabilities are exposed to foreign currency risk. We monitor our foreign currency exposures daily to maximize the economic effectiveness of our foreign currency positions, including hedges. Principal currency exposures include the Euro, Japanese yen, British pound, Canadian dollar, and Australian dollar.

Interest Rate

Securities held in our fixed-income portfolio are subject to different interest rate risks based on their maturities. We manage the average maturity of the fixed-income portfolio to achieve economic returns that correlate to certain global fixed-income indices.

Credit

Our fixed-income portfolio is diversified and consists primarily of investment-grade securities. We manage credit exposures relative to broad-based indices and to facilitate portfolio diversification.

Equity

Securities held in our equity investments portfolio are subject to price risk.

SENSITIVITY ANALYSIS

The following table sets forth the potential loss in future earnings or fair values, including associated derivatives, resulting from hypothetical changes in relevant market rates or prices:

(In millions)

Risk Categories	Hypothetical Change	June 30, 2020	Impact
Foreign currency – Revenue	10% decrease in foreign exchange rates	**$ (4,142)**	Earnings
Foreign currency – Investments	10% decrease in foreign exchange rates	**(119)**	Fair Value
Interest rate	100 basis point increase in U.S. treasury interest rates	**(3,951)**	Fair Value
Credit	100 basis point increase in credit spreads	**(301)**	Fair Value
Equity	10% decrease in equity market prices	**(239)**	Earnings

FINANCIAL STATEMENTS AND SUPPLEMENTARY DATA

INCOME STATEMENTS

(In millions, except per share amounts)

Year Ended June 30,	2020	2019	2018
Revenue:			
Product	**$ 68,041**	$ 66,069	$ 64,497
Service and other	**74,974**	59,774	45,863
Total revenue	**143,015**	125,843	110,360
Cost of revenue:			
Product	**16,017**	16,273	15,420
Service and other	**30,061**	26,637	22,933
Total cost of revenue	**46,078**	42,910	38,353
Gross margin	**96,937**	82,933	72,007
Research and development	**19,269**	16,876	14,726
Sales and marketing	**19,598**	18,213	17,469
General and administrative	**5,111**	4,885	4,754
Operating income	**52,959**	42,959	35,058
Other income, net	**77**	729	1,416
Income before income taxes	**53,036**	43,688	36,474
Provision for income taxes	**8,755**	4,448	19,903
Net income	**$ 44,281**	$ 39,240	$ 16,571
Earnings per share:			
Basic	**$ 5.82**	$ 5.11	$ 2.15
Diluted	**$ 5.76**	$ 5.06	$ 2.13
Weighted average shares outstanding:			
Basic	**7,610**	7,673	7,700
Diluted	**7,683**	7,753	7,794

Refer to accompanying notes.

COMPREHENSIVE INCOME STATEMENTS

(In millions)

Year Ended June 30,	2020	2019	2018
Net income	**$ 44,281**	$ 39,240	$ 16,571
Other comprehensive income (loss), net of tax:			
Net change related to derivatives	**(38)**	(173)	39
Net change related to investments	**3,990**	2,405	(2,717)
Translation adjustments and other	**(426)**	(318)	(178)
Other comprehensive income (loss)	**3,526**	1,914	(2,856)
Comprehensive income	**$ 47,807**	$ 41,154	$ 13,715

Refer to accompanying notes.

BALANCE SHEETS

(In millions)

June 30,	2020	2019
Assets		
Current assets:		
Cash and cash equivalents	**$ 13,576**	$ 11,356
Short-term investments	**122,951**	122,463
Total cash, cash equivalents, and short-term investments	**136,527**	133,819
Accounts receivable, net of allowance for doubtful accounts of **$788** and $411	**32,011**	29,524
Inventories	**1,895**	2,063
Other current assets	**11,482**	10,146
Total current assets	**181,915**	175,552
Property and equipment, net of accumulated depreciation of **$43,197** and $35,330	**44,151**	36,477
Operating lease right-of-use assets	**8,753**	7,379
Equity investments	**2,965**	2,649
Goodwill	**43,351**	42,026
Intangible assets, net	**7,038**	7,750
Other long-term assets	**13,138**	14,723
Total assets	**$ 301,311**	$ 286,556
Liabilities and stockholders' equity		
Current liabilities:		
Accounts payable	**$ 12,530**	$ 9,382
Current portion of long-term debt	**3,749**	5,516
Accrued compensation	**7,874**	6,830
Short-term income taxes	**2,130**	5,665
Short-term unearned revenue	**36,000**	32,676
Other current liabilities	**10,027**	9,351
Total current liabilities	**72,310**	69,420
Long-term debt	**59,578**	66,662
Long-term income taxes	**29,432**	29,612
Long-term unearned revenue	**3,180**	4,530
Deferred income taxes	**204**	233
Operating lease liabilities	**7,671**	6,188
Other long-term liabilities	**10,632**	7,581
Total liabilities	**183,007**	184,226
Commitments and contingencies		
Stockholders' equity:		
Common stock and paid-in capital – shares authorized 24,000; outstanding **7,571** and 7,643	**80,552**	78,520
Retained earnings	**34,566**	24,150
Accumulated other comprehensive income (loss)	**3,186**	(340)
Total stockholders' equity	**118,304**	102,330
Total liabilities and stockholders' equity	**$ 301,311**	$ 286,556

Refer to accompanying notes.

CASH FLOWS STATEMENTS

(In millions)

Year Ended June 30,	2020	2019	2018
Operations			
Net income	**$ 44,281**	$ 39,240	$ 16,571
Adjustments to reconcile net income to net cash from operations:			
Depreciation, amortization, and other	**12,796**	11,682	10,261
Stock-based compensation expense	**5,289**	4,652	3,940
Net recognized gains on investments and derivatives	**(219)**	(792)	(2,212)
Deferred income taxes	**11**	(6,463)	(5,143)
Changes in operating assets and liabilities:			
Accounts receivable	**(2,577)**	(2,812)	(3,862)
Inventories	**168**	597	(465)
Other current assets	**(2,330)**	(1,718)	(952)
Other long-term assets	**(1,037)**	(1,834)	(285)
Accounts payable	**3,018**	232	1,148
Unearned revenue	**2,212**	4,462	5,922
Income taxes	**(3,631)**	2,929	18,183
Other current liabilities	**1,346**	1,419	798
Other long-term liabilities	**1,348**	591	(20)
Net cash from operations	**60,675**	52,185	43,884
Financing			
Repayments of short-term debt, maturities of 90 days or less, net	**0**	0	(7,324)
Proceeds from issuance of debt	**0**	0	7,183
Cash premium on debt exchange	**(3,417)**	0	0
Repayments of debt	**(5,518)**	(4,000)	(10,060)
Common stock issued	**1,343**	1,142	1,002
Common stock repurchased	**(22,968)**	(19,543)	(10,721)
Common stock cash dividends paid	**(15,137)**	(13,811)	(12,699)
Other, net	**(334)**	(675)	(971)
Net cash used in financing	**(46,031)**	(36,887)	(33,590)
Investing			
Additions to property and equipment	**(15,441)**	(13,925)	(11,632)
Acquisition of companies, net of cash acquired, and purchases of intangible and other assets	**(2,521)**	(2,388)	(888)
Purchases of investments	**(77,190)**	(57,697)	(137,380)
Maturities of investments	**66,449**	20,043	26,360
Sales of investments	**17,721**	38,194	117,577
Other, net	**(1,241)**	0	(98)
Net cash used in investing	**(12,223)**	(15,773)	(6,061)
Effect of foreign exchange rates on cash and cash equivalents	**(201)**	(115)	50
Net change in cash and cash equivalents	**2,220**	(590)	4,283
Cash and cash equivalents, beginning of period	**11,356**	11,946	7,663
Cash and cash equivalents, end of period	**$ 13,576**	$ 11,356	$ 11,946

Refer to accompanying notes.

STOCKHOLDERS' EQUITY STATEMENTS

(In millions)

Year Ended June 30,	2020	2019	2018
Common stock and paid-in capital			
Balance, beginning of period	**$ 78,520**	$ 71,223	$ 69,315
Common stock issued	**1,343**	6,829	1,002
Common stock repurchased	**(4,599)**	(4,195)	(3,033)
Stock-based compensation expense	**5,289**	4,652	3,940
Other, net	**(1)**	11	(1)
Balance, end of period	**80,552**	78,520	71,223
Retained earnings			
Balance, beginning of period	**24,150**	13,682	17,769
Net income	**44,281**	39,240	16,571
Common stock cash dividends	**(15,483)**	(14,103)	(12,917)
Common stock repurchased	**(18,382)**	(15,346)	(7,699)
Cumulative effect of accounting changes	**0**	677	(42)
Balance, end of period	**34,566**	24,150	13,682
Accumulated other comprehensive income (loss)			
Balance, beginning of period	**(340)**	(2,187)	627
Other comprehensive income (loss)	**3,526**	1,914	(2,856)
Cumulative effect of accounting changes	**0**	(67)	42
Balance, end of period	**3,186**	(340)	(2,187)
Total stockholders' equity	**$ 118,304**	$ 102,330	$ 82,718
Cash dividends declared per common share	**$ 2.04**	$ 1.84	$ 1.68

Refer to accompanying notes.

NOTES TO FINANCIAL STATEMENTS

NOTE 1 — ACCOUNTING POLICIES

Accounting Principles

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

We have recast certain prior period amounts to conform to the current period presentation. The recast of these prior period amounts had no impact on our consolidated balance sheets, consolidated income statements, or net cash from or used in operating, financing, or investing on our consolidated cash flows statements.

Principles of Consolidation

The consolidated financial statements include the accounts of Microsoft Corporation and its subsidiaries. Intercompany transactions and balances have been eliminated.

Estimates and Assumptions

Preparing financial statements requires management to make estimates and assumptions that affect the reported amounts of assets, liabilities, revenue, and expenses. Examples of estimates and assumptions include: for revenue recognition, determining the nature and timing of satisfaction of performance obligations, and determining the standalone selling price ("SSP") of performance obligations, variable consideration, and other obligations such as product returns and refunds; loss contingencies; product warranties; the fair value of and/or potential impairment of goodwill and intangible assets for our reporting units; product life cycles; useful lives of our tangible and intangible assets; allowances for doubtful accounts; the market value of, and demand for, our inventory; stock-based compensation forfeiture rates; when technological feasibility is achieved for our products; the potential outcome of uncertain tax positions that have been recognized in our consolidated financial statements or tax returns; and determining the timing and amount of impairments for investments. Actual results and outcomes may differ from management's estimates and assumptions due to risks and uncertainties, including uncertainty in the current economic environment due to the recent outbreak of a novel strain of the coronavirus ("COVID-19").

In July 2020, we completed an assessment of the useful lives of our server and network equipment and determined we should increase the estimated useful life of server equipment from three years to four years and increase the estimated useful life of network equipment from two years to four years. This change in accounting estimate will be effective beginning fiscal year 2021.

Foreign Currencies

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

Revenue

Product Revenue and Service and Other Revenue

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

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

Revenue Recognition

Revenue is recognized upon transfer of control of promised products or services to customers in an amount that reflects the consideration we expect to receive in exchange for those products or services. We enter into contracts that can include various combinations of products and services, which are generally capable of being distinct and accounted for as separate performance obligations. Revenue is recognized net of allowances for returns and any taxes collected from customers, which are subsequently remitted to governmental authorities.

Nature of Products and Services

Licenses for on-premises software provide the customer with a right to use the software as it exists when made available to the customer. Customers may purchase perpetual licenses or subscribe to licenses, which provide customers with the same functionality and differ mainly in the duration over which the customer benefits from the software. Revenue from distinct on-premises licenses is recognized upfront at the point in time when the software is made available to the customer. In cases where we allocate revenue to software updates, primarily because the updates are provided at no additional charge, revenue is recognized as the updates are provided, which is generally ratably over the estimated life of the related device or license.

