APPLE INC
Form 10-Q
April 27, 2016
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UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

FORM 10-Q

(Mark One)

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

For the quarterly period ended March 26, 2016

or

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

For the transition period from ______ to ______.

Commission File Number: **001-36743**

Apple Inc.

(Exact name of Registrant as specified in its charter)

California	**94-2404110**
(State or other jurisdiction of incorporation or organization)	(I.R.S. Employer Identification No.)
1 Infinite Loop Cupertino, California	**95014**
(Address of principal executive offices)	(Zip Code)

(408) 996-1010

(Registrant s telephone number, including area code)

Indicate by check mark whether the Registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the Registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days.

Yes x No ¨

Indicate by check mark whether the Registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (§232.405 of this chapter) during the preceding 12 months (or for such shorter period that the Registrant was required to submit and post such files).

Yes x No ¨

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

Large accelerated filer x	Accelerated filer ¨
Non-accelerated filer ¨ (Do not check if a smaller reporting company)	Smaller reporting company ¨

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

Yes ¨ No x

5,477,425,000 shares of common stock, par value $0.00001 per share, issued and outstanding as of April 8, 2016

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Apple Inc.

Form 10-Q

For the Fiscal Quarter Ended March 26, 2016

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PART I FINANCIAL INFORMATION

Item 1. Financial Statements

Apple Inc.

CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS (Unaudited)

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

	Three Months Ended		Six Months Ended	
	March 26, 2016	March 28, 2015	March 26, 2016	March 28, 2015
Net sales	$ 50,557	$ 58,010	$ 126,429	$ 132,609
Cost of sales	30,636	34,354	76,085	79,212
Gross margin	19,921	23,656	50,344	53,397
Operating expenses:				
Research and development	2,511	1,918	4,915	3,813
Selling, general and administrative	3,423	3,460	7,271	7,060
Total operating expenses	5,934	5,378	12,186	10,873
Operating income	13,987	18,278	38,158	42,524
Other income/(expense), net	155	286	557	456
Income before provision for income taxes	14,142	18,564	38,715	42,980
Provision for income taxes	3,626	4,995	9,838	11,387
Net income	$ 10,516	$ 13,569	$ 28,877	$ 31,593
Earnings per share:				
Basic	$ 1.91	$ 2.34	$ 5.22	$ 5.43
Diluted	$ 1.90	$ 2.33	$ 5.19	$ 5.39
Shares used in computing earnings per share:				
Basic	5,514,381	5,793,799	5,536,656	5,818,441
Diluted	5,540,886	5,834,858	5,567,506	5,858,330

Cash dividends declared per share	$ 0.52	$ 0.47	$ 1.04	$ 0.94

See accompanying Notes to Condensed Consolidated Financial Statements.

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Apple Inc.

CONDENSED CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME (Unaudited)

(In millions)

	Three Months Ended		Six Months Ended	
	March 26, 2016	March 28, 2015	March 26, 2016	March 28, 2015
Net income	$ 10,516	$ 13,569	$ 28,877	$ 31,593
Other comprehensive income/(loss):				
Change in foreign currency translation, net of tax	120	(180)	18	(246)
Change in unrealized gains/losses on derivative instruments:				
Change in fair value of derivatives, net of tax	(178)	1,037	109	3,019
Adjustment for net (gains)/losses realized and included in net income, net of tax	(528)	(739)	(973)	(1,304)
Total change in unrealized gains/losses on derivative instruments, net of tax	(706)	298	(864)	1,715
Change in unrealized gains/losses on marketable securities:				
Change in fair value of marketable securities, net of tax	969	593	47	137
Adjustment for net (gains)/losses realized and included in net income, net of tax	49	36	96	22
Total change in unrealized gains/losses on marketable securities, net of tax	1,018	629	143	159
Total other comprehensive income/(loss)	432	747	(703)	1,628
Total comprehensive income	$ 10,948	$ 14,316	$ 28,174	$ 33,221

See accompanying Notes to Condensed Consolidated Financial Statements.

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Apple Inc.

