

VMWARE, INC.

FORM 8-K (Current report filing)

Filed 10/26/16 for the Period Ending 10/25/16

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| Address | 3401 HILLVIEW AVENUE PALO ALTO, CA, 94304 |
| Telephone | (650) 427-5000 |
| CIK | 0001124610 |
| Symbol | VMW |
| SIC Code | 7372 - Services-Prepackaged Software |
| Industry | IT Services & Consulting |
| Sector | Technology |
| Fiscal Year | 01/31 |

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

FORM 8-K

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

Date of report (Date of earliest event reported): October 25, 2016

VMWARE, INC.

(Exact name of registrant as specified in its charter)

Delaware
(State or Other Jurisdiction
of Incorporation)

001-33622
(Commission
File Number)

94-3292913
(IRS Employer
Identification Number)

3401 Hillview Avenue, Palo Alto, CA
(Address of Principal Executive Offices)

94304
(Zip code)

Registrant's telephone number, including area code: (650) 427-5000

N/A
(Former Name or Former Address, if changed since last report)

Check the appropriate box below if the Form 8-K filing is intended to simultaneously satisfy the filing obligation of the registrant under any of the following provisions (see General Instruction A.2. below):

- ☐ Written communications pursuant to Rule 425 under the Securities Act (17 CFR 230.425)
 - ☐ Soliciting material pursuant to Rule 14a-12 under the Exchange Act (17 CFR 240.14a-12)
 - ☐ Pre-commencement communications pursuant to Rule 14d-2(b) under the Exchange Act (17 CFR 240.14d-2(b))
 - ☐ Pre-commencement communications pursuant to Rule 13e-4(c) under the Exchange Act (17 CFR 240.13e-4(c))
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Item 2.02 Results of Operations and Financial Condition.

On October 26, 2016, VMware, Inc. (“VMware” or the “Company”) issued a press release announcing its financial results for the quarter ended September 30, 2016. The press release, which includes information regarding VMware’s use of non-GAAP financial measures, is attached hereto as Exhibit 99.1 and is incorporated by reference herein.

The information in this Item 2.02 and the Exhibit attached hereto shall not be deemed “filed” for purposes of Section 18 of the Securities Exchange Act of 1934 (the “Exchange Act”) or otherwise subject to the liabilities of that section, nor shall it be deemed incorporated by reference in any filing under the Securities Act of 1933 or the Exchange Act, regardless of any general incorporation language in such filing.

Item 5.02 Departure of Directors or Certain Officers; Election of Directors; Appointment of Certain Officers; Compensatory Arrangements of Certain Officers.

On October 26, 2016, VMware announced the appointment of Sanjay Poonen as Chief Operating Officer, Customer Operations, and the appointments of Raghu Raghuram and Rajiv Ramaswami to co-lead a new Products and Cloud Services organization as Chief Operating Officers, Products and Cloud Services.

Prior to his appointment, Mr. Poonen had served as VMware’s Executive Vice President and General Manager, End-User Computing, Head of Global Marketing since April 2016. He joined VMware as Executive Vice President and General Manager, End-User Computing in August 2013. Prior to joining VMware, he spent more than seven years at SAP AG, a maker of enterprise data base solutions, serving as President and Corporate Officer of Platform Solutions and the Mobile Division from April 2012 until July 2013. Previously, he served as President of Global Solutions from November 2010 to March 2012, as Executive Vice President of Performance Optimization Apps from June 2008 to September 2009 and Senior Vice President of Analytics from April 2006 to May 2008. Mr. Poonen’s over 20 years of technology industry experience also included executive-level positions with Symantec and Veritas, and product management and engineering positions with Alphablox, Apple, Inc. and Microsoft Corporation.

Prior to his appointment, Mr. Raghuram had served as VMware’s Executive Vice President, Software-Defined Data Center Division since April 2012. Mr. Raghuram joined VMware in 2003 and has held multiple product management and marketing roles. Mr. Raghuram served as Senior Vice President and General Manager, Cloud Infrastructure and Management, Virtualization and Cloud Platforms, and Enterprise Products, from December 2009 through March 2012. Mr. Raghuram previously served as Vice President of VMware’s Server Business Unit and of Product and Solutions Marketing from September 2003 through December 2009. Prior to VMware, Mr. Raghuram held product management and marketing roles at Netscape and Bang Networks.

Prior to his appointment, Mr. Ramaswami had served as VMware’s Executive Vice President and General Manager of its Networking and Security business since April 2016. Before that, he was executive vice president and general manager of the Infrastructure & Networking Group of Broadcom Corporation, a semiconductor company, from 2010. Previously he was Vice President and General Manager of the Cloud Services and Switching Technology Group at Cisco Systems, Inc., where he also served as Vice President and General Manager for a variety of business units in Optical, Switching and Storage Networking. Prior to joining Cisco, he served in various technical and leadership positions at Xros, Tellabs and IBM’s Thomas J. Watson Research Center. Mr. Ramaswami is a member of the board of directors of NeoPhotonics Corporation.

Information required by Item 404(a) of Regulation S-K with respect to Mr. Poonen is incorporated by reference to page 77 of VMware’s definitive proxy statement dated April 13, 2016 filed with the Securities and Exchange Commission on Schedule 14A and attached hereto as Exhibit 99.2.

Item 5.03 Amendments to Articles of Incorporation or Bylaws; Change in Fiscal Year.

On October 25, 2016, the Board of Directors of VMware approved a change to the Company’s fiscal year (which currently ends on December 31 of each calendar year) whereby each fiscal year will consist of a 52- or 53-week period ending on the Friday nearest to January 31 of each year. The change in the Company’s fiscal year will be effective January 1, 2017 with the period ending February 3, 2017, which will be reported as a transition period. Accordingly, the Company’s first full fiscal year under its revised fiscal calendar will begin February 4, 2017 and end February 2, 2018. Following the change, the Company’s fiscal periods will correspond with those of Dell Technologies Inc., which acquired EMC Corporation, VMware’s controlling stockholder, on September 7, 2016.

The Company will include results for the transition period, beginning January 1, 2017 and ending February 3, 2017, in the first Form 10-Q that it will file in fiscal year 2018 for the fiscal quarter ending May 5, 2017. The Company will not file a separate transition report.

Item 9.01 Financial Statements and Exhibits.**(d) Exhibits**

99.1 Press release of VMware, Inc. dated October 26, 2016

99.2 Excerpt from page 77 of VMware, Inc. Proxy Statement Scheduled 14A information, filed with the SEC on April 13, 2016.

SIGNATURES

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

Date: October 26, 2016

VMware, Inc.