Certain volume licensing programs, including Enterprise Agreements, include on-premises licenses combined with Software Assurance (“SA”). SA conveys rights to new software and upgrades released over the contract period and provides support, tools, and training to help customers deploy and use products more efficiently. On-premises licenses are considered distinct performance obligations when sold with SA. Revenue allocated to SA is generally recognized ratably over the contract period as customers simultaneously consume and receive benefits, given that SA comprises distinct performance obligations that are satisfied over time.

Cloud services, which allow customers to use hosted software over the contract period without taking possession of the software, are provided on either a subscription or consumption basis. Revenue related to cloud services provided on a subscription basis is recognized ratably over the contract period. Revenue related to cloud services provided on a consumption basis, such as the amount of storage used in a period, is recognized based on the customer utilization of such resources. When cloud services require a significant level of integration and interdependency with software and the individual components are not considered distinct, all revenue is recognized over the period in which the cloud services are provided.

Revenue from search advertising is recognized when the advertisement appears in the search results or when the action necessary to earn the revenue has been completed. Revenue from consulting services is recognized as services are provided.

Our hardware is generally highly dependent on, and interrelated with, the underlying operating system and cannot function without the operating system. In these cases, the hardware and software license are accounted for as a single performance obligation and revenue is recognized at the point in time when ownership is transferred to resellers or directly to end customers through retail stores and online marketplaces.

Refer to Note 19 – Segment Information and Geographic Data for further information, including revenue by significant product and service offering.

Significant Judgments

Our contracts with customers often include promises to transfer multiple products and services to a customer. Determining whether products and services are considered distinct performance obligations that should be

accounted for separately versus together may require significant judgment. When a cloud-based service includes both on-premises software licenses and cloud services, judgment is required to determine whether the software license is considered distinct and accounted for separately, or not distinct and accounted for together with the cloud service and recognized over time. Certain cloud services, primarily Office 365, depend on a significant level of integration, interdependency, and interrelation between the desktop applications and cloud services, and are accounted for together as one performance obligation. Revenue from Office 365 is recognized ratably over the period in which the cloud services are provided.

Judgment is required to determine the SSP for each distinct performance obligation. We use a single amount to estimate SSP for items that are not sold separately, including on-premises licenses sold with SA or software updates provided at no additional charge. We use a range of amounts to estimate SSP when we sell each of the products and services separately and need to determine whether there is a discount to be allocated based on the relative SSP of the various products and services.

In instances where SSP is not directly observable, such as when we do not sell the product or service separately, we determine the SSP using information that may include market conditions and other observable inputs. We typically have more than one SSP for individual products and services due to the stratification of those products and services by customers and circumstances. In these instances, we may use information such as the size of the customer and geographic region in determining the SSP.

Due to the various benefits from and the nature of our SA program, judgment is required to assess the pattern of delivery, including the exercise pattern of certain benefits across our portfolio of customers.

Our products are generally sold with a right of return, we may provide other credits or incentives, and in certain instances we estimate customer usage of our products and services, which are accounted for as variable consideration when determining the amount of revenue to recognize. Returns and credits are estimated at contract inception and updated at the end of each reporting period if additional information becomes available. Changes to our estimated variable consideration were not material for the periods presented.

Contract Balances

Timing of revenue recognition may differ from the timing of invoicing to customers. We record a receivable when revenue is recognized prior to invoicing, or unearned revenue when revenue is recognized subsequent to invoicing. For multi-year agreements, we generally invoice customers annually at the beginning of each annual coverage period. We record a receivable related to revenue recognized for multi-year on-premises licenses as we have an unconditional right to invoice and receive payment in the future related to those licenses.

As of June 30, 2020 and 2019, long-term accounts receivable, net of allowance for doubtful accounts, was $2.7 billion and $2.2 billion, respectively, and is included in other long-term assets in our consolidated balance sheets.

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

Activity in the allowance for doubtful accounts was as follows:

(In millions)

Year Ended June 30,	2020	2019	2018
Balance, beginning of period	**$ 434**	$ 397	$ 361
Charged to costs and other	**560**	153	134
Write-offs	**(178)**	(116)	(98)
Balance, end of period	**$ 816**	$ 434	$ 397

Allowance for doubtful accounts included in our consolidated balance sheets:

(In millions) June 30,	2020	2019	2018
Accounts receivable, net of allowance for doubtful accounts	**$ 788**	$ 411	$ 377
Other long-term assets	**28**	23	20
Total	**$ 816**	$ 434	$ 397

Unearned revenue comprises mainly unearned revenue related to volume licensing programs, which may include SA and cloud services. Unearned revenue is generally invoiced annually at the beginning of each contract period for multi-year agreements and recognized ratably over the coverage period. Unearned revenue also includes payments for consulting services to be performed in the future; LinkedIn subscriptions; Office 365 subscriptions; Xbox Live subscriptions; Windows 10 post-delivery support; Dynamics business solutions; Skype prepaid credits and subscriptions; and other offerings for which we have been paid in advance and earn the revenue when we transfer control of the product or service.

Refer to Note 13 – Unearned Revenue for further information, including unearned revenue by segment and changes in unearned revenue during the period.

Payment terms and conditions vary by contract type, although terms generally include a requirement of payment within 30 to 60 days. In instances where the timing of revenue recognition differs from the timing of invoicing, we have determined our contracts generally do not include a significant financing component. The primary purpose of our invoicing terms is to provide customers with simplified and predictable ways of purchasing our products and services, not to receive financing from our customers or to provide customers with financing. Examples include invoicing at the beginning of a subscription term with revenue recognized ratably over the contract period, and multi-year on-premises licenses that are invoiced annually with revenue recognized upfront.

We record financing receivables when we offer certain of our customers the option to acquire our software products and services offerings through a financing program in a limited number of countries. As of June 30, 2020 and 2019, our financing receivables, net were $5.2 billion and $4.3 billion, respectively, for short-term and long-term financing receivables, which are included in other current assets and other long-term assets in our consolidated balance sheets. We record an allowance to cover expected losses based on troubled accounts, historical experience, and other currently available evidence.

Assets Recognized from Costs to Obtain a Contract with a Customer

We recognize an asset for the incremental costs of obtaining a contract with a customer if we expect the benefit of those costs to be longer than one year. We have determined that certain sales incentive programs meet the requirements to be capitalized. Total capitalized costs to obtain a contract were immaterial during the periods presented and are included in other current and long-term assets in our consolidated balance sheets.

We apply a practical expedient to expense costs as incurred for costs to obtain a contract with a customer when the amortization period would have been one year or less. These costs include our internal sales force compensation program and certain partner sales incentive programs as we have determined annual compensation is commensurate with annual sales activities.

Cost of Revenue

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

Product Warranty

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

Research and Development

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

Sales and Marketing

Sales and marketing expenses include payroll, employee benefits, stock-based compensation expense, and other headcount-related expenses associated with sales and marketing personnel, and the costs of advertising, promotions, trade shows, seminars, and other programs. Advertising costs are expensed as incurred. Advertising expense was $1.6 billion in fiscal years 2020, 2019, and 2018.

Stock-Based Compensation

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

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

Income Taxes

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

Financial Instruments

Investments

We consider all highly liquid interest-earning investments with a maturity of three months or less at the date of purchase to be cash equivalents. The fair values of these investments approximate their carrying values. In general, investments with original maturities of greater than three months and remaining maturities of less than one year are classified as short-term investments. Investments with maturities beyond one year may be classified as short-term based on their highly liquid nature and because such marketable securities represent the investment of cash that is available for current operations.

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

Equity investments with readily determinable fair values are measured at fair value. Equity investments without readily determinable fair values are measured using the equity method or measured at cost with adjustments for observable changes in price or impairments (referred to as the measurement alternative). We perform a qualitative assessment on a quarterly basis and recognize an impairment if there are sufficient indicators that the fair value of the investment is less than carrying value. Changes in value are recorded in other income (expense), net.

Derivatives

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

For derivative instruments designated as fair value hedges, gains and losses are recognized in other income (expense), net with offsetting gains and losses on the hedged items. Gains and losses representing hedge components excluded from the assessment of effectiveness are recognized in other income (expense), net.

For derivative instruments designated as cash flow hedges, gains and losses are initially reported as a component of other comprehensive income and subsequently recognized in earnings with the corresponding hedged item. Gains and losses representing hedge components excluded from the assessment of effectiveness are recognized in earnings.

For derivative instruments that are not designated as hedges, gains and losses from changes in fair values are primarily recognized in other income (expense), net.

Fair Value Measurements

We account for certain assets and liabilities at fair value. The hierarchy below lists three levels of fair value based on the extent to which inputs used in measuring fair value are observable in the market. We categorize each of our fair

value measurements in one of these three levels based on the lowest level input that is significant to the fair value measurement in its entirety. These levels are:

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

We measure equity investments without readily determinable fair values on a nonrecurring basis. The fair values of these investments are determined based on valuation techniques using the best information available, and may include quoted market prices, market comparables, and discounted cash flow projections.

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

Inventories

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

Property and Equipment

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

Leases

We determine if an arrangement is a lease at inception. Operating leases are included in operating lease right-of-use ("ROU") assets, other current liabilities, and operating lease liabilities in our consolidated balance sheets. Finance leases are included in property and equipment, other current liabilities, and other long-term liabilities in our consolidated balance sheets.

ROU assets represent our right to use an underlying asset for the lease term and lease liabilities represent our obligation to make lease payments arising from the lease. Operating lease ROU assets and liabilities are recognized at commencement date based on the present value of lease payments over the lease term. As most of our leases do not provide an implicit rate, we generally use our incremental borrowing rate based on the estimated rate of interest for collateralized borrowing over a similar term of the lease payments at commencement date. The operating lease ROU asset also includes any lease payments made and excludes lease incentives. Our lease terms may include options to extend or terminate the lease when it is reasonably certain that we will exercise that option. Lease expense for lease payments is recognized on a straight-line basis over the lease term.

We have lease agreements with lease and non-lease components, which are generally accounted for separately. For certain equipment leases, such as vehicles, we account for the lease and non-lease components as a single lease component. Additionally, for certain equipment leases, we apply a portfolio approach to effectively account for the operating lease ROU assets and liabilities.

Goodwill

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

Intangible Assets

Our intangible assets are subject to amortization and are amortized using the straight-line method over their estimated period of benefit, ranging from one to 20 years. We evaluate the recoverability of intangible assets periodically by taking into account events or circumstances that may warrant revised estimates of useful lives or that indicate the asset may be impaired.

Recent Accounting Guidance

Recently Adopted Accounting Guidance

Financial Instruments – Targeted Improvements to Accounting for Hedging Activities

In August 2017, the Financial Accounting Standards Board (“FASB”) issued new guidance related to accounting for hedging activities. This guidance expands strategies that qualify for hedge accounting, changes how many hedging relationships are presented in the financial statements, and simplifies the application of hedge accounting in certain situations. We adopted the standard effective July 1, 2019. As we did not hold derivative instruments requiring an adjustment upon adoption, there was no impact in our consolidated financial statements. Adoption of the standard enhanced the presentation of the effects of our hedging instruments and the hedged items in our consolidated financial statements to increase the understandability of the results of our hedging strategies.

Recent Accounting Guidance Not Yet Adopted

Financial Instruments – Credit Losses

In June 2016, the FASB issued a new standard to replace the incurred loss impairment methodology under current GAAP with a methodology that reflects expected credit losses and requires consideration of a broader range of reasonable and supportable information to inform credit loss estimates. We will be required to use a forward-looking expected credit loss model for accounts receivable, loans, and other financial instruments. Credit losses relating to available-for-sale debt securities will also be recorded through an allowance for credit losses rather than as a reduction in the amortized cost basis of the securities. The standard will be adopted upon the effective date for us beginning July 1, 2020. Adoption of the standard will be applied using a modified retrospective approach through

a cumulative-effect adjustment to retained earnings as of the effective date to align our credit loss methodology with the new standard. We have evaluated the impact of this standard in our consolidated financial statements, including accounting policies, processes, and systems. We continue to monitor economic implications of the COVID-19 pandemic. Based on current market conditions, adoption of the standard will not have a material impact on our consolidated financial statements.

