

MICROSOFT CORP
Form 10-Q
October 23, 2008
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UNITED STATES
SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

FORM 10-Q

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

For the Quarterly Period Ended September 30, 2008

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: 0-14278

MICROSOFT CORPORATION

(Exact name of registrant as specified in its charter)

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Washington (State or other jurisdiction of incorporation or organization)	91-1144442 (I.R.S. Employer Identification No.)
One Microsoft Way, Redmond, Washington (Address of principal executive offices)	98052-6399 (Zip Code)
(425) 882-8080 (Registrant's telephone number, including area code)	
None (Former name, former address and former fiscal year, if changed since last report)	

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

Indicate by check mark whether the registrant 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 <input checked="" type="checkbox"/>	Accelerated filer <input type="checkbox"/>
Non-accelerated filer <input type="checkbox"/> (Do not check if a smaller reporting company)	Smaller reporting company <input type="checkbox"/>

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

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

Class	Outstanding at October 20, 2008
Common Stock, \$0.00000625 par value per share	8,895,572,720 shares

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MICROSOFT CORPORATION

FORM 10-Q

For the Quarter Ended September 30, 2008

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Table of Contents**Part I. Financial Information****Item 1. Financial Statements****MICROSOFT CORPORATION****INCOME STATEMENTS****(In millions, except per share amounts)(Unaudited)**

	Three Months Ended September 30,	
	2008	2007
Revenue	\$ 15,061	\$ 13,762
Operating expenses:		
Cost of revenue	2,848	2,675
Research and development	2,283	1,837
Sales and marketing	3,044	2,683
General and administrative	887	718
Total operating expenses	9,062	7,913
Operating income	5,999	5,849
Other income (expense)	(8)	367
Income before income taxes	5,991	6,216
Provision for income taxes	1,618	1,927
Net income	\$ 4,373	\$ 4,289
Earnings per share:		
Basic	\$ 0.48	\$ 0.46
Diluted	\$ 0.48	\$ 0.45
Weighted average shares outstanding:		
Basic	9,084	9,380
Diluted	9,183	9,513
Cash dividends declared per common share	\$ 0.13	\$ 0.11

See accompanying notes.

Table of Contents**MICROSOFT CORPORATION****BALANCE SHEETS**

(In millions)

	September 30, 2008 (Unaudited)	June 30, 2008(1)
Assets		
Current assets:		
Cash and cash equivalents	\$ 9,004	\$ 10,339
Short-term investments (including securities pledged as collateral of \$1,011 and \$2,491)	11,718	13,323
Total cash, cash equivalents, and short-term investments	20,722	23,662
Accounts receivable, net of allowance for doubtful accounts of \$168 and \$153	9,535	13,589
Inventories	1,640	985
Deferred income taxes	1,974	2,017
Other	3,331	2,989
Total current assets	37,202	43,242
Property and equipment, net of accumulated depreciation of \$6,622 and \$6,302	6,552	6,242
Equity and other investments	4,381	6,588
Goodwill	12,291	12,108
Intangible assets, net	1,899	1,973
Deferred income taxes	1,041	949
Other long-term assets	1,751	1,691
Total assets	\$ 65,117	\$ 72,793
Liabilities and stockholders equity		
Current liabilities:		
Accounts payable	\$ 3,351	\$ 4,034
Short-term debt	1,975	
Accrued compensation	2,138	2,934
Income taxes	514	3,248
Short-term unearned revenue	11,815	13,397
Securities lending payable	1,070	2,614
Other	3,520	3,659
Total current liabilities	24,383	29,886
Long-term unearned revenue	1,662	1,900
Other long-term liabilities	5,478	4,721
Commitments and contingencies		
Stockholders equity:		
Common stock and paid-in capital shares authorized 24,000; outstanding 8,977 and 9,151	61,655	62,849
Retained deficit, including accumulated other comprehensive income of \$877 and \$1,140	(28,061)	(26,563)
Total stockholders equity	33,594	36,286

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Total liabilities and stockholders' equity	\$	65,117	\$	72,793
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(1) Derived from audited financial statements.

See accompanying notes.

Table of Contents**MICROSOFT CORPORATION****CASH FLOWS STATEMENTS****(In millions)(Unaudited)**

	Three Months Ended September 30,	
	2008	2007
Operations		
Net income	\$ 4,373	\$ 4,289
Depreciation, amortization, and other noncash items	585	435
Stock-based compensation expense	443	333
Net recognized losses (gains) on investments and derivatives	36	(187)
Excess tax benefits from stock-based payment arrangements	(44)	(69)
Deferred income taxes	376	357
Unearned revenue	4,186	3,821
Recognition of unearned revenue	(6,044)	(4,965)
Accounts receivable	3,985	2,806
Other current assets	(558)	(235)
Other long-term assets	(116)	(11)
Other current liabilities	(4,552)	(1,189)
Other long-term liabilities	700	493
Net cash from operations	3,370	5,878
Financing		
Proceeds from short-term debt	1,975	
Common stock issued	228	646
Common stock repurchased	(6,493)	(2,930)
Common stock cash dividends	(998)	(938)
Excess tax benefits from stock-based payment arrangements	44	69
Net cash used in financing	(5,244)	(3,153)
Investing		
Additions to property and equipment	(778)	(510)
Acquisition of companies, net of cash acquired	(377)	(5,396)
Purchases of investments	(4,246)	(5,997)
Maturities of investments	464	330
Sales of investments	7,075	9,120
Securities lending payable	(1,543)	196
Net cash from (used in) investing	595	(2,257)
Effect of exchange rates on cash and cash equivalents	(56)	58
Net change in cash and cash equivalents	(1,335)	526
Cash and cash equivalents, beginning of period	10,339	6,111
Cash and cash equivalents, end of period	\$ 9,004	\$ 6,637

See accompanying notes.