CONDENSED CONSOLIDATED BALANCE SHEETS (Unaudited)

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

	March 26, 2016	September 26, 2015
ASSETS:		
Current assets:		
Cash and cash equivalents	$ 21,514	$ 21,120
Short-term marketable securities	33,769	20,481
Accounts receivable, less allowances of $60 and $63, respectively	12,229	16,849
Inventories	2,281	2,349
Vendor non-trade receivables	7,595	13,494
Other current assets	10,204	15,085
Total current assets	87,592	89,378
Long-term marketable securities	177,645	164,065
Property, plant and equipment, net	23,203	22,471
Goodwill	5,249	5,116
Acquired intangible assets, net	3,843	3,893
Other non-current assets	7,745	5,556
Total assets	$ 305,277	$ 290,479
LIABILITIES AND SHAREHOLDERS EQUITY:		
Current liabilities:		
Accounts payable	$ 25,098	$ 35,490
Accrued expenses	23,208	25,181
Deferred revenue	9,461	8,940
Commercial paper	7,998	8,499
Current portion of long-term debt	2,500	2,500
Total current liabilities	68,265	80,610
Deferred revenue, non-current	3,322	3,624
Long-term debt	69,374	53,463
Other non-current liabilities	33,859	33,427
Total liabilities	174,820	171,124
Commitments and contingencies		

Shareholders equity:				
Common stock and additional paid-in capital, $0.00001 par value: 12,600,000 shares authorized; 5,478,446 and 5,578,753 shares issued and outstanding, respectively		29,484		27,416
Retained earnings		102,021		92,284
Accumulated other comprehensive income/(loss)		(1,048)		(345)
Total shareholders equity		130,457		119,355
Total liabilities and shareholders equity	$	305,277	$	290,479

See accompanying Notes to Condensed Consolidated Financial Statements.

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Apple Inc.

CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS (Unaudited)

(In millions)

	Six Months Ended	
	March 26, 2016	**March 28, 2015**
Cash and cash equivalents, beginning of the period	$ 21,120	$ 13,844
Operating activities:		
Net income	28,877	31,593
Adjustments to reconcile net income to cash generated by operating activities:		
Depreciation and amortization	5,431	5,054
Share-based compensation expense	2,126	1,815
Deferred income tax expense	3,092	1,879
Changes in operating assets and liabilities:		
Accounts receivable, net	4,620	6,555
Inventories	68	(285)
Vendor non-trade receivables	5,899	2,500
Other current and non-current assets	300	2,448
Accounts payable	(9,475)	(5,428)
Deferred revenue	219	993
Other current and non-current liabilities	(2,093)	5,679
Cash generated by operating activities	39,064	52,803
Investing activities:		
Purchases of marketable securities	(86,242)	(92,523)
Proceeds from maturities of marketable securities	9,148	5,871
Proceeds from sales of marketable securities	50,051	48,924
Payments made in connection with business acquisitions, net	(140)	(115)
Payments for acquisition of property, plant and equipment	(5,948)	(5,586)
Payments for acquisition of intangible assets	(657)	(155)
Other	(322)	88
Cash used in investing activities	(34,110)	(43,496)
Financing activities:		
Proceeds from issuance of common stock	247	309
Excess tax benefits from equity awards	264	357
Payments for taxes related to net share settlement of equity awards	(751)	(608)

Payments for dividends and dividend equivalents		(5,871)		(5,544)
Repurchase of common stock		(13,530)		(12,000)
Proceeds from issuance of term debt, net		15,584		11,332
Change in commercial paper, net		(503)		(2,508)
Cash used in financing activities		(4,560)		(8,662)
Increase in cash and cash equivalents		394		645
Cash and cash equivalents, end of the period	$	21,514	$	14,489
Supplemental cash flow disclosure:				
Cash paid for income taxes, net	$	6,630	$	7,058
Cash paid for interest	$	565	$	220

See accompanying Notes to Condensed Consolidated Financial Statements.