Accounting for Income Taxes

In December 2019, the FASB issued a new standard to simplify the accounting for income taxes. The guidance eliminates certain exceptions related to the approach for intraperiod tax allocation, the methodology for calculating income taxes in an interim period, and the recognition of deferred tax liabilities for outside basis differences related to changes in ownership of equity method investments and foreign subsidiaries. The guidance also simplifies aspects of accounting for franchise taxes and enacted changes in tax laws or rates, and clarifies the accounting for transactions that result in a step-up in the tax basis of goodwill. The standard will be effective for us beginning July 1, 2021, with early adoption permitted. We are currently evaluating the impact of this standard in our consolidated financial statements, including accounting policies, processes, and systems.

NOTE 2 — EARNINGS PER SHARE

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

The components of basic and diluted EPS were as follows:

(In millions, except earnings per share)

Year Ended June 30,	**2020**	**2019**	**2018**
Net income available for common shareholders (A)	**$ 44,281**	$ 39,240	$ 16,571
Weighted average outstanding shares of common stock (B)	**7,610**	7,673	7,700
Dilutive effect of stock-based awards	**73**	80	94
Common stock and common stock equivalents (C)	**7,683**	7,753	7,794
Earnings Per Share			
Basic (A/B)	**$ 5.82**	$ 5.11	$ 2.15
Diluted (A/C)	**$ 5.76**	$ 5.06	$ 2.13

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

NOTE 3 — OTHER INCOME (EXPENSE), NET

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

(In millions)

Year Ended June 30,	**2020**	**2019**	**2018**
Interest and dividends income	**$ 2,680**	$ 2,762	$ 2,214
Interest expense	**(2,591)**	(2,686)	(2,733)
Net recognized gains on investments	**32**	648	2,399
Net gains (losses) on derivatives	**187**	144	(187)
Net losses on foreign currency remeasurements	**(191)**	(82)	(218)
Other, net	**(40)**	(57)	(59)
Total	**$ 77**	$ 729	$ 1,416

Net Recognized Gains (Losses) on Investments

Net recognized gains (losses) on debt investments were as follows:

(In millions)

Year Ended June 30,	2020	2019	2018
Realized gains from sales of available-for-sale securities	**$ 50**	$ 12	$ 27
Realized losses from sales of available-for-sale securities	**(37)**	(93)	(987)
Other-than-temporary impairments of investments	**(17)**	(16)	(6)
Total	**$ (4)**	$ (97)	$ (966)

Net recognized gains (losses) on equity investments were as follows:

(In millions)

Year Ended June 30,	2020	2019	2018
Net realized gains on investments sold	**$ 83**	$ 276	$ 3,406
Net unrealized gains on investments still held	**69**	479	0
Impairments of investments	**(116)**	(10)	(41)
Total	**$ 36**	$ 745	$ 3,365

NOTE 4 — INVESTMENTS

Investment Components

The components of investments were as follows:

(In millions)	Fair Value Level	Cost Basis	Unrealized Gains	Unrealized Losses	Recorded Basis	Cash and Cash Equivalents	Short-term Investments	Equity Investments
June 30, 2020								
Changes in Fair Value Recorded in Other Comprehensive Income								
Commercial paper	Level 2	$ 4,687	$ 1	$ 0	$ 4,688	$ 1,618	$ 3,070	$ 0
Certificates of deposit	Level 2	2,898	0	0	2,898	1,646	1,252	0
U.S. government securities	Level 1	92,067	6,495	(1)	98,561	3,168	95,393	0
U.S. agency securities	Level 2	2,439	2	0	2,441	449	1,992	0
Foreign government bonds	Level 2	6,982	6	(3)	6,985	1	6,984	0
Mortgage- and asset-backed securities	Level 2	4,865	41	(6)	4,900	0	4,900	0
Corporate notes and bonds	Level 2	8,500	327	(17)	8,810	0	8,810	0
Corporate notes and bonds	Level 3	58	0	0	58	0	58	0
Municipal securities	Level 2	313	57	(4)	366	0	366	0
Municipal securities	Level 3	91	0	0	91	0	91	0
Total debt investments		$ 122,900	$ 6,929	$ (31)	$ 129,798	$ 6,882	$ 122,916	$ 0
Changes in Fair Value Recorded in Net Income								
Equity investments	Level 1				$ 1,198	$ 784	$ 0	$ 414
Equity investments	Other				2,551	0	0	2,551
Total equity investments					$ 3,749	$ 784	$ 0	$ 2,965
Cash					$ 5,910	$ 5,910	$ 0	$ 0
Derivatives, net [a]					35	0	35	0
Total					$ 139,492	$ 13,576	$ 122,951	$ 2,965

(In millions)	Fair Value Level	Cost Basis	Unrealized Gains	Unrealized Losses	Recorded Basis	Cash and Cash Equivalents	Short-term Investments	Equity Investments
June 30, 2019								
Changes in Fair Value Recorded in Other Comprehensive Income								
Commercial paper	Level 2	$ 2,211	$ 0	$ 0	$ 2,211	$ 1,773	$ 438	$ 0
Certificates of deposit	Level 2	2,018	0	0	2,018	1,430	588	0
U.S. government securities	Level 1	104,925	1,854	(104)	106,675	769	105,906	0
U.S. agency securities	Level 2	988	0	0	988	698	290	0
Foreign government bonds	Level 2	6,350	4	(8)	6,346	2,506	3,840	0
Mortgage- and asset-backed securities	Level 2	3,554	10	(3)	3,561	0	3,561	0
Corporate notes and bonds	Level 2	7,437	111	(7)	7,541	0	7,541	0
Corporate notes and bonds	Level 3	15	0	0	15	0	15	0
Municipal securities	Level 2	242	48	0	290	0	290	0
Municipal securities	Level 3	7	0	0	7	0	7	0
Total debt investments		$ 127,747	$ 2,027	$ (122)	$ 129,652	$ 7,176	$ 122,476	$ 0
Changes in Fair Value Recorded in Net Income								
Equity investments	Level 1				$ 973	$ 409	$ 0	$ 564
Equity investments	Other				2,085	0	0	2,085
Total equity investments					$ 3,058	$ 409	$ 0	$ 2,649
Cash					$ 3,771	$ 3,771	$ 0	$ 0
Derivatives, net [(a)]					(13)	0	(13)	0
Total					$ 136,468	$ 11,356	$ 122,463	$ 2,649

(a) *Refer to Note 5 – Derivatives for further information on the fair value of our derivative instruments.*

Equity investments presented as “Other” in the tables above include investments without readily determinable fair values measured using the equity method or measured at cost with adjustments for observable changes in price or impairments, and investments measured at fair value using net asset value as a practical expedient which are not categorized in the fair value hierarchy. As of June 30, 2020 and 2019, equity investments without readily determinable fair values measured at cost with adjustments for observable changes in price or impairments were $1.4 billion and $1.2 billion, respectively.

Unrealized Losses on Debt Investments

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

(In millions)	Less than 12 Months Fair Value	Less than 12 Months Unrealized Losses	12 Months or Greater Fair Value	12 Months or Greater Unrealized Losses	Total Fair Value	Total Unrealized Losses
June 30, 2020						
U.S. government and agency securities	**$ 2,323**	**$ (1)**	**$ 0**	**$ 0**	**$ 2,323**	**$ (1)**
Foreign government bonds	**500**	**(3)**	**0**	**0**	**500**	**(3)**
Mortgage- and asset-backed securities	**1,014**	**(6)**	**0**	**0**	**1,014**	**(6)**
Corporate notes and bonds	**649**	**(17)**	**0**	**0**	**649**	**(17)**
Municipal securities	**66**	**(4)**	**0**	**0**	**66**	**(4)**
Total	**$ 4,552**	**$ (31)**	**$ 0**	**$ 0**	**$ 4,552**	**$ (31)**

(In millions)	Less than 12 Months Fair Value	Less than 12 Months Unrealized Losses	12 Months or Greater Fair Value	12 Months or Greater Unrealized Losses	Total Fair Value	Total Unrealized Losses
June 30, 2019						
U.S. government and agency securities	$ 1,491	$ (1)	$ 39,158	$ (103)	$ 40,649	$ (104)
Foreign government bonds	25	0	77	(8)	102	(8)
Mortgage- and asset-backed securities	664	(1)	378	(2)	1,042	(3)
Corporate notes and bonds	498	(3)	376	(4)	874	(7)
Total	$ 2,678	$ (5)	$ 39,989	$ (117)	$ 42,667	$ (122)

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

Debt Investment Maturities

(In millions)	Cost Basis	Estimated Fair Value
June 30, 2020		
Due in one year or less	**$ 36,169**	**$ 36,276**
Due after one year through five years	**51,465**	**54,700**
Due after five years through 10 years	**32,299**	**35,674**
Due after 10 years	**2,967**	**3,148**
Total	**$ 122,900**	**$ 129,798**

NOTE 5 — DERIVATIVES

We use derivative instruments to manage risks related to foreign currencies, interest rates, equity prices, and credit; to enhance investment returns; and to facilitate portfolio diversification. Our objectives for holding derivatives include reducing, eliminating, and efficiently managing the economic impact of these exposures as effectively as possible. Our derivative programs include strategies that both qualify and do not qualify for hedge accounting treatment.

Foreign Currencies

Certain forecasted transactions, assets, and liabilities are exposed to foreign currency risk. We monitor our foreign currency exposures daily to maximize the economic effectiveness of our foreign currency hedge positions.

Foreign currency risks related to certain non-U.S. dollar-denominated investments are hedged using foreign exchange forward contracts that are designated as fair value hedging instruments. Foreign currency risks related to certain Euro-denominated debt are hedged using foreign exchange forward contracts that are designated as cash flow hedging instruments.

In the past, option and forward contracts were used to hedge a portion of forecasted international revenue and were designated as cash flow hedging instruments. Principal currencies hedged included the Euro, Japanese yen, British pound, Canadian dollar, and Australian dollar.

Certain options and forwards not designated as hedging instruments are also used to manage the variability in foreign exchange rates on certain balance sheet amounts and to manage other foreign currency exposures.

Interest Rate

Interest rate risks related to certain fixed-rate debt are hedged using interest rate swaps that are designated as fair value hedging instruments to effectively convert the fixed interest rates to floating interest rates.

Securities held in our fixed-income portfolio are subject to different interest rate risks based on their maturities. We manage the average maturity of our fixed-income portfolio to achieve economic returns that correlate to certain broad-based fixed-income indices using exchange-traded option and futures contracts and over-the-counter swap and option contracts. These contracts are not designated as hedging instruments and are included in “Other contracts” in the tables below.

Equity

Securities held in our equity investments portfolio are subject to market price risk. At times, we may hold options, futures, and swap contracts. These contracts are not designated as hedging instruments and are included in “Other contracts” in the tables below.

Credit

Our fixed-income portfolio is diversified and consists primarily of investment-grade securities. We use credit default swap contracts to manage credit exposures relative to broad-based indices and to facilitate portfolio diversification. These contracts are not designated as hedging instruments and are included in “Other contracts” in the tables below.

Credit-Risk-Related Contingent Features

Certain of our counterparty agreements for derivative instruments contain provisions that require our issued and outstanding long-term unsecured debt to maintain an investment grade credit rating and require us to maintain minimum liquidity of $1.0 billion. To the extent we fail to meet these requirements, we will be required to post collateral, similar to the standard convention related to over-the-counter derivatives. As of June 30, 2020, our long-term unsecured debt rating was AAA, and cash investments were in excess of $1.0 billion. As a result, no collateral was required to be posted.

