SALESFORCE COM INC
Form 10-Q
August 31, 2018
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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 July 31, 2018
OR
¨Transition report pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934
Commission File Number: 001-32224

salesforce.com, inc.
(Exact name of registrant as specified in its charter)

Delaware	94-3320693
(State or other jurisdiction of incorporation or organization)	(IRS Employer Identification No.)

The Landmark @ One Market, Suite 300
San Francisco, California 94105
(Address of principal executive offices)
Telephone Number (415) 901-7000
(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 (the "Exchange Act") 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, smaller reporting company or an emerging growth company. See the definitions of "large accelerated filer," "accelerated filer," "smaller reporting company" and "emerging growth company" in Rule 12b-2 of the Exchange Act.

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

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

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

As of July 31, 2018, there were approximately 756.7 million shares of the Registrant's Common Stock outstanding.

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PART I. FINANCIAL INFORMATION

ITEM 1. FINANCIAL STATEMENTS

salesforce.com, inc.
Condensed Consolidated Balance Sheets
(in millions)
(unaudited)

	July 31, 2018	January 31, 2018 (as adjusted)
Assets		
Current assets:		
Cash and cash equivalents	$2,319	$2,543
Marketable securities	1,108	1,978
Accounts receivable, net	1,980	3,921
Costs capitalized to obtain revenue contracts, net	669	671
Prepaid expenses and other current assets	726	471
Total current assets	6,802	9,584
Property and equipment, net	1,986	1,947
Costs capitalized to obtain revenue contracts, noncurrent, net	999	1,105
Capitalized software, net	145	146
Strategic investments	1,202	677
Goodwill	12,254	7,314
Intangible assets acquired through business combinations, net	1,976	827
Other assets, net	459	384
Total assets	$25,823	$21,984
Liabilities and stockholders’ equity		
Current liabilities:		
Accounts payable, accrued expenses and other liabilities	$2,083	$2,047
Unearned revenue	5,883	6,995
Current portion of debt	503	1,025
Total current liabilities	8,469	10,067
Noncurrent debt	3,173	695
Other noncurrent liabilities	653	846
Total liabilities	12,295	11,608
Stockholders’ equity:		
Common stock	1	1
Additional paid-in capital	12,308	9,752
Accumulated other comprehensive loss	(50)	(12)
Retained earnings	1,269	635
Total stockholders’ equity	13,528	10,376
Total liabilities and stockholders’ equity	$25,823	$21,984

See accompanying Notes.

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salesforce.com, inc.
Condensed Consolidated Statements of Operations
(in millions, except per share data)
(unaudited)

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	Three Months Ended July 31,		Six Months Ended July 31,	
	2018	2017 (as adjusted)	2018	2017 (as adjusted)
Revenues:				
Subscription and support	$3,060	$ 2,383	$5,870	$ 4,592
Professional services and other	221	194	417	382
Total revenues	3,281	2,577	6,287	4,974
Cost of revenues (1)(2):				
Subscription and support	638	494	1,211	957
Professional services and other	211	176	405	364
Total cost of revenues	849	670	1,616	1,321
Gross profit	2,432	1,907	4,671	3,653
Operating expenses (1)(2):				
Research and development	463	387	887	763
Marketing and sales	1,504	1,153	2,833	2,259
General and administrative	350	283	645	543
Total operating expenses	2,317	1,823	4,365	3,565
Income from operations	115	84	306	88
Investment income	12	9	28	14
Interest expense	(39)	(22)	(73)	(44)
Gains (losses) on strategic investments, net	143	(8)	354	(5)
Other income	0	0	1	0
Income before benefit from (provision for) income taxes	231	63	616	53
Benefit from (provision for) income taxes	68	(17)	27	(6)
Net income	$299	$ 46	$643	$ 47
Basic net income per share	$0.40	$ 0.06	$0.87	$ 0.07
Diluted net income per share	$0.39	$ 0.06	$0.84	$ 0.06
Shares used in computing basic net income per share	747	712	737	709
Shares used in computing diluted net income per share	774	729	763	726