By: /s/ Zane Rowe

Zane Rowe

Chief Financial Officer and Executive Vice President



VMware Reports Third Quarter 2016 Results

-Strong portfolio performance results in Year-over-Year Revenue Growth of 6% to \$1.78 Billion

-New VMware Cross-Cloud Architecture and new cloud partnerships announced in the quarter to offer customers the most complete and capable hybrid cloud

PALO ALTO, Calif., October 26, 2016 — VMware, Inc. (NYSE: VMW), a leader in cloud infrastructure and business mobility, today announced financial results for the third quarter of 2016:

- Revenue for the third quarter was \$1.78 billion, an increase of 6% from the third quarter of 2015.
- License revenue for the third quarter was \$691 million, an increase of 1% from the third quarter of 2015.
- GAAP net income for the third quarter was \$319 million, or \$0.75 per diluted share, up 25% per diluted share compared to \$256 million, or \$0.60 per diluted share, for the third quarter of 2015. Non-GAAP net income for the quarter was \$485 million, or \$1.14 per diluted share, up 12% per diluted share compared to \$433 million, or \$1.02 per diluted share, for third quarter of 2015.
- GAAP operating income for the third quarter was \$381 million, an increase of 17% from the third quarter of 2015. Non-GAAP operating income for the third quarter was \$592 million, an increase of 12% from the third quarter of 2015.
- Operating cash flows for the third quarter were \$620 million. Free cash flows for the quarter were \$590 million.
- Cash, cash equivalents and short-term investments were \$8.25 billion, and unearned revenue was \$5.09 billion as of September 30, 2016.
- Total revenue plus sequential change in total unearned revenue grew 13% year-over-year.
- License revenue plus sequential change in unearned license revenue grew 9% year-over-year.

“Our very good third-quarter financial results reflect VMware’s strength in delivering strategic value to our customers,” said Pat Gelsinger, chief executive officer, VMware. “We are helping customers run any application across their private, public and hybrid clouds with our new Cross-Cloud Architecture™, the industry’s most complete and capable hybrid cloud offering.”

Zane Rowe, executive vice president and chief financial officer, VMware, said, “We are pleased with our Q3 financial performance, which exceeded the midpoint of our revenue and operating margin guidance. We continue to broaden our portfolio with a range of products that will drive growth for the company.”

Today VMware announced the formation of a new Products and Cloud Services organization focused on extending VMware’s leadership across compute, storage, networking, management

and business mobility. Raghu Raghuram and Rajiv Ramaswami will co-lead this new organization and take on expanded roles as Chief Operating Officers, Products and Cloud Services. Sanjay Poonen is also taking on an expanded role as Chief Operating Officer, Customer Operations responsible for Worldwide Sales and Services, Channels, Marketing, and Global Communications. With these changes, Sumit Dhawan has been promoted to General Manager and Senior Vice President, End-User Computing, replacing Poonen in that role and Jeff Jennings has been promoted to Vice President and General Manager of the Networking and Security BU as Ramaswami moves into his COO role.

The company also announced a transition to the Dell fiscal year beginning on February 4, 2017. The first quarter for fiscal 2018 will begin on February 4 and end on May 5, 2017.

Recent Highlights & Strategic Announcements

- At VMworld 2016, VMware recently hosted over 30,000 customers, partners and influencers in Las Vegas and Barcelona and introduced a wave of new products and services designed to help customers accelerate their digital transformation:
 - As an extension of the company's hybrid cloud strategy, VMware unveiled its new Cross-Cloud Architecture™, which enables customers to run, manage, connect and secure their applications across clouds and devices in a common operating environment.
 - Expanding on VMware's partnership with IBM, the companies announced the availability of industry-first cloud services designed to quickly and easily move enterprise workloads to the cloud. With nearly 1,000 clients engaged, the global partnership between IBM and VMware is helping enterprises extend existing workloads to the public cloud in hours, versus weeks or months.
 - VMware unveiled new releases of its industry-leading compute, storage and cloud management solutions to help IT operations teams more efficiently run, manage and secure their traditional and modern applications on- or off-premises. The new releases of VMware vSphere®, VMware vSAN™ and VMware vRealize® Automation™ all will introduce support for containers enabling developers to become more productive and IT to easily run containerized applications in production.
 - New services for the Photon Platform™ will offer an end-to-end enterprise cloud-native infrastructure platform for running modern, containerized applications in production with end-to-end support provided by VMware.
 - VMware announced a new endpoint management approach for managing Windows 10, along with advancements to VMware Horizon® and VMware Workspace ONE™. These innovations will help advance the digital workspace and solve the challenge of supporting an increasingly mobile workforce that demands anytime, anywhere access to all applications from any device.
- Two weeks ago, VMware, the leader in private cloud, and Amazon Web Services, the leader in public cloud, announced a partnership, to provide a new VMware vSphere-based cloud service running on AWS. VMware Cloud™ on AWS will make it easier to run any application, using a common set of familiar software and tools, in a consistent hybrid cloud environment. This new service will be the primary public cloud solution delivered, sold and supported by VMware.
- At AirWatch Connect™, VMware announced additions its enterprise mobility management portfolio:
 - To help businesses of any size deliver apps, configure email, Wi-Fi, and get devices up and running quickly, VMware launched AirWatch Express™.
 - VMware will add the industry's first unified solution for smart glasses management for augmented and mixed reality experiences to its AirWatch portfolio.
 - Symantec selected VMware AirWatch to build enhanced endpoint security integrations

- For the seventh consecutive year, VMware was positioned in the Leaders Quadrant of Gartner, 2016 Magic Quadrant for x86 Server Virtualization Infrastructure ¹.
- Earlier this week, VMware released its Global Impact Report for 2015. In this report, VMware expands and elevates its long-standing commitment to driving innovations that contribute to a net positive future and sustainable growth. For example, since 2003 VMware's server virtualization products have avoided 603 million megawatt hours of power consumption, enough to power 53 million average U.S. households for one year ².

The company will host a conference call today at 2:00 p.m. PT/ 5:00 p.m. ET to review financial results and business outlook. A live web broadcast of the event will be available on the VMware investor relations website at <http://ir.vmware.com>. Slides will accompany the web broadcast. The replay of the webcast and slides will be available on the website for two months. In addition, six quarters of historical data for revenues which include year-over-year comparisons will also be made available at <http://ir.vmware.com> in conjunction with the conference call.

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About VMware

VMware, a global leader in cloud infrastructure and business mobility, helps customers accelerate their digital transformation. VMware enables enterprises to master a software-defined approach to business and IT with its Cross-Cloud Architecture™ and solutions for the data center, mobility, and security. With 2015 revenue of \$6.6 billion, VMware is headquartered in Palo Alto, CA and has over 500,000 customers and 75,000 partners worldwide.

Additional Information

VMware's website is located at www.vmware.com, and its investor relations website is located at <http://ir.vmware.com>. VMware's goal is to maintain the investor relations website as a portal through which investors can easily find or navigate to pertinent information about VMware, all of which is made available free of charge. The additional information includes materials that VMware files with the SEC; announcements of investor conferences and events at which its executives talk about its products, services and competitive strategies; webcasts of its quarterly earnings calls, investor conferences and events (archives of which are also available for a limited time); additional information on its financial metrics, including reconciliations of non-GAAP financial measures to the most directly comparable GAAP measures; press releases on quarterly earnings, product and service announcements, legal developments and international news; corporate governance information; and other news, blogs and announcements that VMware may post from time to time that investors may find useful or interesting.

VMware, Cross-Cloud Architecture, VMware vSAN, vSphere, vRealize, vRealize Automation, Workspace ONE, Photon Platform, Horizon, VMware Cloud, AirWatch, AirWatch Express, and AirWatch Connect are registered trademarks or trademarks of VMware or its subsidiaries in the United States and other jurisdictions. All other marks and names mentioned herein may be trademarks of their respective organizations.

Footnotes

1. Gartner, Thomas J. Bittman, et al., Magic Quadrant for x86 Server Virtualization Infrastructure, August 3, 2016.
2. IDC Executive Brief, sponsored by VMware, Green IT: Virtualization Delivers Energy and Carbon Emissions Reductions, October 2016.