The following table presents the notional amounts of our outstanding derivative instruments measured in U.S. dollar equivalents:

(In millions)	June 30, 2020	June 30, 2019
Designated as Hedging Instruments		
Foreign exchange contracts purchased	**$ 635**	$ 0
Foreign exchange contracts sold	**6,754**	6,034
Interest rate contracts purchased	**1,295**	0
Not Designated as Hedging Instruments		
Foreign exchange contracts purchased	**11,896**	14,889
Foreign exchange contracts sold	**15,595**	15,614
Other contracts purchased	**1,844**	2,007
Other contracts sold	**757**	456

Fair Values of Derivative Instruments

The following table presents our derivative instruments:

(In millions)	Derivative Assets	Derivative Liabilities	Derivative Assets	Derivative Liabilities
		June 30, 2020		June 30, 2019
Designated as Hedging Instruments				
Foreign exchange contracts	**$ 44**	**$ (54)**	$ 0	$ (93)
Interest rate contracts	**93**	**0**	0	0
Not Designated as Hedging Instruments				
Foreign exchange contracts	**245**	**(334)**	204	(172)
Other contracts	**18**	**(11)**	46	(7)
Gross amounts of derivatives	**400**	**(399)**	250	(272)
Gross amounts of derivatives offset in the balance sheet	**(154)**	**158**	(113)	114
Cash collateral received	**0**	**(154)**	0	(78)
Net amounts of derivatives	**$ 246**	**$ (395)**	$ 137	$ (236)
Reported as				
Short-term investments	**$ 35**	**$ 0**	$ (13)	$ 0
Other current assets	**199**	**0**	146	0
Other long-term assets	**12**	**0**	4	0
Other current liabilities	**0**	**(334)**	0	(221)
Other long-term liabilities	**0**	**(61)**	0	(15)
Total	**$ 246**	**$ (395)**	$ 137	$ (236)

Gross derivative assets and liabilities subject to legally enforceable master netting agreements for which we have elected to offset were $399 million and $399 million, respectively, as of June 30, 2020, and $247 million and $272 million, respectively, as of June 30, 2019.

The following table presents the fair value of our derivatives instruments on a gross basis:

(In millions)	Level 1	Level 2	Level 3	Total
June 30, 2020				
Derivative assets	**$ 1**	**$ 398**	**$ 1**	**$ 400**
Derivative liabilities	**0**	**(399)**	**0**	**(399)**
June 30, 2019				
Derivative assets	0	247	3	250
Derivative liabilities	0	(272)	0	(272)

Gains (losses) on derivative instruments recognized in our consolidated income statements were as follows:

(In millions)

Year Ended June 30,	2020 Revenue	2020 Other Income (Expense), Net	2019 Revenue	2019 Other Income (Expense), Net	2018 Revenue	2018 Other Income (Expense), Net
Designated as Fair Value Hedging Instruments						
Foreign exchange contracts						
Derivatives	**$ 0**	**$ 1**	$ 0	$ (130)	$ 0	$ (78)
Hedged items	**0**	**3**	0	130	0	78
Excluded from effectiveness assessment	**0**	**139**	0	168	0	103
Interest rate contracts						
Derivatives	**0**	**93**	0	0	0	0
Hedged items	**0**	**(93)**	0	0	0	0
Equity contracts						
Derivatives	**0**	**0**	0	0	0	(324)
Hedged items	**0**	**0**	0	0	0	324
Excluded from effectiveness assessment	**0**	**0**	0	0	0	80
Designated as Cash Flow Hedging Instruments						
Foreign exchange contracts						
Amount reclassified from accumulated other comprehensive income	**0**	**0**	341	0	185	0
Excluded from effectiveness assessment	**0**	**0**	(64)	0	(255)	0
Not Designated as Hedging Instruments						
Foreign exchange contracts	**0**	**(123)**	0	(97)	0	(33)
Other contracts	**0**	**50**	0	38	0	(104)

Gains (losses), net of tax, on derivative instruments recognized in our consolidated comprehensive income statements were as follows:

(In millions)

Year Ended June 30,	2020	2019	2018
Designated as Cash Flow Hedging Instruments			
Foreign exchange contracts			
Included in effectiveness assessment	**$ (38)**	$ 159	$ 219

NOTE 6 — INVENTORIES

The components of inventories were as follows:

(In millions) June 30,	2020	2019
Raw materials	**$ 700**	$ 399
Work in process	**83**	53
Finished goods	**1,112**	1,611
Total	**$ 1,895**	$ 2,063

NOTE 7 — PROPERTY AND EQUIPMENT

The components of property and equipment were as follows:

(In millions) June 30,	2020	2019
Land	**$ 1,823**	$ 1,540
Buildings and improvements	**33,995**	26,288
Leasehold improvements	**5,487**	5,316
Computer equipment and software	**41,261**	33,823
Furniture and equipment	**4,782**	4,840
Total, at cost	**87,348**	71,807
Accumulated depreciation	**(43,197)**	(35,330)
Total, net	**$ 44,151**	$ 36,477

During fiscal years 2020, 2019, and 2018, depreciation expense was $10.7 billion, $9.7 billion, and $7.7 billion, respectively. We have committed $5.0 billion for the construction of new buildings, building improvements, and leasehold improvements as of June 30, 2020.

During fiscal year 2020, we recorded an impairment charge of $186 million to Property and Equipment, primarily to leasehold improvements, due to the closing of our Microsoft Store physical locations.

NOTE 8 — BUSINESS COMBINATIONS

GitHub, Inc.

On October 25, 2018, we acquired GitHub, Inc. (“GitHub”), a software development platform, in a $7.5 billion stock transaction (inclusive of total cash payments of $1.3 billion in respect of vested GitHub equity awards and an indemnity escrow). The acquisition is expected to empower developers to achieve more at every stage of the development lifecycle, accelerate enterprise use of GitHub, and bring Microsoft’s developer tools and services to new audiences. The financial results of GitHub have been included in our consolidated financial statements since the date of the acquisition. GitHub is reported as part of our Intelligent Cloud segment.

The allocation of the purchase price to goodwill was completed as of June 30, 2019. The major classes of assets and liabilities to which we allocated the purchase price were as follows:

(In millions)	
Cash, cash equivalents, and short-term investments	$ 234
Goodwill	5,497
Intangible assets	1,267
Other assets	143
Other liabilities	(217)
Total	$ 6,924

The goodwill recognized in connection with the acquisition is primarily attributable to anticipated synergies from future growth and is not expected to be deductible for tax purposes. We assigned the goodwill to our Intelligent Cloud segment.

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

(In millions)	Amount	Weighted Average Life
Customer-related	$ 648	8 years
Technology-based	447	5 years
Marketing-related	170	10 years
Contract-based	2	2 years
Total	$ 1,267	7 years

Transactions recognized separately from the purchase price allocation were approximately $600 million, primarily related to equity awards recognized as expense over the related service period.

Other

During fiscal year 2020, we completed 15 acquisitions for $2.4 billion, substantially all of which were paid in cash. These entities have been included in our consolidated results of operations since their respective acquisition dates. The effects of these business combinations, individually and in aggregate, were not material to our consolidated results of operations.

NOTE 9 — GOODWILL

Changes in the carrying amount of goodwill were as follows:

(In millions)	June 30, 2018	Acquisitions	Other	June 30, 2019	Acquisitions	Other	June 30, 2020
Productivity and Business Processes	$ 23,823	$ 514	$ (60)	**$ 24,277**	**$ 7**	**$ (94)**	**$ 24,190**
Intelligent Cloud	5,703	5,605 [(a)]	43 [(a)]	**11,351**	**1,351**	**(5)**	**12,697**
More Personal Computing	6,157	289	(48)	**6,398**	**96**	**(30)**	**6,464**
Total	$ 35,683	$ 6,408	$ (65)	**$ 42,026**	**$ 1,454**	**$ (129)**	**$ 43,351**

(a) *Includes goodwill of $5.5 billion related to GitHub. See Note 8 – Business Combinations for further information.*

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

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

Goodwill Impairment

We test goodwill for impairment annually on May 1 at the reporting unit level, primarily using a discounted cash flow methodology with a peer-based, risk-adjusted weighted average cost of capital. We believe use of a discounted cash flow approach is the most reliable indicator of the fair values of the businesses.

No instances of impairment were identified in our May 1, 2020, May 1, 2019, or May 1, 2018 tests. As of June 30, 2020 and 2019, accumulated goodwill impairment was $11.3 billion.

NOTE 10 — INTANGIBLE ASSETS

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

(In millions)	Gross Carrying Amount	Accumulated Amortization	Net Carrying Amount	Gross Carrying Amount	Accumulated Amortization	Net Carrying Amount
June 30,			**2020**			**2019**
Technology-based	**$ 8,160**	**$ (6,381)**	**$ 1,779**	$ 7,691	$ (5,771)	$ 1,920
Customer-related	**4,967**	**(2,320)**	**2,647**	4,709	(1,785)	2,924
Marketing-related	**4,158**	**(1,588)**	**2,570**	4,165	(1,327)	2,838
Contract-based	**474**	**(432)**	**42**	574	(506)	68
Total	**$ 17,759**	**$ (10,721)**	**$ 7,038**	$ 17,139 [(a)]	$ (9,389)	$ 7,750

(a) *Includes intangible assets of $1.3 billion related to GitHub. See Note 8 – Business Combinations for further information.*

No material impairments of intangible assets were identified during fiscal years 2020, 2019, or 2018. We estimate that we have no significant residual value related to our intangible assets.

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

(In millions)	Amount	Weighted Average Life	Amount	Weighted Average Life
Year Ended June 30,	**2020**		**2019**	
Technology-based	**$ 531**	**6 years**	$ 814	5 years
Customer-related	**303**	**5 years**	710	8 years
Marketing-related	**2**	**2 years**	177	10 years
Contract-based	**0**	**0 years**	7	3 years
Total	**$ 836**	**5 years**	$ 1,708	7 years

Intangible assets amortization expense was $1.6 billion, $1.9 billion, and $2.2 billion for fiscal years 2020, 2019, and 2018, respectively.

The following table outlines the estimated future amortization expense related to intangible assets held as of June 30, 2020:

(In millions)	
Year Ending June 30,	
2021	**$ 1,483**
2022	**1,399**
2023	**1,219**
2024	**851**
2025	**447**
Thereafter	**1,639**
Total	**$ 7,038**

NOTE 11 — DEBT

The components of debt were as follows:

(In millions, issuance by calendar year)	Maturities (calendar year)	Stated Interest Rate	Effective Interest Rate	June 30, 2020	June 30, 2019
2009 issuance of $3.8 billion [a]	**2039**	**5.20%**	**5.24%**	**$ 559**	$ 750
2010 issuance of $4.8 billion [a]	**2020–2040**	**3.00%–4.50%**	**3.14%–4.57%**	**1,571**	2,000
2011 issuance of $2.3 billion [a]	**2021–2041**	**4.00%–5.30%**	**4.08%–5.36%**	**1,270**	1,500
2012 issuance of $2.3 billion	**2022–2042**	**2.13%–3.50%**	**2.24%–3.57%**	**1,650**	1,650
2013 issuance of $5.2 billion [a]	**2023–2043**	**2.38%–4.88%**	**2.47%–4.92%**	**2,919**	3,500
2013 issuance of €4.1 billion	**2021–2033**	**2.13%–3.13%**	**2.23%–3.22%**	**4,549**	4,613
2014 issuance				**0**	18
2015 issuance of $23.8 billion [a]	**2020–2055**	**2.00%–4.75%**	**2.09%–4.78%**	**15,549**	22,000
2016 issuance of $19.8 billion [a]	**2021–2056**	**1.55%–3.95%**	**1.64%–4.03%**	**16,955**	19,750
2017 issuance of $17.0 billion [a]	**2022–2057**	**2.40%–4.50%**	**2.52%–4.53%**	**12,385**	17,000
2020 issuance of $10.0 billion [a]	**2050–2060**	**2.53%–2.68%**	**2.53%–2.68%**	**10,000**	0
Total face value				**67,407**	72,781
Unamortized discount and issuance costs				**(554)**	(603)
Hedge fair value adjustments [b]				**93**	0
Premium on debt exchange [a]				**(3,619)**	0
Total debt				**63,327**	72,178
Current portion of long-term debt				**(3,749)**	(5,516)
Long-term debt				**$ 59,578**	$ 66,662

(a) *In June 2020, we exchanged a portion of our existing debt at premium for cash and new debt with longer maturities. The premium will be amortized over the term of the new debt.*

(b) *Refer to Note 5 – Derivatives for further information on the interest rate swaps related to fixed-rate debt.*

As of June 30, 2020 and 2019, the estimated fair value of long-term debt, including the current portion, was $77.1 billion and $78.9 billion, respectively. The estimated fair values are based on Level 2 inputs.