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Notes to Condensed Consolidated Financial Statements (Unaudited)

Note 1 Summary of Significant Accounting Policies

Apple Inc. and its wholly-owned subsidiaries (collectively Apple or the Company) designs, manufactures and markets mobile communication and media devices, personal computers and portable digital music players, and sells a variety of related software, services, accessories, networking solutions and third-party digital content and applications. The Company sells its products worldwide through its retail stores, online stores and direct sales force, as well as through third-party cellular network carriers, wholesalers, retailers and value-added resellers. In addition, the Company sells a variety of third-party Apple-compatible products, including application software and various accessories through its online and retail stores. The Company sells to consumers, small and mid-sized businesses and education, enterprise and government customers.

Basis of Presentation and Preparation

The accompanying condensed consolidated financial statements include the accounts of the Company. Intercompany accounts and transactions have been eliminated. In the opinion of the Company s management, the condensed consolidated financial statements reflect all adjustments, which are normal and recurring in nature, necessary for fair financial statement presentation. The preparation of these condensed consolidated financial statements in conformity with U.S. generally accepted accounting principles (GAAP) requires management to make estimates and assumptions that affect the amounts reported in these condensed consolidated financial statements and accompanying notes. Actual results could differ materially from those estimates. Certain prior period amounts in the condensed consolidated financial statements have been reclassified to conform to the current period s presentation.

These condensed consolidated financial statements and accompanying notes should be read in conjunction with the Company s annual consolidated financial statements and the notes thereto included in its Annual Report on Form 10-K for the fiscal year ended September 26, 2015 (the 2015 Form 10-K). The Company s fiscal year is the 52 or 53-week period that ends on the last Saturday of September. An additional week is included in the first fiscal quarter approximately every six years to realign fiscal quarters with calendar quarters. The Company s fiscal years 2016 and 2015 each include 52 weeks. Unless otherwise stated, references to particular years, quarters or months refer to the Company s fiscal years ended in September and the associated quarters or months of those fiscal years.

During the first quarter of 2016, the Company adopted an accounting standard that simplified the presentation of deferred taxes by requiring deferred tax assets and liabilities be classified as noncurrent in a classified statement of financial position. The Company has adopted this accounting standard prospectively; accordingly, the prior period amounts in the Company s Condensed Consolidated Balance Sheets within this Quarterly Report on Form 10-Q were not adjusted to conform to the new accounting standard. The adoption of this accounting standard was not material to the Company s condensed consolidated financial statements.

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Earnings Per Share

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

The following table shows the computation of basic and diluted earnings per share for the three- and six-month periods ended March 26, 2016 and March 28, 2015 (net income in millions and shares in thousands):

	Three Months Ended		Six Months Ended	
	March 26, 2016	March 28, 2015	March 26, 2016	March 28, 2015
Numerator:				
Net income	$ 10,516	$ 13,569	$ 28,877	$ 31,593
Denominator:				
Weighted-average shares outstanding	5,514,381	5,793,799	5,536,656	5,818,441
Effect of dilutive securities	26,505	41,059	30,850	39,889
Weighted-average diluted shares	5,540,886	5,834,858	5,567,506	5,858,330
Basic earnings per share	$ 1.91	$ 2.34	$ 5.22	$ 5.43
Diluted earnings per share	$ 1.90	$ 2.33	$ 5.19	$ 5.39

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

Note 2 Financial Instruments

Cash, Cash Equivalents and Marketable Securities

The following tables show the Company s cash and available-for-sale securities adjusted cost, gross unrealized gains, gross unrealized losses and fair value by significant investment category recorded as cash and cash equivalents or short- or long-term marketable securities as of March 26, 2016 and September 26, 2015 (in millions):