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Use of Non-GAAP Financial Measures

Reconciliations of non-GAAP financial measures to VMware's financial results as determined in accordance with GAAP are included at the end of this press release following the accompanying financial data. For a description of these non-GAAP financial measures, including the reasons management uses each measure, please see the section of the tables titled "About Non-GAAP Financial Measures."

Forward-Looking Statements

This press release contains forward-looking statements including, among other things, statements regarding the features and expected benefits to customers of the new VMware Cross-Cloud Architecture, VMware Cloud on AWS, advancements to VMware Horizon and VMware Workspace ONE, new releases of VMware vSphere, VMware vSAN and VMware vRealize Automation, new services for the VMware Photon Platform, AirWatch smart glasses management and end point security integrations built in connection with Symantec; expectations of future growth driven by our broadening portfolio; and VMware's transition to the Dell fiscal year beginning on February 4, 2017. These forward-looking statements are subject to the safe harbor provisions created by the Private Securities Litigation Reform Act of 1995. Actual results could differ materially from those projected in the forward-looking statements as a result of certain risk factors, including but not limited to: (i) adverse changes in general economic or market conditions; (ii) delays or reductions in consumer, government and information technology spending; (iii) competitive factors, including but not limited to pricing pressures, industry consolidation, entry of new competitors into the virtualization software and cloud, end user and mobile computing industries, and new product and marketing initiatives by VMware's competitors; (iv) VMware's customers' ability to transition to new products and computing strategies such as cloud computing, desktop virtualization and the software defined data center; (v) VMware's ability to enter into and maintain strategically effective partnerships; (vi) the uncertainty of customer acceptance of emerging technology; (vii) rapid technological changes in the virtualization software and cloud, end user and mobile computing industries; (viii) changes to product and service development timelines; (ix) VMware's relationship with Dell Technologies and Dell's ability to control matters requiring stockholder approval, including the election of VMware's board members and matters relating to Dell's investment in VMware, and any changes that Dell may implement, having completed its acquisition of EMC Corporation in September 2016; (x) VMware's ability to protect its proprietary technology; (xi) VMware's ability to attract and retain highly qualified employees; (xii) the ability to successfully integrate acquired companies and assets into VMware; (xiii) disruptions to VMware's business resulting from the consummation of EMC's acquisition by Dell; (xiv) the ability of VMware to realize synergies following Dell's acquisition of EMC; (xv) disruptions resulting from key management changes; (xvi) fluctuating currency exchange rates; (xvii) changes in VMware's financial condition; and (xviii) potential disruptions relating to the transition to Dell's fiscal year and further business integrations with Dell. These forward-looking statements are made as of the date of this press release, are based on current expectations and are subject to uncertainties and changes in condition, significance, value and effect as well as other risks detailed in documents filed with the Securities and Exchange Commission, including VMware's most recent reports on Form 10-K and Form 10-Q and current reports on Form 8-K that we may file from time to time, which could cause actual results to vary from expectations. VMware assumes no obligation to, and does not currently intend to, update any such forward-looking statements after the date of this release.

Contacts:

Paul Ziots
VMware Investor Relations
pziots@vmware.com
650-427-3267

Michael Thacker
VMware Global PR
mthacker@vmware.com
650-427-4454

VMware, Inc.

CONDENSED CONSOLIDATED STATEMENTS OF INCOME
(amounts in millions, except per share amounts, and shares in thousands)
(unaudited)

| | Three Months Ended September 30, | | Nine Months Ended September 30, | |
|--|-------------------------------------|---------|------------------------------------|----------|
| | 2016 | 2015 | 2016 | 2015 |
| Revenue: | | | | |
| License | \$ 691 | \$ 681 | \$ 1,907 | \$ 1,896 |
| Services | 1,087 | 991 | 3,153 | 2,883 |
| GSA settlement | — | — | — | (76) |
| Total revenue | 1,778 | 1,672 | 5,060 | 4,703 |
| Operating expenses (1) : | | | | |
| Cost of license revenue | 40 | 46 | 121 | 142 |
| Cost of services revenue | 226 | 212 | 658 | 609 |
| Research and development | 389 | 331 | 1,109 | 958 |
| Sales and marketing | 564 | 556 | 1,708 | 1,656 |
| General and administrative | 178 | 201 | 516 | 568 |
| Realignment | — | — | 52 | 20 |
| Operating income | 381 | 326 | 896 | 750 |
| Investment income | 21 | 13 | 56 | 38 |
| Interest expense with Dell | (7) | (7) | (20) | (20) |
| Other income (expense), net | (8) | (7) | (8) | (8) |
| Income before income tax | 387 | 325 | 924 | 760 |
| Income tax provision | 68 | 69 | 179 | 137 |
| Net income | \$ 319 | \$ 256 | \$ 745 | \$ 623 |
| Net income per weighted-average share, basic for Class A and Class B | \$ 0.76 | \$ 0.61 | \$ 1.76 | \$ 1.47 |
| Net income per weighted-average share, diluted for Class A and Class B | \$ 0.75 | \$ 0.60 | \$ 1.75 | \$ 1.46 |
| Weighted-average shares, basic for Class A and Class B | 421,704 | 422,329 | 423,341 | 424,799 |
| Weighted-average shares, diluted for Class A and Class B | 425,008 | 423,981 | 425,851 | 427,466 |

(1) Includes stock-based compensation as follows:

| | | | | |
|----------------------------|------|------|------|------|
| Cost of license revenue | \$ — | \$ — | \$ 2 | \$ 1 |
| Cost of services revenue | 13 | 11 | 38 | 32 |
| Research and development | 80 | 56 | 224 | 164 |
| Sales and marketing | 51 | 43 | 146 | 124 |
| General and administrative | 26 | 16 | 62 | 47 |

VMware, Inc.

CONDENSED CONSOLIDATED BALANCE SHEETS
(amounts in millions, except per share amounts, and shares in thousands)
(unaudited)

| | September 30, 2016 | December 31, 2015 |
|---|-----------------------|----------------------|
| ASSETS | | |
| Current assets: | | |
| Cash and cash equivalents | \$ 2,654 | \$ 2,493 |
| Short-term investments | 5,600 | 5,016 |
| Accounts receivable, net of allowance for doubtful accounts of \$2 and \$2 | 1,119 | 1,633 |
| Due from related parties, net | 23 | 74 |
| Other current assets | 159 | 144 |
| Total current assets | 9,555 | 9,360 |
| Property and equipment, net | 1,050 | 1,128 |
| Other assets | 232 | 193 |
| Deferred tax assets | 462 | 456 |
| Intangible assets, net | 538 | 616 |
| Goodwill | 4,032 | 3,993 |
| Total assets | <u>\$ 15,869</u> | <u>\$ 15,746</u> |
| LIABILITIES AND STOCKHOLDERS' EQUITY | | |
| Current liabilities: | | |
| Accounts payable | \$ 104 | \$ 138 |
| Accrued expenses and other | 649 | 746 |
| Unearned revenue | 3,279 | 3,245 |
| Total current liabilities | 4,032 | 4,129 |
| Notes payable to Dell | 1,500 | 1,500 |
| Unearned revenue | 1,815 | 1,831 |
| Other liabilities | 388 | 363 |
| Total liabilities | 7,735 | 7,823 |
| Contingencies | | |
| Stockholders' equity: | | |
| Class A common stock, par value \$.01; authorized 2,500,000 shares; issued and outstanding 113,870 and 121,947 shares | 1 | 1 |
| Class B convertible common stock, par value \$.01; authorized 1,000,000 shares; issued and outstanding 300,000 shares | 3 | 3 |
| Additional paid-in capital | 2,174 | 2,728 |
| Accumulated other comprehensive income (loss) | 16 | (8) |
| Retained earnings | 5,940 | 5,195 |
| Total VMware, Inc.'s stockholders' equity | 8,134 | 7,919 |
| Non-controlling interests | — | 4 |
| Total stockholders' equity | 8,134 | 7,923 |
| Total liabilities and stockholders' equity | <u>\$ 15,869</u> | <u>\$ 15,746</u> |

VMware, Inc.

CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS

(in millions)
(unaudited)

| | Three Months Ended September 30, | | Nine Months Ended September 30, | |
|---|-------------------------------------|-----------------|------------------------------------|-----------------|
| | 2016 | 2015 | 2016 | 2015 |
| Operating activities: | | | | |
| Net income | \$ 319 | \$ 256 | \$ 745 | \$ 623 |
| Adjustments to reconcile net income to net cash provided by operating activities: | | | | |
| Depreciation and amortization | 87 | 87 | 261 | 246 |
| Stock-based compensation | 170 | 126 | 472 | 368 |
| Excess tax benefits from stock-based compensation | (6) | (1) | (7) | (27) |
| Deferred income taxes, net | (19) | (21) | (24) | (44) |
| Impairment of strategic investments | 7 | 5 | 12 | 5 |
| Gain on sale of strategic investments | — | — | (1) | — |
| Loss on disposal of assets | 5 | — | 12 | — |
| Other | — | — | (1) | — |
| Changes in assets and liabilities, net of acquisitions: | | | | |
| Accounts receivable | 96 | 203 | 513 | 508 |
| Other assets | 4 | 27 | (22) | 14 |
| Due to/from related parties, net | 73 | (32) | 55 | 31 |
| Accounts payable | (16) | (2) | (26) | (36) |
| Accrued expenses | (83) | (180) | (64) | (153) |
| Income taxes payable | 10 | 71 | (26) | 24 |
| Unearned revenue | (27) | (128) | 18 | (148) |
| Net cash provided by operating activities | <u>620</u> | <u>411</u> | <u>1,917</u> | <u>1,411</u> |
| Investing activities: | | | | |
| Additions to property and equipment | (30) | (90) | (109) | (274) |
| Purchases of available-for-sale securities | (1,126) | (580) | (3,337) | (2,675) |
| Sales of available-for-sale securities | 790 | 326 | 1,769 | 1,700 |
| Maturities of available-for-sale securities | 396 | 317 | 1,015 | 840 |
| Proceeds from disposal of assets | 1 | — | 3 | — |
| Purchases of strategic investments | (7) | (7) | (33) | (11) |
| Sales of strategic investments | — | — | 1 | 2 |
| Business acquisitions, net of cash acquired | — | — | (59) | (21) |
| Decrease (increase) in restricted cash | — | 76 | (2) | 77 |
| Net cash provided by (used in) investing activities | <u>24</u> | <u>42</u> | <u>(752)</u> | <u>(362)</u> |
| Financing activities: | | | | |
| Proceeds from issuance of common stock | 54 | 55 | 106 | 123 |
| Proceeds from non-controlling interests | — | — | — | 4 |
| Payment to acquire non-controlling interests | — | — | (4) | — |
| Repurchase of common stock | (1,016) | (200) | (1,016) | (1,050) |
| Excess tax benefits from stock-based compensation | 6 | 1 | 7 | 27 |
| Shares repurchased for tax withholdings on vesting of restricted stock | (25) | (17) | (97) | (141) |
| Net cash used in financing activities | <u>(981)</u> | <u>(161)</u> | <u>(1,004)</u> | <u>(1,037)</u> |
| Net increase (decrease) in cash and cash equivalents | (337) | 292 | 161 | 12 |
| Cash and cash equivalents at beginning of the period | <u>2,991</u> | <u>1,791</u> | <u>2,493</u> | <u>2,071</u> |
| Cash and cash equivalents at end of the period | <u>\$ 2,654</u> | <u>\$ 2,083</u> | <u>\$ 2,654</u> | <u>\$ 2,083</u> |
| Supplemental disclosures of cash flow information: | | | | |
| Cash paid for interest | \$ 7 | \$ 7 | \$ 21 | \$ 21 |
| Cash paid for taxes, net | 76 | 19 | 212 | 155 |
| Non-cash items: | | | | |
| Changes in capital additions, accrued but not paid | \$ 4 | \$ (27) | \$ (15) | \$ (49) |

CONSTANT CURRENCY GROWTH IN REVENUE PLUS SEQUENTIAL CHANGE IN UNEARNED REVENUE
(in millions)
(unaudited)

Constant Currency Growth in Total Revenue Plus Sequential Change in Unearned Revenue

| | Three Months Ended September 30, | |
|---|---|-----------------|
| | 2016 | 2015 |
| Total revenue, as reported | \$ 1,778 | \$ 1,672 |
| Sequential change in unearned revenue | (27) | (128) |
| Total revenue plus sequential change in unearned revenue | <u>\$ 1,751</u> | <u>\$ 1,544</u> |
| Change (%) over prior year, as reported | 13% | |
| Change (%) over prior year, including adjustment for impact of foreign currency (1) | 13% | |

Constant Currency Growth in License Revenue Plus Sequential Change in Unearned License Revenue

| | Three Months Ended September 30, | |
|---|---|---------------|
| | 2016 | 2015 |
| Total license revenue, as reported | \$ 691 | \$ 681 |
| Sequential change in unearned license revenue | (30) | (77) |
| Total license revenue plus sequential change in unearned license revenue | <u>\$ 661</u> | <u>\$ 604</u> |
| Change (%) over prior year, as reported | 9% | |
| Change (%) over prior year, including adjustment for impact of foreign currency (2) | 10% | |

- (1) Percentage change compares total revenue plus sequential change in unearned revenue in constant currency for the three months ended September 30, 2016 versus total revenue plus sequential change in unearned revenue as reported for the three months ended September 30, 2015. See “Growth in Constant Currency” for more information.
- (2) Percentage change compares license revenue plus sequential change in unearned license revenue in constant currency for the three months ended September 30, 2016 versus license revenue plus sequential change in unearned license revenue as reported for the three months ended September 30, 2015. See “Growth in Constant Currency” for more information.

VMware, Inc.