Debt in the table above is comprised of senior unsecured obligations and ranks equally with our other outstanding obligations. Interest is paid semi-annually, except for the Euro-denominated debt, which is paid annually.

The following table outlines maturities of our long-term debt, including the current portion, as of June 30, 2020:

(In millions)	
Year Ending June 30,	
2021	**$ 3,750**
2022	**7,966**
2023	**2,750**
2024	**5,250**
2025	**2,250**
Thereafter	**45,441**
Total	**$ 67,407**

NOTE 12 — INCOME TAXES

Tax Cuts and Jobs Act

On December 22, 2017, the Tax Cuts and Jobs Act ("TCJA") was enacted into law, which significantly changed existing U.S. tax law and included numerous provisions that affect our business. We recorded a provisional net charge of $13.7 billion related to the enactment of the TCJA in fiscal year 2018, and adjusted the provisional net charge by recording additional tax expense of $157 million in fiscal year 2019 pursuant to Securities and Exchange Commission Staff Accounting Bulletin No. 118.

In fiscal year 2019, in response to the TCJA and recently issued regulations, we transferred certain intangible properties held by our foreign subsidiaries to the U.S. and Ireland. The transfers of intangible properties resulted in a $2.6 billion net income tax benefit recorded in the fourth quarter of fiscal year 2019, as the value of future tax deductions exceeded the current tax liability from foreign jurisdictions and U.S. global intangible low-taxed income ("GILTI") tax.

Provision for Income Taxes

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

(In millions)

Year Ended June 30,	2020	2019	2018
Current Taxes			
U.S. federal	**$ 3,537**	$ 4,718	$ 19,764
U.S. state and local	**763**	662	934
Foreign	**4,444**	5,531	4,348
Current taxes	**$ 8,744**	$ 10,911	$ 25,046
Deferred Taxes			
U.S. federal	**$ 58**	$ (5,647)	$ (4,292)
U.S. state and local	**(6)**	(1,010)	(458)
Foreign	**(41)**	194	(393)
Deferred taxes	**$ 11**	$ (6,463)	$ (5,143)
Provision for income taxes	**$ 8,755**	$ 4,448	$ 19,903

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

(In millions)

Year Ended June 30,	2020	2019	2018
U.S.	**$ 24,116**	$ 15,799	$ 11,527
Foreign	**28,920**	27,889	24,947
Income before income taxes	**$ 53,036**	$ 43,688	$ 36,474

Effective Tax Rate

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

Year Ended June 30,	2020	2019	2018
Federal statutory rate	**21.0%**	21.0%	28.1%
Effect of:			
Foreign earnings taxed at lower rates	**(3.7)%**	(4.1)%	(7.8)%
Impact of the enactment of the TCJA	**0%**	0.4%	37.7%
Impact of intangible property transfers	**0%**	(5.9)%	0%
Foreign-derived intangible income deduction	**(1.1)%**	(1.4)%	0%
State income taxes, net of federal benefit	**1.3%**	0.7%	1.3%
Research and development credit	**(1.1)%**	(1.1)%	(1.3)%
Excess tax benefits relating to stock-based compensation	**(2.2)%**	(2.2)%	(2.5)%
Interest, net	**1.0%**	1.0%	1.2%
Other reconciling items, net	**1.3%**	1.8%	(2.1)%
Effective rate	**16.5%**	10.2%	54.6%

The decrease from the federal statutory rate in fiscal year 2020 is primarily due to earnings taxed at lower rates in foreign jurisdictions resulting from producing and distributing our products and services through our foreign regional operations centers in Ireland and Puerto Rico, and tax benefits relating to stock-based compensation. The decrease from the federal statutory rate in fiscal year 2019 is primarily due to a $2.6 billion net income tax benefit related to intangible property transfers, and earnings taxed at lower rates in foreign jurisdictions resulting from producing and distributing our products and services through our foreign regional operations centers in Ireland, Singapore, and Puerto Rico. The increase from the federal statutory rate in fiscal year 2018 is primarily due to the net charge related to the enactment of the TCJA in the second quarter of fiscal year 2018, offset in part by earnings taxed at lower rates in foreign jurisdictions. In fiscal year 2020, our foreign regional operating centers in Ireland and Puerto Rico, which are taxed at rates lower than the U.S. rate, generated 86% of our foreign income before tax. In fiscal years 2019 and 2018, our foreign regional operating centers in Ireland, Singapore, and Puerto Rico, which are taxed at rates lower than the U.S. rate, generated 82% and 87% of our foreign income before tax, respectively. Other reconciling items, net consists primarily of tax credits and GILTI tax. In fiscal years 2020, 2019, and 2018, there were no individually significant other reconciling items.

The increase in our effective tax rate for fiscal year 2020 compared to fiscal year 2019 was primarily due to a $2.6 billion net income tax benefit in the fourth quarter of fiscal year 2019 related to intangible property transfers. The decrease in our effective tax rate for fiscal year 2019 compared to fiscal year 2018 was primarily due to the net charge related to the enactment of the TCJA in the second quarter of fiscal year 2018, and a $2.6 billion net income tax benefit in the fourth quarter of fiscal year 2019 related to intangible property transfers.

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

(In millions)

June 30,	**2020**	**2019**
Deferred Income Tax Assets		
Stock-based compensation expense	**$ 461**	$ 406
Accruals, reserves, and other expenses	**2,721**	2,287
Loss and credit carryforwards	**865**	3,518
Depreciation and amortization	**6,361**	7,046
Leasing liabilities	**3,025**	1,594
Unearned revenue	**1,553**	475
Other	**354**	367
Deferred income tax assets	**15,340**	15,693
Less valuation allowance	**(755)**	(3,214)
Deferred income tax assets, net of valuation allowance	**$ 14,585**	$ 12,479
Deferred Income Tax Liabilities		
Book/tax basis differences in investments and debt	**$ (2,642)**	$ (738)
Unearned revenue	**0**	(30)
Leasing assets	**(2,817)**	(1,510)
Deferred GILTI tax liabilities	**(2,581)**	(2,607)
Other	**(344)**	(291)
Deferred income tax liabilities	**$ (8,384)**	$ (5,176)
Net deferred income tax assets	**$ 6,201**	$ 7,303
Reported As		
Other long-term assets	**$ 6,405**	$ 7,536
Long-term deferred income tax liabilities	**(204)**	(233)
Net deferred income tax assets	**$ 6,201**	$ 7,303

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

As of June 30, 2020, we had federal, state, and foreign net operating loss carryforwards of $547 million, $975 million, and $2.0 billion, respectively. The federal and state net operating loss carryforwards will expire in various years from fiscal 2021 through 2040, if not utilized. The majority of our foreign net operating loss carryforwards do not expire. Certain acquired net operating loss carryforwards are subject to an annual limitation, but are expected to be realized with the exception of those which have a valuation allowance.

The valuation allowance disclosed in the table above relates to the foreign net operating loss carryforwards and other net deferred tax assets that may not be realized. In fiscal year 2020, we removed $2.0 billion of foreign net operating losses and corresponding valuation allowances as a result of the liquidation of a foreign subsidiary. There was no impact to our consolidated financial statements.

Income taxes paid, net of refunds, were $12.5 billion, $8.4 billion, and $5.5 billion in fiscal years 2020, 2019, and 2018, respectively.

Uncertain Tax Positions

Gross unrecognized tax benefits related to uncertain tax positions as of June 30, 2020, 2019, and 2018, were $13.8 billion, $13.1 billion, and $12.0 billion, respectively, which were primarily included in long-term income taxes in

our consolidated balance sheets. If recognized, the resulting tax benefit would affect our effective tax rates for fiscal years 2020, 2019, and 2018 by $12.1 billion, $12.0 billion, and $11.3 billion, respectively.

As of June 30, 2020, 2019, and 2018, we had accrued interest expense related to uncertain tax positions of $4.0 billion, $3.4 billion, and $3.0 billion, respectively, net of income tax benefits. The provision for income taxes for fiscal years 2020, 2019, and 2018 included interest expense related to uncertain tax positions of $579 million, $515 million, and $688 million, respectively, net of income tax benefits.

The aggregate changes in the gross unrecognized tax benefits related to uncertain tax positions were as follows:

(In millions)

Year Ended June 30,	2020	2019	2018
Beginning unrecognized tax benefits	**$ 13,146**	$ 11,961	$ 11,737
Decreases related to settlements	**(31)**	(316)	(193)
Increases for tax positions related to the current year	**647**	2,106	1,445
Increases for tax positions related to prior years	**366**	508	151
Decreases for tax positions related to prior years	**(331)**	(1,113)	(1,176)
Decreases due to lapsed statutes of limitations	**(5)**	0	(3)
Ending unrecognized tax benefits	**$ 13,792**	$ 13,146	$ 11,961

We settled a portion of the Internal Revenue Service ("IRS") audit for tax years 2004 to 2006 in fiscal year 2011. In February 2012, the IRS withdrew its 2011 Revenue Agents Report related to unresolved issues for tax years 2004 to 2006 and reopened the audit phase of the examination. We also settled a portion of the IRS audit for tax years 2007 to 2009 in fiscal year 2016, and a portion of the IRS audit for tax years 2010 to 2013 in fiscal year 2018. We remain under audit for tax years 2004 to 2013. In April 2020, the IRS commenced the audit for tax years 2014 to 2017.

As of June 30, 2020, the primary unresolved issues for the IRS audits relate to transfer pricing, which could have a material impact in our consolidated financial statements when the matters are resolved. We believe our allowances for income tax contingencies are adequate. We have not received a proposed assessment for the unresolved issues and do not expect a final resolution of these issues in the next 12 months. Based on the information currently available, we do not anticipate a significant increase or decrease to our tax contingencies for these issues within the next 12 months.

We are subject to income tax in many jurisdictions outside the U.S. Our operations in certain jurisdictions remain subject to examination for tax years 1996 to 2019, some of which are currently under audit by local tax authorities. The resolution of each of these audits is not expected to be material to our consolidated financial statements.

NOTE 13 — UNEARNED REVENUE

Unearned revenue by segment was as follows:

(In millions)

June 30,	2020	2019
Productivity and Business Processes	**$ 18,643**	$ 16,831
Intelligent Cloud	**16,620**	16,988
More Personal Computing	**3,917**	3,387
Total	**$ 39,180**	$ 37,206

Changes in unearned revenue were as follows:

(In millions)	
Year Ended June 30, 2020	
Balance, beginning of period	**$ 37,206**
Deferral of revenue	**78,922**
Recognition of unearned revenue	**(76,948)**
Balance, end of period	**$ 39,180**

Revenue allocated to remaining performance obligations, which includes unearned revenue and amounts that will be invoiced and recognized as revenue in future periods, was $111 billion as of June 30, 2020, of which $107 billion is related to the commercial portion of revenue. We expect to recognize approximately 50% of this revenue over the next 12 months and the remainder thereafter.