March 26, 2016

	Adjusted Cost	Unrealized Gains	Unrealized Losses	Fair Value	Cash and Cash Equivalents	Short-Term Marketable Securities	Long Mark Secu
	$ 10,199	$ 0	$ 0	$ 10,199	$ 10,199	$ 0	$
1):							
narket funds	2,798	0	0	2,798	2,798	0	
unds	1,772	0	(203)	1,569	0	1,569	
	4,570	0	(203)	4,367	2,798	1,569	
2):							
asury securities	47,883	207	(24)	48,066	3,753	10,614	
ncy securities	6,641	12	(2)	6,651	465	2,703	
. government securities	6,873	91	(121)	6,843	0	696	
tes of deposit and time deposits	4,169	0	0	4,169	1,529	660	
cial paper	4,500	0	0	4,500	2,681	1,819	
e securities	129,394	543	(1,074)	128,863	89	15,553	1
al securities	952	6	0	958	0	72	
e- and asset-backed securities	18,268	86	(42)	18,312	0	83	
	218,680	945	(1,263)	218,362	8,517	32,200	1
	$ 233,449	$ 945	$ (1,466)	$ 232,928	$ 21,514	$ 33,769	$ 1

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	September 26, 2015						
	Adjusted Cost	Unrealized Gains	Unrealized Losses	Fair Value	Cash and Cash Equivalents	Short-Term Marketable Securities	Long Mark Secu
	$ 11,389	$ 0	$ 0	$ 11,389	$ 11,389	$ 0	$
1):							
narket funds	1,798	0	0	1,798	1,798	0	
unds	1,772	0	(144)	1,628	0	1,628	
	3,570	0	(144)	3,426	1,798	1,628	
2):							
asury securities	34,902	181	(1)	35,082	0	3,498	
ncy securities	5,864	14	0	5,878	841	767	
. government securities	6,356	45	(167)	6,234	43	135	
tes of deposit and time deposits	4,347	0	0	4,347	2,065	1,405	
cial paper	6,016	0	0	6,016	4,981	1,035	
e securities	116,908	242	(985)	116,165	3	11,948	1
al securities	947	5	0	952	0	48	
e- and asset-backed securities	16,121	87	(31)	16,177	0	17	
	191,461	574	(1,184)	190,851	7,933	18,853	1
	$ 206,420	$ 574	$ (1,328)	$ 205,666	$ 21,120	$ 20,481	$ 1

(1) The fair value of Level 1 securities is estimated based on quoted prices in active markets for identical assets or liabilities.

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

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

The Company considers the declines in market value of its marketable securities investment portfolio to be temporary in nature. The Company typically invests in highly-rated securities, and its investment policy generally limits the amount of credit exposure to any one issuer. The policy generally requires investments to be investment grade, with the primary objective of minimizing the potential risk of principal loss. Fair values were determined for each individual security in the investment portfolio. When evaluating an investment for other-than-temporary impairment the Company reviews factors such as the length of time and extent to which fair value has been below its cost basis, the financial condition of the issuer and any changes thereto, changes in market interest rates and the Company s intent to sell, or whether it is more likely than not it will be required to sell the investment before recovery of the investment s cost basis. As of March 26, 2016, the Company does not consider any of its investments to be other-than-temporarily impaired.

Derivative Financial Instruments

The Company may use derivatives to partially offset its business exposure to foreign currency and interest rate risk on expected future cash flows, on net investments in certain foreign subsidiaries and on certain existing assets and liabilities. However, the Company may choose not to hedge certain exposures for a variety of reasons including, but not limited to, accounting considerations and the prohibitive economic cost of hedging particular exposures. There can be no assurance the hedges will offset more than a portion of the financial impact resulting from movements in foreign currency exchange or interest rates.

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

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

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

The Company may enter into interest rate swaps, options, or other instruments to manage interest rate risk. These instruments may offset a portion of changes in income or expense, or changes in fair value of the Company s term debt or investments. The Company designates these instruments as either cash flow or fair value hedges. The Company s hedged interest rate transactions as of March 26, 2016 are expected to be recognized within ten years.

Cash Flow Hedges

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

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

Net Investment Hedges

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

Fair Value Hedges

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

Non-Designated Derivatives

Derivatives that are not designated as hedging instruments are adjusted to fair value through earnings in the financial statement line item to which the derivative relates.