SUPPLEMENTAL REVENUE SCHEDULE
(INCLUDES RECONCILIATION OF GAAP TO NON-GAAP DATA)
(in millions)
(unaudited)

| | Three Months Ended | | | | | |
|---|-----------------------|------------------|-------------------|----------------------|-----------------------|------------------|
| | September 30, 2016 | June 30, 2016 | March 31, 2016 | December 31, 2015 | September 30, 2015 | June 30, 2015 |
| Revenue as reported (1) : | | | | | | |
| License | \$ 691 | \$ 644 | \$ 572 | \$ 825 | \$ 681 | \$ 638 |
| Software maintenance | 947 | 915 | 891 | 901 | 863 | 829 |
| Professional services | 140 | 134 | 126 | 142 | 128 | 130 |
| GSA settlement | — | — | — | — | — | (76) |
| Total revenue | <u>\$ 1,778</u> | <u>\$ 1,693</u> | <u>\$ 1,589</u> | <u>\$ 1,868</u> | <u>\$ 1,672</u> | <u>\$ 1,521</u> |
| Change (%) over prior year: | | | | | | |
| License | 1.4% | 0.9% | (0.7)% | 6.2% | 6.6% | 3.9% |
| Software maintenance | 9.7% | 10.4% | 9.7% | 12.1% | 10.8% | 12.4% |
| Professional services | 10.7% | 3.5% | 2.7% | 16.1% | 31.3% | 22.6% |
| GSA settlement | n/a | n/a | n/a | n/a | n/a | n/a |
| Total revenue | <u>6.4%</u> | <u>11.3%</u> | <u>5.2%</u> | <u>9.7%</u> | <u>10.3%</u> | <u>4.4%</u> |
| Revenue as reported, excluding GSA settlement (2) : | | | | | | |
| License | \$ 691 | \$ 644 | \$ 572 | \$ 825 | \$ 681 | \$ 638 |
| Software maintenance | 947 | 915 | 891 | 901 | 863 | 829 |
| Professional services | 140 | 134 | 126 | 142 | 128 | 130 |
| Non-GAAP total revenue | <u>\$ 1,778</u> | <u>\$ 1,693</u> | <u>\$ 1,589</u> | <u>\$ 1,868</u> | <u>\$ 1,672</u> | <u>\$ 1,597</u> |
| Change (%) over prior year: | | | | | | |
| License | 1.4% | 0.9% | (0.7)% | 6.2% | 6.6% | 3.9% |
| Software maintenance | 9.7% | 10.4% | 9.7% | 12.1% | 10.8% | 12.4% |
| Professional services | 10.7% | 3.5% | 2.7% | 16.1% | 31.3% | 22.6% |
| Non-GAAP total revenue | <u>6.4%</u> | <u>6.0%</u> | <u>5.2%</u> | <u>9.7%</u> | <u>10.3%</u> | <u>9.6%</u> |

(1) Represents revenue reported each quarter.

(2) Represents revenue reported each quarter less the reduction of revenue due to the GSA settlement recognized in the second quarter of 2015.

VMware, Inc.

SUPPLEMENTAL UNEARNED REVENUE SCHEDULE

(in millions)

(unaudited)

| | September 30, 2016 | June 30, 2016 | March 31, 2016 | December 31, 2015 | September 30, 2015 | June 30, 2015 |
|-------------------------------|-----------------------|------------------|-------------------|----------------------|-----------------------|------------------|
| Unearned revenue as reported: | | | | | | |
| License | \$ 425 | \$ 455 | \$ 415 | \$ 428 | \$ 404 | \$ 481 |
| Software maintenance | 4,201 | 4,189 | 4,105 | 4,174 | 3,850 | 3,894 |
| Professional services | 468 | 478 | 456 | 474 | 432 | 438 |
| Total unearned revenue | <u>\$ 5,094</u> | <u>\$ 5,122</u> | <u>\$ 4,976</u> | <u>\$ 5,076</u> | <u>\$ 4,686</u> | <u>\$ 4,813</u> |
| Change (%) over prior year: | | | | | | |
| License | 5.1% | (5.5)% | (11.0)% | (12.2)% | (5.6)% | 1.1% |
| Software maintenance | 9.1% | 7.6% | 6.7% | 6.9% | 8.2% | 10.0% |
| Professional services | 8.6% | 9.2% | 6.0% | 7.9% | 11.2% | 17.9% |
| Total unearned revenue | <u>8.7%</u> | <u>6.4%</u> | <u>4.9%</u> | <u>5.0%</u> | <u>7.1%</u> | <u>9.7%</u> |

VMware, Inc.

RECONCILIATION OF GAAP TO NON-GAAP DATA

For the Three Months Ended September 30, 2016

(amounts in millions, except per share amounts, and shares in thousands)

(unaudited)

| | GAAP | Stock-Based Compensation | Employer Payroll Taxes on Employee Stock Transactions | Intangible Amortization | Acquisition and Other Related Items | Tax Adjustment (1) | Non-GAAP, as adjusted (2) |
|--|---------|-----------------------------|---|----------------------------|--|-----------------------|------------------------------|
| Operating expenses: | | | | | | | |
| Cost of license revenue | \$ 40 | — | — | (26) | — | — | \$ 13 |
| Cost of services revenue | \$ 226 | (13) | — | (1) | — | — | \$ 212 |
| Research and development | \$ 389 | (80) | — | — | — | — | \$ 309 |
| Sales and marketing | \$ 564 | (51) | (2) | (5) | — | — | \$ 507 |
| General and administrative | \$ 178 | (26) | — | — | (6) | — | \$ 145 |
| Operating income | \$ 381 | 170 | 2 | 32 | 6 | — | \$ 592 |
| Operating margin (2) | 21.4% | 9.6% | 0.1% | 1.8% | 0.4% | — | 33.3% |
| Other income (expense), net | \$ (8) | — | — | — | 13 | — | \$ 5 |
| Income before income tax | \$ 387 | 170 | 2 | 32 | 19 | — | \$ 611 |
| Income tax provision | \$ 68 | | | | | 57 | \$ 126 |
| Tax rate (2) | 17.6% | | | | | | 20.5% |
| Net income | \$ 319 | 170 | 2 | 32 | 19 | (57) | \$ 485 |
| Net income per weighted-average share, diluted for Class A and Class B (2) (3) | \$ 0.75 | \$ 0.40 | \$ 0.01 | \$ 0.08 | \$ 0.04 | \$ (0.13) | \$ 1.14 |

- (1) Non-GAAP financial information for the quarter is adjusted for a tax rate equal to our annual estimated tax rate on non-GAAP income. This rate is based on our estimated annual GAAP income tax rate forecast, adjusted to account for items excluded from GAAP income in calculating the non-GAAP financial measures presented above as well as significant tax adjustments. Our estimated tax rate on non-GAAP income is determined annually and may be adjusted during the year to take into account events or trends that we believe materially impact the estimated annual rate including, but not limited to, significant changes resulting from tax legislation, material changes in the geographic mix of revenue and expenses and other significant events. Due to the differences in the tax treatment of items excluded from non-GAAP earnings, as well as the methodology applied to our estimated annual tax rates as described above, our estimated tax rate on non-GAAP income may differ from our GAAP tax rate and from our actual tax liabilities.
- (2) Totals may not sum, due to rounding. Operating margin, tax rate and net income per weighted average share information are calculated based upon the respective underlying, non-rounded data.
- (3) Calculated based upon 425,008 diluted weighted-average shares for Class A and Class B.

VMware, Inc.