NOTE 14 — LEASES

We have operating and finance leases for datacenters, corporate offices, research and development facilities, retail stores, and certain equipment. Our leases have remaining lease terms of 1 year to 20 years, some of which include options to extend the leases for up to 5 years, and some of which include options to terminate the leases within 1 year.

The components of lease expense were as follows:

(In millions)			
Year Ended June 30,	**2020**	**2019**	**2018**
Operating lease cost	**$ 2,043**	$ 1,707	$ 1,585
Finance lease cost:			
Amortization of right-of-use assets	**$ 611**	$ 370	$ 243
Interest on lease liabilities	**336**	247	175
Total finance lease cost	**$ 947**	$ 617	$ 418

Supplemental cash flow information related to leases was as follows:

(In millions)			
Year Ended June 30,	**2020**	**2019**	**2018**
Cash paid for amounts included in the measurement of lease liabilities:			
Operating cash flows from operating leases	**$ 1,829**	$ 1,670	$ 1,522
Operating cash flows from finance leases	**336**	247	175
Financing cash flows from finance leases	**409**	221	144
Right-of-use assets obtained in exchange for lease obligations:			
Operating leases	**3,677**	2,303	1,571
Finance leases	**3,467**	2,532	1,933

Supplemental balance sheet information related to leases was as follows:

(In millions, except lease term and discount rate)

June 30,	2020	2019
Operating Leases		
Operating lease right-of-use assets	**$ 8,753**	$ 7,379
Other current liabilities	**$ 1,616**	$ 1,515
Operating lease liabilities	**7,671**	6,188
Total operating lease liabilities	**$ 9,287**	$ 7,703
Finance Leases		
Property and equipment, at cost	**$ 10,371**	$ 7,041
Accumulated depreciation	**(1,385)**	(774)
Property and equipment, net	**$ 8,986**	$ 6,267
Other current liabilities	**$ 540**	$ 317
Other long-term liabilities	**8,956**	6,257
Total finance lease liabilities	**$ 9,496**	$ 6,574
Weighted Average Remaining Lease Term		
Operating leases	**8 years**	7 years
Finance leases	**13 years**	13 years
Weighted Average Discount Rate		
Operating leases	**2.7%**	3.0%
Finance leases	**3.9%**	4.6%

Maturities of lease liabilities were as follows:

(In millions)

Year Ending June 30,	Operating Leases	Finance Leases
2021	**$ 1,807**	**$ 880**
2022	**1,652**	**894**
2023	**1,474**	**903**
2024	**1,262**	**916**
2025	**1,000**	**1,236**
Thereafter	**3,122**	**7,194**
Total lease payments	**10,317**	**12,023**
Less imputed interest	**(1,030)**	**(2,527)**
Total	**$ 9,287**	**$ 9,496**

As of June 30, 2020, we have additional operating and finance leases, primarily for datacenters, that have not yet commenced of $3.4 billion and $3.5 billion, respectively. These operating and finance leases will commence between fiscal year 2021 and fiscal year 2023 with lease terms of 1 year to 16 years.

During fiscal year 2020, we recorded an impairment charge of $161 million to operating lease right-of-use assets due to the closing of our Microsoft Store physical locations.

NOTE 15 — CONTINGENCIES

Patent and Intellectual Property Claims

There were 64 patent infringement cases pending against Microsoft as of June 30, 2020, none of which are material individually or in aggregate.

Antitrust, Unfair Competition, and Overcharge Class Actions

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

The trial of the British Columbia action commenced in May 2016. Following a mediation, the parties agreed to a global settlement of all three Canadian actions, and submitted the proposed settlement agreement to the courts in all three jurisdictions for approval. The final settlement has been approved by the courts in British Columbia, Ontario, and Quebec, and the claims administration process will commence once each court approves the form of notice to the class.

Other Antitrust Litigation and Claims

China State Administration for Industry and Commerce Investigation

In 2014, Microsoft was informed that China's State Agency for Market Regulation ("SAMR") (formerly State Administration for Industry and Commerce) had begun a formal investigation relating to China's Anti-Monopoly Law, and the SAMR conducted onsite inspections of Microsoft offices in Beijing, Shanghai, Guangzhou, and Chengdu. The SAMR has presented its preliminary views as to certain possible violations of China's Anti-Monopoly Law, and discussions are expected to continue.

Product-Related Litigation

U.S. Cell Phone Litigation

Microsoft Mobile Oy, a subsidiary of Microsoft, along with other handset manufacturers and network operators, is a defendant in 40 lawsuits filed in the Superior Court for the District of Columbia by individual plaintiffs who allege that radio emissions from cellular handsets caused their brain tumors and other adverse health effects. We assumed responsibility for these claims in our agreement to acquire Nokia's Devices and Services business and have been substituted for the Nokia defendants. Nine of these cases were filed in 2002 and are consolidated for certain pre-trial proceedings; the remaining cases are stayed. In a separate 2009 decision, the Court of Appeals for the District of Columbia held that adverse health effect claims arising from the use of cellular handsets that operate within the U.S. Federal Communications Commission radio frequency emission guidelines ("FCC Guidelines") are pre-empted by federal law. The plaintiffs allege that their handsets either operated outside the FCC Guidelines or were manufactured before the FCC Guidelines went into effect. The lawsuits also allege an industry-wide conspiracy to manipulate the science and testing around emission guidelines.

In 2013, the defendants in the consolidated cases moved to exclude the plaintiffs' expert evidence of general causation on the basis of flawed scientific methodologies. In 2014, the trial court granted in part and denied in part the defendants' motion to exclude the plaintiffs' general causation experts. The defendants filed an interlocutory appeal to the District of Columbia Court of Appeals challenging the standard for evaluating expert scientific evidence. In October 2016, the Court of Appeals issued its decision adopting the standard advocated by the defendants and remanding the cases to the trial court for further proceedings under that standard. The plaintiffs have filed supplemental expert evidence, portions of which the defendants have moved to strike. In August 2018, the trial court issued an order striking portions of the plaintiffs' expert reports. A hearing is expected to occur in the second quarter of fiscal year 2021.

Other Contingencies

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

As of June 30, 2020, we accrued aggregate legal liabilities of $306 million. While we intend to defend these matters vigorously, adverse outcomes that we estimate could reach approximately $500 million in aggregate beyond recorded amounts are reasonably possible. Were unfavorable final outcomes to occur, there exists the possibility of a material adverse impact in our consolidated financial statements for the period in which the effects become reasonably estimable.

NOTE 16 — STOCKHOLDERS' EQUITY

Shares Outstanding

Shares of common stock outstanding were as follows:

(In millions)			
Year Ended June 30,	**2020**	**2019**	**2018**
Balance, beginning of year	**7,643**	7,677	7,708
Issued	**54**	116	68
Repurchased	**(126)**	(150)	(99)
Balance, end of year	**7,571**	7,643	7,677

Share Repurchases

On September 20, 2016, our Board of Directors approved a share repurchase program authorizing up to $40.0 billion in share repurchases. This share repurchase program commenced in December 2016 and was completed in February 2020.

On September 18, 2019, our Board of Directors approved a share repurchase program authorizing up to $40.0 billion in share repurchases. This share repurchase program commenced in February 2020, following completion of the program approved on September 20, 2016, has no expiration date, and may be terminated at any time. As of June 30, 2020, $31.7 billion remained of this $40.0 billion share repurchase program.

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

(In millions)	Shares	Amount	Shares	Amount	Shares	Amount
Year Ended June 30,		**2020**		**2019**		**2018**
First Quarter	**29**	**$ 4,000**	24	$ 2,600	22	$ 1,600
Second Quarter	**32**	**4,600**	57	6,100	22	1,800
Third Quarter	**37**	**6,000**	36	3,899	34	3,100
Fourth Quarter	**28**	**5,088**	33	4,200	21	2,100
Total	**126**	**$ 19,688**	150	$ 16,799	99	$ 8,600

Shares repurchased during the fourth quarter of fiscal year 2020 were under the share repurchase program approved on September 18, 2019. Shares repurchased during the third quarter of fiscal year 2020 were under the share repurchase programs approved on both September 20, 2016 and September 18, 2019. All other shares repurchased were under the share repurchase program approved on September 20, 2016. The above table excludes shares repurchased to settle employee tax withholding related to the vesting of stock awards of $3.3 billion, $2.7 billion, and $2.1 billion for fiscal years 2020, 2019, and 2018, respectively. All share repurchases were made using cash resources.

Dividends

Our Board of Directors declared the following dividends:

Declaration Date	Record Date	Payment Date	Dividend Per Share	Amount
Fiscal Year 2020				(In millions)
September 18, 2019	**November 21, 2019**	**December 12, 2019**	**$ 0.51**	**$ 3,886**
December 4, 2019	**February 20, 2020**	**March 12, 2020**	**0.51**	**3,876**
March 9, 2020	**May 21, 2020**	**June 11, 2020**	**0.51**	**3,865**
June 17, 2020	**August 20, 2020**	**September 10, 2020**	**0.51**	**3,861**
Total			**$ 2.04**	**$ 15,488**
Fiscal Year 2019				
September 18, 2018	November 15, 2018	December 13, 2018	$ 0.46	$ 3,544
November 28, 2018	February 21, 2019	March 14, 2019	0.46	3,526
March 11, 2019	May 16, 2019	June 13, 2019	0.46	3,521
June 12, 2019	August 15, 2019	September 12, 2019	0.46	3,510
Total			$ 1.84	$ 14,101

The dividend declared on June 17, 2020 was included in other current liabilities as of June 30, 2020.

NOTE 17 — ACCUMULATED OTHER COMPREHENSIVE INCOME (LOSS)

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

(In millions)			
Year Ended June 30,	**2020**	**2019**	**2018**
Derivatives			
Balance, beginning of period	**$ 0**	$ 173	$ 134
Unrealized gains (losses), net of tax of **$(10)**, $2, and $11	**(38)**	160	218
Reclassification adjustments for gains included in revenue	**0**	(341)	(185)
Tax expense included in provision for income taxes	**0**	8	6
Amounts reclassified from accumulated other comprehensive income (loss)	**0**	(333)	(179)
Net change related to derivatives, net of tax of **$(10)**, $(6), and $5	**(38)**	(173)	39
Balance, end of period	**$ (38)**	$ 0	$ 173
Investments			
Balance, beginning of period	**$ 1,488**	$ (850)	$ 1,825
Unrealized gains (losses), net of tax of **$1,057**, $616, and $(427)	**3,987**	2,331	(1,146)
Reclassification adjustments for (gains) losses included in other income (expense), net	**4**	93	(2,309)
Tax expense (benefit) included in provision for income taxes	**(1)**	(19)	738
Amounts reclassified from accumulated other comprehensive income (loss)	**3**	74	(1,571)
Net change related to investments, net of tax of **$1,058**, $635, and $(1,165)	**3,990**	2,405	(2,717)
Cumulative effect of accounting changes	**0**	(67)	42
Balance, end of period	**$ 5,478**	$ 1,488	$ (850)
Translation Adjustments and Other			
Balance, beginning of period	**$ (1,828)**	$ (1,510)	$ (1,332)
Translation adjustments and other, net of tax effects of **$1**, $(1), and $0	**(426)**	(318)	(178)
Balance, end of period	**$ (2,254)**	$ (1,828)	$ (1,510)
Accumulated other comprehensive income (loss), end of period	**$ 3,186**	$ (340)	$ (2,187)

NOTE 18 — EMPLOYEE STOCK AND SAVINGS PLANS

We grant stock-based compensation to employees and directors. As of June 30, 2020, an aggregate of 283 million shares were authorized for future grant under our stock plans. Awards that expire or are canceled without delivery of shares generally become available for issuance under the plans. We issue new shares of Microsoft common stock to satisfy vesting of awards granted under our stock plans. We also have an ESPP for all eligible employees.