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(1) Amounts include amortization of intangible assets acquired through business combinations, as follows:

	Three Months Ended July 31,		Six Months Ended July 31,	
	2018	2017	2018	2017
Cost of revenues	$52	$ 43	$91	$ 87
Marketing and sales	67	31	97	61

(2) Amounts include stock-based expense, as follows:

	Three Months Ended July 31,		Six Months Ended July 31,	
	2018	2017	2018	2017

Cost of revenues	$43	$ 32	$77	$ 64
Research and development	81	67	147	131
Marketing and sales	174	120	294	239
General and administrative	53	37	85	74

See accompanying Notes.

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salesforce.com, inc.
Condensed Consolidated Statements of Comprehensive Income
(in millions)
(unaudited)

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	Three Months Ended July 31,		Six Months Ended July 31,	
	2018	2017 (as adjusted)	2018	2017 (as adjusted)
Net income	$299	$ 46 *	$643	$ 47 *
Other comprehensive income (loss), before tax and net of reclassification adjustments:				
Foreign currency translation and other gains (losses)	(17)	16	(27)	30
Unrealized gains (losses) on marketable securities and strategic investments	0	(8)	(4)	63
Other comprehensive income (loss), before tax	(17)	8	(31)	93
Other comprehensive income (loss), net of tax	(17)	8	(31)	93
Comprehensive income	$282	$ 54	$612	$ 140

*Prior period information has been adjusted for Topic 606.

See accompanying Notes.

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salesforce.com, inc.
Condensed Consolidated Statements of Cash Flows
(in millions)
(unaudited)

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	Three Months Ended July 31,		Six Months Ended July 31,	
	2018	2017 (as adjusted)	2018	2017 (as adjusted)
Operating activities:				
Net income	$299	$ 46	$643	$ 47
Adjustments to reconcile net income to net cash provided by operating activities:				
Depreciation and amortization	252	192	433	377
Amortization of debt discount and issuance costs	1	7	17	15
Amortization of costs capitalized to obtain revenue contracts, net	183	148	371	289
Expenses related to employee stock plans	351	256	603	508
(Gains) losses on strategic investments, net	(143)	8	(354)	5
Changes in assets and liabilities, net of business combinations:				
Accounts receivable, net	(149)	(130)	2,013	1,629
Costs capitalized to obtain revenue contracts, net	(146)	(185)	(264)	(318)
Prepaid expenses and other current assets and other assets	4	6	(86)	(179)
Accounts payable, accrued expenses and other liabilities	179	203	(277)	(94)
Unearned revenue	(373)	(220)	(1,175)	(718)
Net cash provided by operating activities	458	331	1,924	1,561
Investing activities:				
Business combinations, net of cash acquired	(4,803)	0	(4,985)	(20)
Purchases of strategic investments	(37)	(46)	(184)	(58)
Sales of strategic investments	2	3	6	15
Purchases of marketable securities	(28)	(501)	(291)	(1,200)
Sales of marketable securities	335	139	1,273	243
Maturities of marketable securities	40	9	88	13
Capital expenditures	(170)	(128)	(292)	(285)
Net cash used in investing activities	(4,661)	(524)	(4,385)	(1,292)
Financing activities:				
Proceeds from issuance of debt, net	496	0	2,966	0
Proceeds from employee stock plans	182	183	383	343
Principal payments on capital lease obligations	(89)	(66)	(108)	(75)
Repayments of debt	0	0	(1,027)	(200)
Net cash provided by financing activities	589	117	2,214	68
Effect of exchange rate changes	11	0	23	5
Net increase (decrease) in cash and cash equivalents	(3,603)	(76)	(224)	342
Cash and cash equivalents, beginning of period	5,922	2,025	2,543	1,607
Cash and cash equivalents, end of period	$2,319	$ 1,949	$2,319	$ 1,949

See accompanying Notes.