The Company records all derivatives in the Condensed Consolidated Balance Sheets at fair value. The Company s accounting treatment for these derivative instruments is based on its hedge designation. The following tables show the Company s derivative instruments at gross fair value as of March 26, 2016 and September 26, 2015 (in millions):

	March 26, 2016		
	Fair Value of Derivatives Designated as Hedge Instruments	**Fair Value of Derivatives Not Designated as Hedge Instruments**	**Total Fair Value**
Derivative assets [1]:			
Foreign exchange contracts	$ 564	$ 69	$ 633
Interest rate contracts	$ 557	$ 0	$ 557
Derivative liabilities [2]:			
Foreign exchange contracts	$ 1,033	$ 243	$ 1,276
Interest rate contracts	$ 36	$ 0	$ 36

	September 26, 2015		
	Fair Value of Derivatives Designated as Hedge Instruments	Fair Value of Derivatives Not Designated as Hedge Instruments	Total Fair Value
Derivative assets [1]:			
Foreign exchange contracts	$ 1,442	$ 109	$ 1,551
Interest rate contracts	$ 394	$ 0	$ 394
Derivative liabilities [2]:			
Foreign exchange contracts	$ 905	$ 94	$ 999
Interest rate contracts	$ 13	$ 0	$ 13

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

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

The following table shows the pre-tax gains and losses of the Company s derivative and non-derivative instruments designated as cash flow, net investment and fair value hedges on OCI and the Condensed Consolidated Statements of Operations for the three- and six-month periods ended March 26, 2016 and March 28, 2015 (in millions):

	Three Months Ended		Six Months Ended	
	March 26, 2016	March 28, 2015	March 26, 2016	March 28, 2015
Gains/(Losses) recognized in OCI effective portion:				
Cash flow hedges:				
Foreign exchange contracts	$ (138)	$ 1,249	$ 188	$ 3,750
Interest rate contracts	(50)	(87)	(42)	(91)
Total	$ (188)	$ 1,162	$ 146	$ 3,659
Net investment hedges:				
Foreign exchange contracts	$ 0	$ (6)	$ 0	$ 112
Foreign currency debt	(87)	0	(77)	0
Total	$ (87)	$ (6)	$ (77)	$ 112
Gains/(Losses) reclassified from AOCI into net income effective portion:				

Cash flow hedges:								
Foreign exchange contracts	$	668	$	818	$	1,183	$	1,485
Interest rate contracts		(3)		(5)		(7)		(9)
Total	$	665	$	813	$	1,176	$	1,476
Gains/(Losses) on derivative instruments:								
Fair value hedges:								
Interest rate contracts	$	250	$	122	$	139	$	239
Gains/(Losses) related to hedged items:								
Fair value hedges:								
Interest rate contracts	$	(250)	$	(122)	$	(139)	$	(239)

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The following table shows the notional amounts of the Company s outstanding derivative instruments and credit risk amounts associated with outstanding or unsettled derivative instruments as of March 26, 2016 and September 26, 2015 (in millions):

	March 26, 2016		September 26, 2015	
	Notional Amount	Credit Risk Amount	Notional Amount	Credit Risk Amount
Instruments designated as accounting hedges:				
Foreign exchange contracts	$ 41,996	$ 564	$ 70,054	$ 1,385
Interest rate contracts	$ 23,750	$ 557	$ 18,750	$ 394
Instruments not designated as accounting hedges:				
Foreign exchange contracts	$ 30,573	$ 69	$ 49,190	$ 109

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

The Company generally enters into master netting arrangements, which are designed to reduce credit risk by permitting net settlement of transactions with the same counterparty. To further limit credit risk, the Company generally enters into collateral security arrangements that provide for collateral to be received or posted when the net fair value of certain financial instruments fluctuates from contractually established thresholds. The Company presents its derivative assets and derivative liabilities at their gross fair values in its Condensed Consolidated Balance Sheets. As of March 26, 2016, the net cash collateral posted by the Company related to derivative instruments under its collateral security arrangements was $3 million, which was recorded as other current assets in the Condensed Consolidated Balance Sheet. As of September 26, 2015, the net cash collateral received by the Company related to derivative instruments under its collateral security arrangements was $1.0 billion, which was recorded as accrued expenses in the Condensed Consolidated Balance Sheet.