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

(In millions)			
Year Ended June 30,	**2020**	**2019**	**2018**
Stock-based compensation expense	**$ 5,289**	$ 4,652	$ 3,940
Income tax benefits related to stock-based compensation	**938**	816	823

Stock Plans

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

Executive Incentive Plan

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

Activity for All Stock Plans

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

Year ended June 30,	**2020**	**2019**	**2018**
Dividends per share (quarterly amounts)	**$ 0.46 - 0.51**	$ 0.42 - 0.46	$ 0.39 - 0.42
Interest rates	**0.1% - 2.2%**	1.8% - 3.1%	1.7% - 2.9%

During fiscal year 2020, the following activity occurred under our stock plans:

	Shares	**Weighted Average Grant-Date Fair Value**
	(In millions)	
Stock Awards		
Nonvested balance, beginning of year	**147**	**$ 78.49**
Granted [(a)]	**53**	**140.49**
Vested	**(65)**	**75.35**
Forfeited	**(9)**	**90.30**
Nonvested balance, end of year	**126**	**$ 105.23**

(a) *Includes 2 million, 2 million, and 3 million of PSUs granted at target and performance adjustments above target levels for fiscal years 2020, 2019, and 2018, respectively.*

As of June 30, 2020, there was approximately $10.2 billion of total unrecognized compensation costs related to stock awards. These costs are expected to be recognized over a weighted average period of three years. The weighted average grant-date fair value of stock awards granted was $140.49, $107.02, and $75.88 for fiscal years 2020, 2019, and 2018, respectively. The fair value of stock awards vested was $10.1 billion, $8.7 billion, and $6.6 billion, for fiscal years 2020, 2019, and 2018, respectively.

Employee Stock Purchase Plan

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

(Shares in millions)

Year Ended June 30,	2020	2019	2018
Shares purchased	**9**	11	13
Average price per share	**$ 142.22**	$ 104.85	$ 76.40

As of June 30, 2020, 96 million shares of our common stock were reserved for future issuance through the ESPP.

Savings Plan

We have savings plans in the U.S. that qualify under Section 401(k) of the Internal Revenue Code, and a number of savings plans in international locations. Eligible U.S. employees may contribute a portion of their salary into the savings plans, subject to certain limitations. We contribute fifty cents for each dollar a participant contributes into the plans, with a maximum employer contribution of 50% of the IRS contribution limit for the calendar year. Employer-funded retirement benefits for all plans were $1.0 billion, $877 million, and $807 million in fiscal years 2020, 2019, and 2018, respectively, and were expensed as contributed.

NOTE 19 — SEGMENT INFORMATION AND GEOGRAPHIC DATA

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

Our reportable segments are described below.

Productivity and Business Processes

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

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

Intelligent Cloud

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

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

More Personal Computing

Our More Personal Computing segment consists of products and services that put customers at the center of the experience with our technology. This segment primarily comprises:

- Windows, including Windows OEM licensing and other non-volume licensing of the Windows operating system; Windows Commercial, comprising volume licensing of the Windows operating system, Windows cloud services, and other Windows commercial offerings; patent licensing; Windows Internet of Things; and MSN advertising.
- Devices, including Surface and PC accessories.
- Gaming, including Xbox hardware and Xbox content and services, comprising Xbox Live (transactions, subscriptions, cloud services, and advertising), video games, and third-party video game royalties.
- Search.

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

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

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

(In millions)

Year Ended June 30,	2020	2019	2018
Revenue			
Productivity and Business Processes	**$ 46,398**	$ 41,160	$ 35,865
Intelligent Cloud	**48,366**	38,985	32,219
More Personal Computing	**48,251**	45,698	42,276
Total	**$ 143,015**	$ 125,843	$ 110,360
Operating Income			
Productivity and Business Processes	**$ 18,724**	$ 16,219	$ 12,924
Intelligent Cloud	**18,324**	13,920	11,524
More Personal Computing	**15,911**	12,820	10,610
Total	**$ 52,959**	$ 42,959	$ 35,058

No sales to an individual customer or country other than the United States accounted for more than 10% of revenue for fiscal years 2020, 2019, or 2018. Revenue, classified by the major geographic areas in which our customers were located, was as follows:

(In millions)

Year Ended June 30,	2020	2019	2018
United States [(a)]	**$ 73,160**	$ 64,199	$ 55,926
Other countries	**69,855**	61,644	54,434
Total	**$ 143,015**	$ 125,843	$ 110,360

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

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

(In millions)

Year Ended June 30,	2020	2019	2018
Server products and cloud services	**$ 41,379**	$ 32,622	$ 26,129
Office products and cloud services	**35,316**	31,769	28,316
Windows	**22,294**	20,395	19,518
Gaming	**11,575**	11,386	10,353
LinkedIn	**8,077**	6,754	5,259
Search advertising	**7,740**	7,628	7,012
Devices	**6,457**	6,095	5,134
Enterprise Services	**6,409**	6,124	5,846
Other	**3,768**	3,070	2,793
Total	**$ 143,015**	$ 125,843	$ 110,360

Our commercial cloud revenue, which includes Office 365 Commercial, Azure, the commercial portion of LinkedIn, Dynamics 365, and other commercial cloud properties, was $51.7 billion, $38.1 billion and $26.6 billion in fiscal years 2020, 2019, and 2018, respectively. These amounts are primarily included in Office products and cloud services, Server products and cloud services, and LinkedIn in the table above.

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

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

(In millions)

June 30,	2020	2019	2018
United States	**$ 60,789**	$ 55,252	$ 44,501
Ireland	**12,734**	12,958	12,843
Other countries	**29,770**	25,422	22,538
Total	**$ 103,293**	$ 93,632	$ 79,882

NOTE 20 — QUARTERLY INFORMATION (UNAUDITED)

(In millions, except per share amounts)

Quarter Ended	September 30	December 31	March 31	June 30	Total
Fiscal Year 2020					
Revenue	**$ 33,055**	**$ 36,906**	**$ 35,021**	**$ 38,033**	**$ 143,015**
Gross margin	**22,649**	**24,548**	**24,046**	**25,694**	**96,937**
Operating income	**12,686**	**13,891**	**12,975**	**13,407**	**52,959**
Net income	**10,678**	**11,649**	**10,752**	**11,202**	**44,281**
Basic earnings per share	**1.40**	**1.53**	**1.41**	**1.48**	**5.82**
Diluted earnings per share	**1.38**	**1.51**	**1.40**	**1.46**	**5.76**
Fiscal Year 2019					
Revenue	29,084	32,471	30,571	33,717	125,843
Gross margin	19,179	20,048	20,401	23,305	82,933
Operating income	9,955	10,258	10,341	12,405	42,959
Net income [(a)]	8,824	8,420	8,809	13,187	39,240
Basic earnings per share	1.15	1.09	1.15	1.72	5.11
Diluted earnings per share [(b)]	1.14	1.08	1.14	1.71	5.06

(a) *Reflects the $157 million net charge related to the enactment of the TCJA for the second quarter and the $2.6 billion net income tax benefit related to the intangible property transfers for the fourth quarter, which together increased net income by $2.4 billion for fiscal year 2019. See Note 12 – Income Taxes for further information.*

(b) *Reflects the net charge related to the enactment of the TCJA and the net income tax benefit related to the intangible property transfers, which decreased (increased) diluted EPS $0.02 for the second quarter, $(0.34) for the fourth quarter, and $(0.31) for fiscal year 2019.*

REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM

To the Stockholders and the Board of Directors of Microsoft Corporation

Opinion on the Financial Statements

We have audited the accompanying consolidated balance sheets of Microsoft Corporation and subsidiaries (the "Company") as of June 30, 2020 and 2019, the related consolidated statements of income, comprehensive income, cash flows, and stockholders' equity, for each of the three years in the period ended June 30, 2020, and the related notes (collectively referred to as the "financial statements"). In our opinion, the financial statements present fairly, in all material respects, the financial position of the Company as of June 30, 2020 and 2019, and the results of its operations and its cash flows for each of the three years in the period ended June 30, 2020, in conformity with accounting principles generally accepted in the United States of America.

We have also audited, in accordance with the standards of the Public Company Accounting Oversight Board (United States) (PCAOB), the Company's internal control over financial reporting as of June 30, 2020, based on criteria established in *Internal Control — Integrated Framework (2013)* issued by the Committee of Sponsoring Organizations of the Treadway Commission and our report dated July 30, 2020, expressed an unqualified opinion on the Company's internal control over financial reporting.

Basis for Opinion

These financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on the Company's financial statements based on our audits. We are a public accounting firm registered with the PCAOB and are required to be independent with respect to the Company in accordance with the U.S. federal securities laws and the applicable rules and regulations of the Securities and Exchange Commission and the PCAOB.

We conducted our audits in accordance with the standards of the PCAOB. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement, whether due to error or fraud. Our audits included performing procedures to assess the risks of material misstatement of the financial statements, whether due to error or fraud, and performing procedures that respond to those risks. Such procedures included examining, on a test basis, evidence regarding the amounts and disclosures in the financial statements. Our audits also included evaluating the accounting principles used and significant estimates made by management, as well as evaluating the overall presentation of the financial statements. We believe that our audits provide a reasonable basis for our opinion.

Critical Audit Matters

The critical audit matters communicated below are matters arising from the current-period audit of the financial statements that were communicated or required to be communicated to the audit committee and that (1) relate to accounts or disclosures that are material to the financial statements and (2) involved our especially challenging, subjective, or complex judgments. The communication of critical audit matters does not alter in any way our opinion on the financial statements, taken as a whole, and we are not, by communicating the critical audit matters below, providing separate opinions on the critical audit matters or on the accounts or disclosures to which they relate.

Revenue Recognition — Refer to Note 1 to the financial statements

Critical Audit Matter Description

The Company recognizes revenue upon transfer of control of promised products or services to customers in an amount that reflects the consideration the Company expects to receive in exchange for those products or services. The Company offers customers the ability to acquire multiple licenses of software products and services, including cloud-based services, in its customer agreements through its volume licensing programs.

Significant judgment is exercised by the Company in determining revenue recognition for these customer agreements, and includes the following:

- Determination of whether products and services are considered distinct performance obligations that should be accounted for separately versus together, such as software licenses and related services that are sold with cloud-based services.
- The pattern of delivery (i.e., timing of when revenue is recognized) for each distinct performance obligation.
- Identification and treatment of contract terms that may impact the timing and amount of revenue recognized (e.g., variable consideration, optional purchases, and free services).
- Determination of stand-alone selling prices for each distinct performance obligation and for products and services that are not sold separately.

Given these factors and due to the volume of transactions, the related audit effort in evaluating management's judgments in determining revenue recognition for these customer agreements was extensive and required a high degree of auditor judgment.

How the Critical Audit Matter Was Addressed in the Audit

Our principal audit procedures related to the Company's revenue recognition for these customer agreements included the following:

- We tested the effectiveness of controls related to the identification of distinct performance obligations, the determination of the timing of revenue recognition, and the estimation of variable consideration.
- We evaluated management's significant accounting policies related to these customer agreements for reasonableness.
- We selected a sample of customer agreements and performed the following procedures:
- Obtained and read contract source documents for each selection, including master agreements, and other documents that were part of the agreement.
- Tested management's identification and treatment of contract terms.
- Assessed the terms in the customer agreement and evaluated the appropriateness of management's application of their accounting policies, along with their use of estimates, in the determination of revenue recognition conclusions.
- We evaluated the reasonableness of management's estimate of stand-alone selling prices for products and services that are not sold separately.
- We tested the mathematical accuracy of management's calculations of revenue and the associated timing of revenue recognized in the financial statements.