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salesforce.com, inc.
Condensed Consolidated Statements of Cash Flows
Supplemental Cash Flow Disclosure
(in millions)

	Three Months Ended July 31,		Six Months Ended July 31,	
	2018	2017	2018	2017
Supplemental cash flow disclosure:				
Cash paid during the period for:				
Interest	$22	$ 21	$29	$ 27
Income taxes, net of tax refunds	$18	$ 9	$37	$ 27
Non-cash investing and financing activities:				
Fair value of equity awards assumed	$387	$ 0	$387	$ 0
Fair value of common stock issued as consideration for business combinations	$1,178	$ 0	$1,178	$ 6

See accompanying Notes.

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salesforce.com, inc.
Notes to Condensed Consolidated Financial Statements
1. Summary of Business and Significant Accounting Policies
Description of Business
Salesforce.com, inc. (the "Company") is a leading provider of enterprise software, delivered through the cloud, with a focus on customer relationship management, or CRM. The Company introduced its first CRM solution in 2000, and has since expanded its service offerings into new areas and industries with new editions, features and platform capabilities.
The Company's core mission is to empower its customers to connect with their customers in entirely new ways through cloud, mobile, social, Internet of Things (“IoT”) and artificial intelligence technologies.
The Company's Customer Success Platform is a comprehensive portfolio of service offerings providing sales force automation, customer service and support, marketing automation, digital commerce, integration solutions, community management, industry-specific solutions, analytics, application development, IoT integration, collaborative productivity tools, an enterprise cloud marketplace which the Company refers to as the AppExchange, and its professional cloud services.
Fiscal Year
The Company’s fiscal year ends on January 31. References to fiscal 2019, for example, refer to the fiscal year ending January 31, 2019.
Basis of Presentation
The accompanying condensed consolidated balance sheets as of July 31, 2018 and January 31, 2018 and the condensed consolidated statements of operations, condensed consolidated statements of comprehensive income and condensed consolidated statements of cash flows for the three and six months ended July 31, 2018 and 2017, respectively, are unaudited.
These financial statements have been prepared in accordance with U.S. generally accepted accounting principles (“U.S. GAAP”) for interim financial information. Accordingly, they do not include all of the financial information and footnotes required by U.S. GAAP for complete financial statements. In the opinion of the Company’s management, the unaudited condensed consolidated financial statements include all adjustments necessary for the fair presentation of the Company’s balance sheets as of July 31, 2018 and January 31, 2018, and its results of operations, including its comprehensive income, and its cash flows for the three and six months ended July 31, 2018 and 2017. All adjustments are of a normal recurring nature. The results for the three and six months ended July 31, 2018 are not necessarily indicative of the results to be expected for any subsequent quarter or for the fiscal year ending January 31, 2019.
These unaudited interim condensed consolidated financial statements should be read in conjunction with the consolidated financial statements and related notes included in the Company's Annual Report on Form 10-K for the fiscal year ended January 31, 2018, filed with the Securities and Exchange Commission (the “SEC”) on March 9, 2018.
The Company has adjusted its condensed consolidated financial statements from amounts previously reported due to the adoption of Accounting Standards Update No. 2014-09, “Revenue from Contracts with Customers (Topic 606)” (“ASU 2014-09”) as discussed below. In addition, the Company prospectively adopted Accounting Standards Update No. 2016-01, "Financial Instrument-Overall (Subtopic 825-10)" ("ASU 2016-01") and Accounting Standards Update No. 2016-16, "Income Taxes (Topic 740): Intra-Entity Transfers of Assets Other Than Inventory" ("ASU 2016-16"), as discussed below.
Use of Estimates
The preparation of financial statements in conformity with U.S. GAAP requires management to make estimates and assumptions in the Company’s condensed consolidated financial statements and notes thereto.
Significant estimates and assumptions made by management include the determination of:
- the standalone selling price (SSP) of performance obligations for contracts with multiple performance obligations;
- the estimate of variable consideration as part of the adoption of ASU 2014-09;
- the fair value of assets acquired and liabilities assumed for business combinations;
- the recognition, measurement and valuation of current and deferred income taxes;
- the average period of benefit associated with costs capitalized to obtain revenue contracts;

- the fair value of certain stock awards issued;
- the useful lives of intangible assets; and
- the valuation of privately-held strategic investments.