Under master netting arrangements with the respective counterparties to the Company s derivative contracts, the Company is allowed to net settle transactions with a single net amount payable by one party to the other. As of March 26, 2016 and September 26, 2015, the potential effects of these rights of set-off associated with the Company s derivative contracts, including the effects of collateral, would be a reduction to both derivative assets and derivative liabilities of $1.4 billion and $2.2 billion, respectively, resulting in net derivative liabilities of $119 million and $78 million, respectively.

Accounts Receivable

Trade Receivables

The Company has considerable trade receivables outstanding with its third-party cellular network carriers, wholesalers, retailers, value-added resellers, small and mid-sized businesses and education, enterprise and government customers that are not covered by collateral, third-party financing arrangements or credit insurance. As of March 26, 2016 and September 26, 2015, the Company had one customer that represented 12% of total trade receivables. The Company s cellular network carriers accounted for 55% and 71% of trade receivables as of March 26, 2016 and September 26, 2015, respectively.

Vendor Non-Trade Receivables

The Company has non-trade receivables from certain of its manufacturing vendors resulting from the sale of components to these vendors who manufacture sub-assemblies or assemble final products for the Company. Vendor non-trade receivables from three of the Company s vendors accounted for 55%, 14% and 11% of total vendor non-trade receivables as of March 26, 2016 and three of the Company s vendors accounted for 38%, 18% and 14% of total vendor non-trade receivables as of September 26, 2015.

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Note 3 Condensed Consolidated Financial Statement Details

The following tables show the Company s condensed consolidated financial statement details as of March 26, 2016 and September 26, 2015 (in millions):

Property, Plant and Equipment, Net

	March 26, 2016	September 26, 2015
Land and buildings	$ 8,391	$ 6,956
Machinery, equipment and internal-use software	39,723	37,038
Leasehold improvements	5,937	5,263
Gross property, plant and equipment	54,051	49,257
Accumulated depreciation and amortization	(30,848)	(26,786)
Total property, plant and equipment, net	$ 23,203	$ 22,471

Other Non-Current Liabilities

	March 26, 2016	September 26, 2015
Deferred tax liabilities	$ 22,955	$ 24,062
Other non-current liabilities	10,904	9,365
Total other non-current liabilities	$ 33,859	$ 33,427

Other Income/(Expense), Net

The following table shows the detail of other income/(expense), net for the three- and six-month periods ended March 26, 2016 and March 28, 2015 (in millions):

	Three Months Ended		Six Months Ended	
	March 26, 2016	March 28, 2015	March 26, 2016	March 28, 2015
Interest and dividend income	$ 986	$ 675	$ 1,927	$ 1,329
Interest expense	(321)	(163)	(597)	(294)
Other expense, net	(510)	(226)	(773)	(579)

Total other income/(expense), net	$	155	$	286	$	557	$	456

Note 4 Acquired Intangible Assets

The Company s acquired intangible assets with definite useful lives primarily consist of patents and licenses and are amortized over periods typically from three to seven years. The following table summarizes the components of gross and net acquired intangible asset balances as of March 26, 2016 and September 26, 2015 (in millions):

	March 26, 2016			September 26, 2015		
	Gross Carrying Amount	Accumulated Amortization	Net Carrying Amount	Gross Carrying Amount	Accumulated Amortization	Net Carrying Amount
Definite-lived and amortizable acquired intangible assets	$ 8,797	$ (5,054)	$ 3,743	$ 8,125	$ (4,332)	$ 3,793
Indefinite-lived and non-amortizable acquired intangible assets	100	0	100	100	0	100
Total acquired intangible assets	$ 8,897	$ (5,054)	$ 3,843	$ 8,225	$ (4,332)	$ 3,893

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Note 5   Income Taxes

As of March 26, 2016, the Company recorded gross unrecognized tax benefits of $7.5 billion, of which $2.8 billion, if recognized, would affect the Company s effective tax rate. As of September 26, 2015, the total amount of gross unrecognized tax benefits was $6.9 billion, of which $2.5 billion, if recognized, would have affected the Company s effective tax rate. The Company s total gross unrecognized tax benefits are classified as other non-current liabilities in the Condensed Consolidated Balance Sheets. The Company had $1.5 billion and $1.3 billion of gross interest and penalties accrued as of March 26, 2016 and September 26, 2015, respectively, which are classified as other non-current liabilities in the Condensed Consolidated Balance Sheets.