Income Taxes — Uncertain Tax Positions — Refer to Note 12 to the financial statements

Critical Audit Matter Description

The Company's long-term income taxes liability includes uncertain tax positions related to transfer pricing issues that remain unresolved with the Internal Revenue Service ("IRS"). The Company remains under IRS audit, or subject to IRS audit, for tax years subsequent to 2003. While the Company has settled a portion of the IRS audits, resolution of the remaining matters could have a material impact on the Company's financial statements.

Conclusions on recognizing and measuring uncertain tax positions involve significant estimates and management judgment and include complex considerations of the Internal Revenue Code, related regulations, tax case laws, and prior-year audit settlements. Given the complexity and the subjective nature of the transfer pricing issues that remain unresolved with the IRS, evaluating management's estimates relating to their determination of uncertain tax positions required extensive audit effort and a high degree of auditor judgment, including involvement of our tax specialists.

How the Critical Audit Matter Was Addressed in the Audit

Our principal audit procedures to evaluate management's estimates of uncertain tax positions related to unresolved transfer pricing issues included the following:

- We evaluated the appropriateness and consistency of management's methods and assumptions used in the identification, recognition, measurement, and disclosure of uncertain tax positions, which included testing the effectiveness of the related internal controls.
- We read and evaluated management's documentation, including relevant accounting policies and information obtained by management from outside tax specialists, that detailed the basis of the uncertain tax positions.
- We tested the reasonableness of management's judgments regarding the future resolution of the uncertain tax positions, including an evaluation of the technical merits of the uncertain tax positions.
- For those uncertain tax positions that had not been effectively settled, we evaluated whether management had appropriately considered new information that could significantly change the recognition, measurement or disclosure of the uncertain tax positions.
- We evaluated the reasonableness of management's estimates by considering how tax law, including statutes, regulations and case law, impacted management's judgments.

/s/ DELOITTE & TOUCHE LLP

Seattle, Washington
July 30, 2020

We have served as the Company's auditor since 1983.

CHANGES IN AND DISAGREEMENTS WITH ACCOUNTANTS ON ACCOUNTING AND FINANCIAL DISCLOSURE

Not applicable.

CONTROLS AND PROCEDURES

Under the supervision and with the participation of our management, including the Chief Executive Officer and Chief Financial Officer, we have evaluated the effectiveness of our disclosure controls and procedures as required by Exchange Act Rule 13a-15(b) as of the end of the period covered by this report. Based on that evaluation, the Chief Executive Officer and Chief Financial Officer have concluded that these disclosure controls and procedures are effective.

REPORT OF MANAGEMENT ON INTERNAL CONTROL OVER FINANCIAL REPORTING

Our management is responsible for establishing and maintaining adequate internal control over financial reporting for the Company. Internal control over financial reporting is a process to provide reasonable assurance regarding the reliability of our financial reporting for external purposes in accordance with accounting principles generally accepted in the United States of America. Internal control over financial reporting includes maintaining records that in reasonable detail accurately and fairly reflect our transactions; providing reasonable assurance that transactions are recorded as necessary for preparation of our consolidated financial statements; providing reasonable assurance that receipts and expenditures of company assets are made in accordance with management authorization; and providing reasonable assurance that unauthorized acquisition, use, or disposition of company assets that could have a material effect on our consolidated financial statements would be prevented or detected on a timely basis. Because of its inherent limitations, internal control over financial reporting is not intended to provide absolute assurance that a misstatement of our consolidated financial statements would be prevented or detected.

Management conducted an evaluation of the effectiveness of our internal control over financial reporting based on the framework in *Internal Control – Integrated Framework (2013)* issued by the Committee of Sponsoring Organizations of the Treadway Commission. Based on this evaluation, management concluded that the Company's internal control over financial reporting was effective as of June 30, 2020. There were no changes in our internal control over financial reporting during the quarter ended June 30, 2020 that have materially affected, or are reasonably likely to materially affect, our internal control over financial reporting. Deloitte & Touche LLP has audited our internal control over financial reporting as of June 30, 2020; their report follows.

REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM

To the Stockholders and the Board of Directors of Microsoft Corporation

Opinion on Internal Control over Financial Reporting

We have audited the internal control over financial reporting of Microsoft Corporation and subsidiaries (the "Company") as of June 30, 2020, based on criteria established in *Internal Control – Integrated Framework (2013)* issued by the Committee of Sponsoring Organizations of the Treadway Commission (COSO). In our opinion, the Company maintained, in all material respects, effective internal control over financial reporting as of June 30, 2020, based on the criteria established in *Internal Control – Integrated Framework (2013)* issued by COSO.

We have also audited, in accordance with the standards of the Public Company Accounting Oversight Board (United States) (PCAOB), the consolidated financial statements and the related notes (collectively referred to as the "financial statements") as of and for the year ended June 30, 2020, of the Company and our report dated July 30, 2020, expressed an unqualified opinion on those financial statements.

Basis for Opinion

The Company's management is responsible for maintaining effective internal control over financial reporting and for its assessment of the effectiveness of internal control over financial reporting, included in the accompanying Report of Management on Internal Control over Financial Reporting. Our responsibility is to express an opinion on the Company's internal control over financial reporting based on our audit. We are a public accounting firm registered with the PCAOB and are required to be independent with respect to the Company in accordance with the U.S. federal securities laws and the applicable rules and regulations of the Securities and Exchange Commission and the PCAOB.

We conducted our audit in accordance with the standards of the PCAOB. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether effective internal control over financial reporting was maintained in all material respects. Our audit included obtaining an understanding of internal control over financial reporting, assessing the risk that a material weakness exists, testing and evaluating the design and operating effectiveness of internal control based on the assessed risk, and performing such other procedures as we considered necessary in the circumstances. We believe that our audit provides a reasonable basis for our opinion.

Definition and Limitations of Internal Control over Financial Reporting

A company's internal control over financial reporting is a process designed to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles. A company's internal control over financial reporting includes those policies and procedures that (1) pertain to the maintenance of records that, in reasonable detail, accurately and fairly reflect the transactions and dispositions of the assets of the company; (2) provide reasonable assurance that transactions are recorded as necessary to permit preparation of financial statements in accordance with generally accepted accounting principles, and that receipts and expenditures of the company are being made only in accordance with authorizations of management and directors of the company; and (3) provide reasonable assurance regarding prevention or timely detection of unauthorized acquisition, use, or disposition of the company's assets that could have a material effect on the financial statements.

Because of its inherent limitations, internal control over financial reporting may not prevent or detect misstatements. Also, projections of any evaluation of effectiveness to future periods are subject to the risk that controls may become inadequate because of changes in conditions, or that the degree of compliance with the policies or procedures may deteriorate.

/s/ DELOITTE & TOUCHE LLP

Seattle, Washington
July 30, 2020

DIRECTORS AND EXECUTIVE OFFICERS OF MICROSOFT CORPORATION

DIRECTORS

John W. Thompson [3,4]
Independent Board Chair, Microsoft Corporation

Reid G. Hoffman
Partner, Greylock Partners

Hugh F. Johnston [1]
Vice Chairman, Executive Vice President, and Chief Financial Officer, PepsiCo

Teri L. List-Stoll [1,3]
Former Executive Vice President and Chief Financial Officer, The Gap, Inc.

Satya Nadella
Chief Executive Officer, Microsoft Corporation

Sandra E. Peterson [2,3]
Operating Partner, Clayton, Dubilier & Rice

Penny S. Pritzker [4]
Founder and Chairman, PSP Partners

Charles W. Scharf [2,3]
President and Chief Executive Officer, Wells Fargo & Company

Arne M. Sorenson [1]
President and Chief Executive Officer, Marriott International, Inc.

John W. Stanton [1,4]
Founder and Chairman, Trilogy Partnerships

Emma N. Walmsley [2,4]
Chief Executive Officer, GlaxoSmithKline

Padmasree Warrior [2]
Founder, Chief Executive Officer and President, Fable Group Inc.

Board Committees
1. Audit Committee
2. Compensation Committee
3. Governance and Nominating Committee
4. Regulatory and Public Policy Committee

EXECUTIVE OFFICERS

Satya Nadella
Chief Executive Officer

Christopher C. Capossela
Executive Vice President, Marketing and Consumer Business, and Chief Marketing Officer

Jean-Philippe Courtois
Executive Vice President and President, Microsoft Global Sales, Marketing and Operations

Kathleen T. Hogan
Executive Vice President, Human Resources

Amy E. Hood
Executive Vice President, Chief Financial Officer

Bradford L. Smith
President and Chief Legal Officer

INVESTOR RELATIONS

Investor Relations

You can contact Microsoft Investor Relations at any time to order financial documents such as annual reports and Form 10-Ks free of charge.

Call us toll-free at (800) 285-7772 or outside the United States, call (425) 706-4400. We can be contacted between the hours of 9:00 a.m. to 5:00 p.m. Pacific Time to answer investment oriented questions about Microsoft.

For access to additional financial information, visit the Investor Relations website online at:
www.microsoft.com/investor

Our e-mail is msft@microsoft.com

Our mailing address is:
Investor Relations
Microsoft Corporation
One Microsoft Way
Redmond, Washington 98052-6399

Attending the Annual Meeting

The 2020 Annual Shareholders Meeting will be held as a virtual-only meeting. Any shareholder can join the Annual Meeting, while shareholders of record as of October 8, 2020 will be able to vote and submit questions during the meeting.

Date: Wednesday, December 2, 2020
Time: 8:00 a.m. Pacific Time
Virtual Shareholder Meeting:
www.virtualshareholdermeeting.com/MSFT20

Submit Your Question

We invite you to submit any questions via the proxy voting site at www.proxyvote.com. We will include as many of your questions as possible during the Q&A session of the meeting and will provide answers to questions on the Microsoft Investor Relations website under the Annual Meeting page.

Registered Shareholder Services

Computershare, our transfer agent, can help you with a variety of shareholder related services including:

- Change of address
- Lost stock certificates
- Transfer of stock to another person
- Additional administrative services

Computershare also administers a direct stock purchase plan and a dividend reinvestment program for the company.

Contact Computershare directly to find out more about these services and programs at 800-285-7772, option 1, or visit online at:
https://www.computershare.com/Microsoft

You can e-mail the transfer agent at:
web.queries@computershare.com

You can also send mail to the transfer agent at:
Computershare
P.O. Box 505000
Louisville, KY 40233-5000

Shareholders can sign up for electronic alerts to access the annual report and proxy statement online. The service gets you the information you need faster and also gives you the power and convenience of online proxy voting. To sign up for this free service, visit the Annual Report site on the Investor Relations website at:
http://www.microsoft.com/investor/AnnualReports/default.aspx

Environmental, Social, Governance ("ESG")/Corporate Social Responsibility ("CSR")

Many of our shareholders are increasingly focused on the importance of the effective engagement and action on ESG topics. To meet the expectations of our stakeholders and to and maintain their trust, we are committed to conducting our business in ways that are principled, transparent, and accountable and we have made a broad range of environmental and social commitments. From our CEO and Senior Leadership Team and throughout our organization, people at Microsoft are working to conduct our business in principled ways that make a significant positive impact on important global issues. Microsoft's Board of Directors provides insight, feedback, and oversight across a broad range of environmental and social matters. In particular, among the responsibilities of the Board's Regulatory and Public Policy Committee is to review and provide guidance to the Board and management about the Company's policies and programs that relate to CSR.

For more about Microsoft's CSR commitments and performance, please visit:
www.microsoft.com/transparency


FSC
www.fsc.org
MIX
Paper from
responsible sources
FSC® C132107