RECONCILIATION OF GAAP TO NON-GAAP DATA

For the Three Months Ended September 30, 2015

(amounts in millions, except per share amounts, and shares in thousands)

(unaudited)

| | GAAP | Stock-Based Compensation | Employer Payroll Taxes on Employee Stock Transactions | Intangible Amortization | Acquisition and Other Related Items | Tax Adjustment (1) | Non-GAAP, as adjusted (2) |
|--|---------|-----------------------------|---|----------------------------|--|-----------------------|------------------------------|
| Operating expenses: | | | | | | | |
| Cost of license revenue | \$ 46 | — | — | (27) | — | — | \$ 19 |
| Cost of services revenue | \$ 212 | (11) | — | (1) | — | — | \$ 200 |
| Research and development | \$ 331 | (56) | — | — | — | — | \$ 274 |
| Sales and marketing | \$ 556 | (43) | (2) | (6) | — | — | \$ 506 |
| General and administrative | \$ 201 | (16) | — | (1) | (38) | — | \$ 146 |
| Operating income | \$ 326 | 126 | 2 | 35 | 38 | — | \$ 527 |
| Operating margin (2) | 19.5% | 7.5% | 0.1% | 2.1% | 2.3% | — | 31.5% |
| Other income (expense), net | \$ (7) | — | — | — | 5 | — | \$ (2) |
| Income before income tax | \$ 325 | 126 | 2 | 35 | 43 | — | \$ 531 |
| Income tax provision | \$ 69 | | | | | 29 | \$ 98 |
| Tax rate (2) | 21.4% | | | | | | 18.5% |
| Net income | \$ 256 | 126 | 2 | 35 | 43 | (29) | \$ 433 |
| Net income per weighted-average share, diluted for Class A and Class B (2) (3) | \$ 0.60 | \$ 0.30 | \$ 0.01 | \$ 0.08 | \$ 0.10 | \$ (0.07) | \$ 1.02 |

- (1) Non-GAAP financial information for the quarter is adjusted for a tax rate equal to our annual estimated tax rate on non-GAAP income. This rate is based on our estimated annual GAAP income tax rate forecast, adjusted to account for items excluded from GAAP income in calculating the non-GAAP financial measures presented above as well as significant tax adjustments. Our estimated tax rate on non-GAAP income is determined annually and may be adjusted during the year to take into account events or trends that we believe materially impact the estimated annual rate including, but not limited to, significant changes resulting from tax legislation, material changes in the geographic mix of revenue and expenses and other significant events. Due to the differences in the tax treatment of items excluded from non-GAAP earnings, as well as the methodology applied to our estimated annual tax rates as described above, our estimated tax rate on non-GAAP income may differ from our GAAP tax rate and from our actual tax liabilities.
- (2) Totals may not sum, due to rounding. Operating margin, tax rate and net income per weighted average share information are calculated based upon the respective underlying, non-rounded data.
- (3) Calculated based upon 423,981 diluted weighted-average shares for Class A and Class B.

VMware, Inc.

RECONCILIATION OF GAAP TO NON-GAAP DATA

For the Nine Months Ended September 30, 2016

(amounts in millions, except per share amounts, and shares in thousands)

(unaudited)

| | GAAP | Stock-Based Compensation | Employer Payroll Taxes on Employee Stock Transactions | Intangible Amortization | Realignment Charges | Acquisition and Other Related Items | Tax Adjustment (1) | Non-GAAP, as adjusted (2) |
|---|----------|-----------------------------|---|----------------------------|------------------------|--|-----------------------|------------------------------|
| Operating expenses: | | | | | | | | |
| Cost of license revenue | \$ 121 | (2) | — | (76) | — | — | — | \$ 43 |
| Cost of services revenue | \$ 658 | (38) | (1) | (2) | — | — | — | \$ 617 |
| Research and development | \$ 1,109 | (224) | (1) | — | — | — | — | \$ 883 |
| Sales and marketing | \$ 1,708 | (146) | (3) | (16) | — | — | — | \$ 1,542 |
| General and administrative | \$ 516 | (62) | (1) | (1) | — | (25) | — | \$ 428 |
| Realignment | \$ 52 | — | — | — | (52) | — | — | \$ — |
| Operating income | \$ 896 | 472 | 6 | 95 | 52 | 25 | — | \$ 1,547 |
| Operating margin (2) | 17.7% | 9.3% | 0.1% | 1.9% | 1.0% | 0.5% | — | 30.6% |
| Other income (expense), net | \$ (8) | — | — | — | — | 15 | — | \$ 6 |
| Income before income tax | \$ 924 | 472 | 6 | 95 | 52 | 40 | — | \$ 1,589 |
| Income tax provision | \$ 179 | | | | | | 145 | \$ 324 |
| Tax rate (2) | 19.4% | | | | | | | 20.4% |
| Net income | \$ 745 | 472 | 6 | 95 | 52 | 40 | (145) | \$ 1,265 |
| Net income per weighted- average share, diluted for Class A and Class B (2) (3) | \$ 1.75 | \$ 1.11 | \$ 0.01 | \$ 0.22 | \$ 0.12 | \$ 0.09 | \$ (0.34) | \$ 2.97 |

- (1) Non-GAAP financial information for the quarter is adjusted for a tax rate equal to our annual estimated tax rate on non-GAAP income. This rate is based on our estimated annual GAAP income tax rate forecast, adjusted to account for items excluded from GAAP income in calculating the non-GAAP financial measures presented above as well as significant tax adjustments. Our estimated tax rate on non-GAAP income is determined annually and may be adjusted during the year to take into account events or trends that we believe materially impact the estimated annual rate including, but not limited to, significant changes resulting from tax legislation, material changes in the geographic mix of revenue and expenses and other significant events. Due to the differences in the tax treatment of items excluded from non-GAAP earnings, as well as the methodology applied to our estimated annual tax rates as described above, our estimated tax rate on non-GAAP income may differ from our GAAP tax rate and from our actual tax liabilities.
- (2) Totals may not sum, due to rounding. Operating margin, tax rate and net income per weighted average share information are calculated based upon the respective underlying, non-rounded data.
- (3) Calculated based upon 425,851 diluted weighted-average shares for Class A and Class B.

VMware, Inc.

RECONCILIATION OF GAAP TO NON-GAAP DATA

For the Nine Months Ended September 30, 2015

(amounts in millions, except per share amounts, and shares in thousands)

(unaudited)

| | GAAP | Stock-Based Compensation | Employer Payroll Taxes on Employee Stock Transactions | Intangible Amortization | Realignment Charges | Acquisition and Other Related Items | GSA Settlement | Certain Litigation and Other Contingencies | Tax Adjustment (1) | Non-GAAP, as adjusted (2) |
|--|----------|-----------------------------|---|----------------------------|------------------------|--|-------------------|---|-----------------------|------------------------------|
| Revenue: | | | | | | | | | | |
| GSA settlement | \$ (76) | — | — | — | — | — | 76 | — | — | \$ — |
| Total revenue | \$ 4,703 | — | — | — | — | — | 76 | — | — | \$ 4,779 |
| Operating expenses: | | | | | | | | | | |
| Cost of license revenue | \$ 142 | (1) | — | (82) | — | — | — | — | — | \$ 59 |
| Cost of services revenue | \$ 609 | (32) | (1) | (2) | — | — | — | — | — | \$ 574 |
| Research and development | \$ 958 | (164) | (2) | — | — | — | — | — | — | \$ 792 |
| Sales and marketing | \$ 1,656 | (124) | (4) | (21) | — | — | — | — | — | \$ 1,507 |
| General and administrative | \$ 568 | (47) | (2) | (2) | — | (123) | 6 | (11) | — | \$ 389 |
| Realignment | \$ 20 | — | — | — | (20) | — | — | — | — | \$ — |
| Operating income | \$ 750 | 368 | 9 | 107 | 20 | 123 | 70 | 11 | — | \$ 1,458 |
| Operating margin (2) | 15.9% | 7.8% | 0.2% | 2.3% | 0.4% | 2.6% | 1.5% | 0.2% | — | 30.5% |
| Other income (expense), net | \$ (8) | — | — | — | — | 2 | — | — | — | \$ (6) |
| Income before income tax | \$ 760 | 368 | 9 | 107 | 20 | 124 | 70 | 11 | — | \$ 1,470 |
| Income tax provision | \$ 137 | | | | | | | | 135 | \$ 272 |
| Tax rate (2) | 18.0% | | | | | | | | | 18.5% |
| Net income | \$ 623 | 368 | 9 | 107 | 20 | 124 | 70 | 11 | (135) | \$ 1,198 |
| Net income per weighted-average share, diluted for Class A and Class B (2) (3) | \$ 1.46 | \$ 0.86 | \$ 0.02 | \$ 0.25 | \$ 0.05 | \$ 0.29 | \$ 0.16 | \$ 0.03 | \$ (0.32) | \$ 2.80 |