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MICROSOFT CORPORATION
STOCKHOLDERS EQUITY STATEMENTS

(In millions)(Unaudited)

	Three Months Ended September 30,	
	2008	2007
Common stock and paid-in capital		
Balance, beginning of period	\$ 62,849	\$ 60,557
Common stock issued	226	655
Common stock repurchased	(1,897)	(816)
Stock-based compensation expense	443	333
Stock option income tax benefits (deficiencies)	33	(87)
Other, net	1	57
Balance, end of period	61,655	60,699
Retained deficit		
Balance, beginning of period	(26,563)	(29,460)
Cumulative effect of a change in accounting principle adoption of FIN 48		(395)
Cumulative effect of a change in accounting principle adoption of EITF 06-2		(17)
Net income	4,373	4,289
Other comprehensive income:		
Net gains (losses) on derivative instruments	293	(88)
Net unrealized investments losses	(398)	(86)
Translation adjustments and other	(158)	50
Comprehensive income	4,110	4,165
Common stock cash dividends	(1,157)	(1,029)
Common stock repurchased	(4,451)	(1,828)
Balance, end of period	(28,061)	(28,564)
Total stockholders equity	\$ 33,594	\$ 32,135

See accompanying notes.

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MICROSOFT CORPORATION

NOTES TO FINANCIAL STATEMENTS

(Unaudited)

Note 1 Basis of Presentation and Consolidation and Recent Accounting Pronouncements

Basis of Presentation

In the opinion of management, the accompanying balance sheets and related interim statements of income, cash flows, and stockholders' equity include all adjustments, consisting only of normal recurring items, necessary for their fair presentation in conformity with accounting principles generally accepted in the United States of America (U.S. GAAP). Preparing financial statements requires management to make estimates and assumptions that affect the reported amounts of assets, liabilities, revenue, and expenses. Examples include: estimates of loss contingencies, product warranties, product life cycles, product returns, and stock-based compensation forfeiture rates; assumptions such as the elements comprising a software arrangement, including the distinction between upgrades/enhancements and new products; when technological feasibility is achieved for our products; the potential outcome of future tax consequences of events that have been recognized in our financial statements or tax returns; estimating the fair value and/or goodwill impairment for our reporting units; and determining when investment impairments are other-than-temporary. Actual results and outcomes may differ from management's estimates and assumptions.

Effective July 1, 2008, we began presenting gains and losses resulting from foreign currency remeasurements as a component of other income (expense). Prior to July 1, 2008, we included gains and losses resulting from foreign currency remeasurements as a component of sales and marketing expense. We changed our presentation because this better reflects how we manage these foreign currency exposures and as such gains and losses arising from the remeasurement of foreign currency transactions are incidental to our operations. Prior period amounts have been recast to conform to the current period presentation. See Note 3 Other Income (Expense).

Interim results are not necessarily indicative of results for a full year. The information included in this Form 10-Q should be read in conjunction with information included in the Microsoft Corporation 2008 Form 10-K.

Basis of Consolidation

The financial statements include the accounts of Microsoft Corporation and its subsidiaries. Intercompany transactions and balances have been eliminated. Equity investments in which we exercise significant influence but do not exercise control and are not the primary beneficiary are accounted for using the equity method. Investments in which we are not able to exercise significant influence over the investee and which do not have readily determinable fair values are accounted for under the cost method.

Recently Adopted Accounting Pronouncements

On July 1, 2008, we adopted Financial Accounting Standards Board (FASB) Statement No. 157, *Fair Value Measurements* (SFAS No. 157) for all financial assets and liabilities and nonfinancial assets and liabilities that are recognized or disclosed at fair value in the financial statements on a recurring basis (at least annually). SFAS No. 157 defines fair value, establishes a framework for measuring fair value in generally accepted accounting principles, and expands disclosures about fair value measurements. This statement does not require any new fair value measurements, but provides guidance on how to measure fair value by providing a fair value hierarchy used to classify the source of the information. See Note 4 Financial Instruments.

Statement of Financial Accounting Standard (SFAS) No. 159, *The Fair Value Option for Financial Assets and Financial Liabilities Including an amendment of FASB Statement No. 115*, became effective for us on

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MICROSOFT CORPORATION
NOTES TO FINANCIAL STATEMENTS (Continued)
(Unaudited)

July 1, 2008. SFAS No. 159 gives us the irrevocable option to elect fair value for the initial and subsequent measurement for certain financial assets and liabilities on a contract-by-contract basis with the difference between the carrying value before election of the fair value option and the fair value recorded upon election as an adjustment to beginning retained earnings. We chose not to elect the fair value option.

Recent Accounting Pronouncements Not Yet Adopted