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Actual results could differ materially from those estimates. The Company bases its estimates on historical experience and on various other assumptions that are believed to be reasonable, the result of which forms the basis for making judgments about the carrying values of assets and liabilities.

Principles of Consolidation

The condensed consolidated financial statements include the accounts of the Company and its wholly-owned subsidiaries. All significant intercompany balances and transactions have been eliminated in consolidation.

Segments

The Company operates as one operating segment. Operating segments are defined as components of an enterprise for which separate financial information is evaluated regularly by the chief operating decision maker, Marc Benioff, who is the co-chief executive officer, and the chairman of the board, in deciding how to allocate resources and assess performance. Over the past few years, the Company has completed a number of acquisitions. These acquisitions have allowed the Company to expand its offerings, presence and reach in various market segments of the enterprise cloud computing market. While the Company has offerings in multiple enterprise cloud computing market segments, including as a result of the Company's acquisitions, the Company's business operates in one operating segment because the Company's offerings operate on its single Customer Success Platform and most of the Company's products are deployed in an identical way, and the Company's chief operating decision maker evaluates the Company's financial information and resources and assesses the performance of these resources on a consolidated basis. Since the Company operates in one operating segment, all required financial segment information can be found in the condensed consolidated financial statements.

In August 2018, the Company moved to a co-chief executive officer model with the promotion of the Company's vice chairman and chief operating officer. The Company will continue to assess who the chief operating decision maker is for the purposes of segment reporting in light of this recent change.

Concentrations of Credit Risk and Significant Customers

The Company's financial instruments that are exposed to concentrations of credit risk consist primarily of cash and cash equivalents, marketable securities and accounts receivable. Collateral is not required for accounts receivable. The Company maintains an allowance for its doubtful accounts receivable. This allowance is based upon historical loss patterns, the number of days that billings are past due and an evaluation of the potential risk of loss associated with delinquent accounts. Receivables are written-off and charged against the recorded allowance when the Company has exhausted collection efforts without success.

No single customer accounted for more than five percent of accounts receivable at July 31, 2018 and January 31, 2018. No single customer accounted for five percent or more of total revenue during the six months ended July 31, 2018 and 2017. As of July 31, 2018 and January 31, 2018, assets located outside the Americas were 12 percent and 17 percent of total assets, respectively. As of July 31, 2018 and January 31, 2018, assets located in the United States were 87 percent and 81 percent of total assets, respectively.

Revenue Recognition

Adoption of Topic 606

Effective at the start of fiscal 2019, the Company adopted the provisions and expanded disclosure requirements described in ASU 2014-09 also referred to as Topic 606. The Company adopted the standard using the full retrospective method. Accordingly, the results for the prior comparable period were adjusted to conform to the current period measurement and recognition of results.

The impact of Topic 606 on reported revenue results was not material. Topic 606, however, modified the Company's revenue recognition policy in the following ways:

•Removal of the limitation on contingent revenue, which can result in the subscription and support revenue for certain multi-year customer contracts being recognized earlier in the duration of the contract term;

•More allocation of subscription and support revenues across the Company's cloud service offerings and to professional services revenue; and

•Inclusion of an estimate of variable consideration, such as overage fees, in the total transaction price, which results in the estimated fees being recognized ratably over the contract term, further resulting in the recognition of subscription and support revenues before the actual variable consideration occurs.

The Company used the following transitional practical expedients in the adoption of Topic 606:
•The Company has not disclosed the remaining performance obligation (formerly, remaining transaction price) for all of the reporting periods prior to the first quarter of fiscal 2019; and

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•Contracts modified before fiscal 2017 were reflected using the retrospective method.