- (1) Non-GAAP financial information for the quarter is adjusted for a tax rate equal to our annual estimated tax rate on non-GAAP income. This rate is based on our estimated annual GAAP income tax rate forecast, adjusted to account for items excluded from GAAP income in calculating the non-GAAP financial measures presented above as well as significant tax adjustments. Our estimated tax rate on non-GAAP income is determined annually and may be adjusted during the year to take into account events or trends that we believe materially impact the estimated annual rate including, but not limited to, significant changes resulting from tax legislation, material changes in the geographic mix of revenue and expenses and other significant events. Due to the differences in the tax treatment of items excluded from non-GAAP earnings, as well as the methodology applied to our estimated annual tax rates as described above, our estimated tax rate on non-GAAP income may differ from our GAAP tax rate and from our actual tax liabilities.
- (2) Totals may not sum, due to rounding. Operating margin, tax rate and net income per weighted average share information are calculated based upon the respective underlying, non-rounded data.
- (3) Calculated based upon 427,466 diluted weighted-average shares for Class A and Class B.

VMware, Inc.

REVENUE BY TYPE
(in millions)
(unaudited)

| | Three Months Ended September 30, | | Nine Months Ended September 30, | |
|------------------------|---|-----------------|--|-----------------|
| | 2016 | 2015 | 2016 | 2015 |
| Revenue: | | | | |
| License | \$ 691 | \$ 681 | \$1,907 | \$ 1,896 |
| Services: | | | | |
| Software maintenance | 947 | 863 | 2,753 | 2,505 |
| Professional services | 140 | 128 | 400 | 378 |
| Total services | 1,087 | 991 | 3,153 | 2,883 |
| GSA settlement | — | — | — | (76) |
| Total revenue | <u>\$ 1,778</u> | <u>\$ 1,672</u> | <u>\$ 5,060</u> | <u>\$ 4,703</u> |
| Percentage of revenue: | | | | |
| License | 38.9% | 40.8% | 37.7% | 40.3% |
| Services: | | | | |
| Software maintenance | 53.3% | 51.6% | 54.4% | 53.3% |
| Professional services | 7.8% | 7.6% | 7.9% | 8.0% |
| Total services | 61.1% | 59.2% | 62.3% | 61.3% |
| GSA settlement | — % | — % | — % | (1.6)% |
| Total revenue | <u>100.0%</u> | <u>100.0%</u> | <u>100.0%</u> | <u>100.0%</u> |

VMware, Inc.

REVENUE BY GEOGRAPHY
(in millions)
(unaudited)

| | Three Months Ended September 30, | | Nine Months Ended September 30, | |
|------------------------|-------------------------------------|-----------------|------------------------------------|-----------------|
| | 2016 | 2015 | 2016 | 2015 |
| Revenue: | | | | |
| United States | \$ 916 | \$ 861 | \$2,587 | \$ 2,364 |
| International | 862 | 811 | 2,473 | 2,339 |
| Total revenue | <u>\$ 1,778</u> | <u>\$ 1,672</u> | <u>\$5,060</u> | <u>\$ 4,703</u> |
| Percentage of revenue: | | | | |
| United States | 51.5% | 51.5% | 51.1% | 50.3% |
| International | 48.5% | 48.5% | 48.9% | 49.7% |
| Total revenue | <u>100.0%</u> | <u>100.0%</u> | <u>100.0%</u> | <u>100.0%</u> |

VMware, Inc.

RECONCILIATION OF GAAP CASH FLOWS FROM OPERATING ACTIVITIES
TO FREE CASH FLOWS

(A NON-GAAP FINANCIAL MEASURE)

(in millions)

(unaudited)

| | Three Months Ended September 30, | | Nine Months Ended September 30, | |
|---|-------------------------------------|---------------|------------------------------------|-----------------|
| | 2016 | 2015 | 2016 | 2015 |
| GAAP cash flows from operating activities | \$ 620 | \$ 411 | \$ 1,917 | \$ 1,411 |
| Capital expenditures | (30) | (90) | (109) | (274) |
| Free cash flows | <u>\$ 590</u> | <u>\$ 321</u> | <u>\$ 1,808</u> | <u>\$ 1,137</u> |

About Non-GAAP Financial Measures

To provide investors and others with additional information regarding VMware's results, VMware has disclosed in this earnings release the following non-GAAP financial measures: non-GAAP revenue, non-GAAP operating income, non-GAAP operating margin, non-GAAP net income, non-GAAP income per diluted share, and free cash flows. VMware has provided a reconciliation of each non-GAAP financial measure used in this earnings release to the most directly comparable GAAP financial measure. These non-GAAP financial measures, other than free cash flows, differ from GAAP in that they exclude stock-based compensation, employer payroll tax on employee stock transactions, amortization of acquired intangible assets, realignment charges, acquisition and other-related items, certain litigation and other contingencies, and the GSA settlement, each as discussed below. Free cash flows differ from GAAP cash flows from operating activities with respect to the treatment of capital expenditures.

VMware has also presented in this earnings release (i) quarterly historical data for total revenue, excluding the GSA settlement, and unearned revenue; and (ii) data on the percentage change in total revenue and license revenue plus the sequential change in unearned revenue and unearned license revenue, respectively.

VMware's management believes that these measures are useful to investors because they allow investors to make meaningful comparisons of VMware revenue and unearned revenue across periods.

Additionally, VMware has presented in this earnings release data on the year-over-year growth in constant currency of (i) total revenue plus the sequential change in total unearned revenue and (ii) license revenue plus sequential change in unearned license revenue. VMware provides this information in order to provide a comparable framework for assessing how our business performed, adjusted for the impact of foreign currency fluctuations.

VMware's management uses these non-GAAP financial measures to understand and compare operating results across accounting periods, for internal budgeting and forecasting purposes, for short- and long-term operating plans, to calculate bonus payments and to evaluate VMware's financial performance, the performance of its individual functional groups and the ability of operations to generate cash. Management believes these non-GAAP financial measures reflect VMware's ongoing business in a manner that allows for meaningful period-to-period comparisons and analysis of trends in VMware's business, as they exclude charges and gains that are not reflective of ongoing operating results. Management also believes that these non-GAAP financial measures provide useful information to investors and others in understanding and evaluating VMware's operating results and future prospects in the same manner as management and in comparing financial results across accounting periods and to those of peer companies. Additionally, management believes information regarding free cash flows provides investors and others with an important perspective on the cash available to make strategic acquisitions and investments, to repurchase shares, to fund ongoing operations and to fund other capital expenditures.