Management believes that an adequate provision has been made for any adjustments that may result from tax examinations. However, the outcome of tax audits cannot be predicted with certainty. If any issues addressed in the Company s tax audits are resolved in a manner not consistent with management s expectations, the Company could be required to adjust its provision for income taxes in the period such resolution occurs. Although timing of the resolution and/or closure of audits is not certain, the Company believes it is reasonably possible that its gross unrecognized tax benefits could decrease (whether by payment, release or a combination of both) in the next 12 months by as much as $800 million.

On June 11, 2014, the European Commission issued an opening decision initiating a formal investigation against Ireland for alleged state aid to the Company. The opening decision concerns the allocation of profits for taxation purposes of the Irish branches of two subsidiaries of the Company. The Company believes the European Commission s assertions are without merit. If the European Commission were to conclude against Ireland, the European Commission could require Ireland to recover from the Company past taxes covering a period of up to 10 years reflective of the disallowed state aid. While such amount could be material, as of March 26, 2016 the Company is unable to estimate the impact.

Note 6   Debt

Commercial Paper

The Company issues unsecured short-term promissory notes (Commercial Paper) pursuant to a commercial paper program. The Company uses net proceeds from the commercial paper program for general corporate purposes, including dividends and share repurchases. As of March 26, 2016 and September 26, 2015, the Company had $8.0 billion and $8.5 billion of Commercial Paper outstanding, respectively, with maturities generally less than nine months. The weighted-average interest rate of the Company s Commercial Paper was 0.39% as of March 26, 2016 and 0.14% as of September 26, 2015.

The following table provides a summary of cash flows associated with the issuance and maturities of Commercial Paper for the six months ended March 26, 2016 and March 28, 2015 (in millions):

	Six Months Ended	
	March 26, 2016	**March 28, 2015**
Maturities less than 90 days:		
Proceeds from (repayments of) commercial paper, net	$ 660	$ 985

Maturities greater than 90 days:				
Proceeds from commercial paper		669		547
Repayments of commercial paper		(1,832)		(4,040)
Proceeds from (repayments of) commercial paper, net		(1,163)		(3,493)
Total change in commercial paper, net	$	(503)	$	(2,508)

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Long-Term Debt

As of March 26, 2016, the Company had outstanding floating- and fixed-rate notes with varying maturities for an aggregate principal amount of $71.3 billion (collectively the Notes). The Notes are senior unsecured obligations, and interest is payable in arrears, quarterly for the U.S. dollar-denominated and Australian dollar-denominated floating-rate notes, semi-annually for the U.S. dollar-denominated, Australian dollar-denominated, British pound-denominated and Japanese yen-denominated fixed-rate notes and annually for the euro-denominated and Swiss franc-denominated fixed-rate notes. The following table provides a summary of the Company s term debt as of March 26, 2016 and September 26, 2015:

		March, 26, 2016			September 26, 2015		
	Maturities		Amount (in millions)	Effective Interest Rate		Amount (in millions)	Effective Interest Rate
2013 debt issuance of $17.0 billion:							
Floating-rate notes	2016 - 2018	$	3,000	0.51% - 1.10%	$	3,000	0.51% - 1.10%
Fixed-rate 0.45% - 3.85% notes	2016 - 2043		14,000	0.51% - 3.91%		14,000	0.51% - 3.91%
2014 debt issuance of $12.0 billion:							
Floating-rate notes	2017 - 2019		2,000	0.69% - 0.92%		2,000	0.37% - 0.60%
Fixed-rate 1.05% - 4.45% notes	2017 - 2044		10,000	0.69% - 4.48%		10,000	0.37% - 4.48%
2015 debt issuances of $27.3 billion:							
Floating-rate notes	2017 - 2020		1,781	0.67% - 1.87%		1,743	0.36% - 1.87%
Fixed-rate 0.35% - 4.375% notes	2017 - 2045		25,063	0.28% - 4.51%		24,958	0.28% - 4.51%
Second quarter 2016 debt issuance of $15.5 billion:							
Floating-rate notes	2019		500	1.44%		0	0
Floating-rate notes	2021		500	1.75%		0	0
Fixed-rate 1.30% notes	2018		500	1.32%		0	0
Fixed-rate 1.70% notes	2019		1,000	1.71%		0	0
Fixed-rate 2.25% notes	2021		3,000	1.80%		0	0
Fixed-rate 2.85% notes	2023		1,500	2.48%		0	0
Fixed-rate 3.25% notes	2026		3,250	2.33%		0	0
Fixed-rate 4.50% notes	2036		1,250	4.54%		0	0
Fixed-rate 4.65% notes	2046		4,000	4.58%		0	0
Total debt issuance			15,500			0	

Total term debt		71,344		55,701
Unamortized premium/(discount)		15		(114)
Hedge accounting fair value adjustments		515		376
Less: Current portion of long-term debt		(2,500)		(2,500)
Total long-term debt	$	69,374	$	53,463

During the second quarter of 2016, the Company issued $15.5 billion U.S. dollar-denominated notes. To manage interest rate risk on the U.S. dollar-denominated fixed-rate notes maturing in 2021, 2023 and 2026, the Company entered into interest rate swaps with an aggregate notional amount of $5.0 billion, which effectively converted a portion of the fixed interest rates on these notes to a floating interest rate.

As of March 26, 2016, ¥149.3 billion of Japanese yen-denominated notes was designated as a hedge of the foreign currency exposure of its net investment in a foreign operation. The foreign currency transaction gain or loss on the Japanese yen-denominated debt designated as a hedge is recorded in OCI as a part of the cumulative translation adjustment. As of March 26, 2016 and September 26, 2015, the carrying value of the debt designated as a net investment hedge was $1.3 billion and $2.1 billion, respectively. For further discussion regarding the Company s use of derivative instruments see the Derivative Financial Instruments section of Note 2, Financial Instruments.

The effective interest rates for the Notes include the interest on the Notes, amortization of the discount and, if applicable, adjustments related to hedging. The Company recognized $311 million and $582 million of interest expense on its term debt for the three- and six-month periods ended March 26, 2016, respectively. The Company recognized $161 million and $289 million of interest expense on its term debt for the three- and six-month periods ended March 28, 2015, respectively.

As of March 26, 2016 and September 26, 2015, the fair value of the Company s Notes, based on Level 2 inputs, was $72.4 billion and $54.9 billion, respectively.

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Note 7 Shareholders Equity

Dividends

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

	Dividends Per Share	Amount (in millions)
2016:		
Second quarter	$ 0.52	$ 2,879
First quarter	0.52	2,898
Total cash dividends declared and paid	$ 1.04	$ 5,777
2015:		
Fourth quarter	$ 0.52	$ 2,950
Third quarter	0.52	2,997
Second quarter	0.47	2,734
First quarter	0.47	2,750
Total cash dividends declared and paid	$ 1.98	$ 11,431

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

Share Repurchase Program

In 2015, the Company s Board of Directors increased the share repurchase authorization to $140 billion of the Company s common stock, of which $117 billion had been utilized as of March 26, 2016. The Company s share repurchase program does not obligate it to acquire any specific number of shares. Under the program, shares may be repurchased in privately negotiated and/or open market transactions, including under plans complying with Rule 10b5-1 under the Securities Exchange Act of 1934, as amended (the Exchange Act).

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

The following table shows the Company s ASR activity and related information during the six months ended March 26, 2016 and the year ended September 26, 2015:

	Purchase Period End Date	**Number of Shares** (in thousands)	**Average Repurchase Price Per Share**	**ASR Amount** (in millions)