Management believes these non-GAAP financial measures are useful to investors and others in assessing VMware's operating performance due to the following factors:

- *Stock-based compensation* . Stock-based compensation is generally fixed at the time the stock-based instrument is granted and amortized over a period of several years. Although stock-based compensation is an important aspect of the compensation of VMware's employees and executives, the expense for the fair value of the stock-based instruments VMware utilizes may bear little resemblance to the actual value realized upon the vesting or future exercise of the related stock-based awards. Management believes it is useful to exclude stock-based compensation in order to better understand the long-term performance of VMware's core business and to facilitate comparison of its results to those of peer companies.
- *Employer payroll tax on employee stock transactions* . The amount of employer payroll taxes on stock-based compensation is dependent on VMware's stock price and other factors that are beyond VMware's control and do not correlate to the operation of the business.
- *Amortization of acquired intangible assets* . A portion of the purchase price of VMware's acquisitions is generally allocated to intangible assets, such as intellectual property, and is subject to amortization. However, VMware does not acquire businesses on a predictable cycle. Additionally, the amount of an acquisition's purchase price allocated to intangible assets and the term of its related amortization can vary significantly and are unique to each acquisition. Therefore, VMware believes that the presentation of non-GAAP financial measures that adjust for the amortization of intangible assets provides investors and others with a consistent basis for comparison across accounting periods.

- *Realignment charges.* Realignment charges include workforce reductions, asset impairments, losses on asset disposals and costs to exit facilities. VMware's management believes it is useful to exclude these items, when significant, as they are not reflective of VMware's ongoing business and operating results.
- *Acquisition and other-related items .* As VMware does not acquire or dispose of businesses on a predictable cycle and the terms of each transaction can vary significantly and are unique to each transaction, VMware believes it is useful to exclude acquisition and other-related items when looking for a consistent basis for comparison across accounting periods. These items include:
 - Direct costs of acquisitions and dispositions, such as transaction and advisory fees.
 - Accruals for the portion of merger consideration payable in installments that may be paid in cash or VMware stock, at the option of VMware. These accruals are primarily composed of amounts VMware has committed to make to designated founders and key executives of AirWatch, subject to employment conditions and indemnification claims, if any.
 - Charges recognized for non-recoverable strategic investments or gains recognized on the disposition of strategic investments are included as other-related items.
 - Gains or losses on sale or disposal of distinct lines of business or product offerings, or transactions with features similar to discontinued operations, including recoveries or charges recognized to adjust the fair value of assets that qualify as "held for sale".
 - Certain costs incurred related to Dell's acquisition of VMware's parent company, EMC Corporation.
- *Certain litigation and other contingencies.* VMware, from time to time, may incur charges or benefits that are outside of the ordinary course of VMware's business related to litigation and other contingencies. VMware believes it is useful to exclude such charges or benefits because it does not consider such amounts to be part of the ongoing operation of VMware's business and because of the singular nature of the claims underlying such matters.
- *GSA Settlement.* During the second quarter of 2015, VMware reached an agreement with the Department of Justice ("DOJ") and the General Services Administration ("GSA") to resolve allegations that its sales practices between 2006 and 2013 had violated the federal False Claims Act. The settlement amount was \$76 million and was recorded as a reduction of total revenue. VMware believes it is useful to exclude this amount because it does not consider it to be part of the ongoing operations of VMware's business and because of the singular nature of the claims underlying the matter.
- *Tax adjustment .* Non-GAAP financial information for the quarter is adjusted for a tax rate equal to VMware's annual estimated tax rate on non-GAAP income. This rate is based on VMware's estimated annual GAAP income tax rate forecast, adjusted to account for items excluded from GAAP income in calculating VMware's non-GAAP income as well as significant tax adjustments. VMware's estimated tax rate on non-GAAP income is determined annually and may be adjusted during the year to take into account events or trends that VMware management believes materially impact the estimated annual rate including, but not limited to, significant changes resulting from tax legislation, material changes in the geographic mix of revenue and expenses and other significant events. Due to the differences in the tax treatment of items excluded from non-GAAP earnings, as well as the methodology applied to VMware's estimated annual tax rates as described above, the estimated tax rate on non-GAAP income may differ from the GAAP tax rate and from VMware's actual tax liabilities.

Additionally, VMware's management believes that the non-GAAP financial measure of free cash flows is meaningful to investors because management reviews cash flows generated from operations after taking into consideration capital expenditures due to the fact that these expenditures are considered to be a necessary component of ongoing operations.

The use of non-GAAP financial measures has certain limitations because they do not reflect all items of income and expense that affect VMware's operations. Specifically, in the case of stock-based compensation, if VMware did not pay out a portion of its compensation in the form of stock-based compensation and related employer payroll taxes, the cash salary expense included in operating expenses would be higher, which would affect VMware's cash position. VMware compensates for these limitations by reconciling the non-GAAP financial measures to the most comparable GAAP financial measures. These non-GAAP financial measures should be considered in addition to, not as a substitute for or in isolation from, measures prepared in accordance with GAAP and should not be

considered measures of VMware's liquidity. Further, these non-GAAP measures may differ from the non-GAAP information used by other companies, including peer companies, and therefore comparability may be limited. Management encourages investors and others to review VMware's financial information in its entirety and not rely on a single financial measure.

Growth in Constant Currency

A majority of VMware's sales are denominated in the U.S. dollar; however, VMware also invoices and collects in the euro, the British pound, the Japanese yen, the Australian dollar and the Chinese renminbi in their respective regions. The U.S. dollar is the functional currency for all of VMware's legal entities. At the time a non-U.S. dollar transaction is recorded, the value of the transaction is converted into U.S. dollars at the exchange rate in effect for the month in which each order is booked.

As a result, the amount of license and total revenues and unearned revenues derived from these transactions will be impacted by foreign exchange fluctuations. In order to provide a comparable framework for assessing how VMware's business performed adjusted for the impact of foreign currency fluctuations, management analyzes year-over-year license and total revenues growth on a constant currency basis.

Revenues Growth in Constant Currency and Sequential Change in Unearned Revenues

License and total revenues recognized during the current period derived from non-U.S. dollar based transactions were converted into U.S. dollars using the exchange rates that were effective in the comparable prior year period. The calculated current period license and total revenues, adjusted for foreign currency fluctuations, is compared to the license and total revenues of the comparable prior year period, as reported, in calculating license and total revenues growth in constant currency.

Unearned license revenue and unearned total revenue at the end of the period, derived from non-U.S. dollar transactions recorded during the current period, were adjusted for foreign currency fluctuations using the exchange rates that were effective in the comparable prior year period. Unearned license revenue and unearned total revenue, adjusted for foreign currency fluctuations at the end of the period, are compared to unearned license revenue and unearned total revenue at the beginning of the period, as reported, in determining the sequential change in unearned revenue.

Excerpt from page 77 of VMware, Inc. Proxy Statement Scheduled 14A information, filed with the SEC on April 13, 2016

Other Transactions with Related Persons

A brother of Sanjay Poonen, VMware's Executive Vice President, General Manager End-User Computing and Head of Global Marketing, was hired by VMware as a Director, Cloud Service Security on March 30, 2015. During 2015, Mr. Poonen's brother earned \$217,489 (including signing bonus, salary and annual bonus), which was commensurate with his level of experience and other employees having similar responsibilities. Mr. Poonen's brother also received equity awards for restricted stock units with a value of \$182,314 and which are subject to vesting over 4 years.