Additionally, as part of its business strategy, the Company periodically makes acquisitions of complementary businesses, services and technology. These acquired businesses may have customer arrangements that include the delivery of an on-premise software element combined with a software-as-a-service element. This was the case with the Company's acquisition of MuleSoft, Inc. (“MuleSoft”) in May 2018. The Company has to apply significant judgment to determine the appropriate revenue recognition policy for such products and services since Topic 606 eliminated the provision that service revenue accounting was appropriate when the relative selling price of one or more deliverables in a multiple element solution arrangement could not be determined.

Revenue Recognition Policy

The Company derives its revenues from two sources: (1) subscription revenues, which are comprised of subscription fees from customers accessing the Company’s enterprise cloud computing services (collectively, "Cloud Services"), software licenses, and from customers paying for additional support beyond the standard support that is included in the basic subscription fees; and (2) related professional services such as process mapping, project management and implementation services. Other revenue consists primarily of training fees.

With the adoption of Topic 606, revenue is recognized upon transfer of control of promised products and services to customers in an amount that reflects the consideration the Company expects to receive in exchange for those products or services. If the consideration promised in a contract includes a variable amount, for example, overage fees, contingent fees or service level penalties, the Company includes an estimate of the amount it expects to receive for the total transaction price if it is probable that a significant reversal of cumulative revenue recognized will not occur.

The Company determines the amount of revenue to be recognized through application of the following steps:

•Identification of the contract, or contracts with a customer;

•Identification of the performance obligations in the contract;

•Determination of the transaction price;

•Allocation of the transaction price to the performance obligations in the contract; and

•Recognition of revenue when or as the Company satisfies the performance obligations.

The Company’s subscription service arrangements are non-cancelable and do not contain refund-type provisions.

Subscription and Support Revenues

Subscription and support revenues are comprised of fees that provide customers with access to Cloud Services, software licenses and related support and updates during the term of the arrangement.

Cloud Services allow customers to use the Company's multi-tenant software without taking possession of the software. Revenue is generally recognized ratably over the contract term.

Since the May 2018 acquisition of Mulesoft, subscription and support revenues also includes software licenses. These licenses for on-premises software provide the customer with a right to use the software as it exists when made available. Customers purchase these licenses through a subscription. Revenues from distinct licenses are generally recognized upfront when the software is made available to the customer. In cases where the Company allocates revenue to software updates and support, primarily because the updates are provided at no additional charge, revenue is recognized as the updates are provided, which is generally ratably over the contract term.

The Company typically invoices its customers annually in advance upon execution of the contract or subsequent renewals. Amounts that have been invoiced are recorded in accounts receivable and in unearned revenue or revenue, depending on whether transfer of control to customers has occurred.

Professional Services and Other Revenues

The Company’s professional services contracts are either on a time and materials, fixed fee or subscription basis. These revenues are recognized as the services are rendered for time and materials contracts, when the milestones are achieved and accepted by the customer or on a proportional performance basis for fixed price contracts and ratably over the contract term or on a proportional performance basis for subscription professional services contracts. The milestone method for revenue recognition is used when there is substantive uncertainty at the date the contract is entered into whether the milestone will be achieved. Training revenues are recognized as the services are performed.

Significant Judgments - Contracts with Multiple Performance Obligations

The Company enters into contracts with its customers that may include promises to transfer multiple Cloud Services, software licenses, premium support and professional services. A performance obligation is a promise in a contract with a

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customer to transfer products or services that are distinct. Determining whether products and services are distinct performance obligations that should be accounted for separately or combined as one unit of accounting may require significant judgment.

Cloud Services and software licenses are distinct as such services are often sold separately. In determining whether professional services are distinct, the Company considers the following factors for each professional services agreement: availability of the services from other vendors, the nature of the professional services, the timing of when the professional services contract was signed in comparison to the start date and the contractual dependence of the service on the customer's satisfaction with the professional services work. To date, the Company has concluded that all of the professional services included in contracts with multiple performance obligations are distinct.

The Company allocates the transaction price to each performance obligation on a relative standalone selling price ("SSP") basis. The SSP is the price at which the Company would sell a promised product or service separately to a customer. Judgment is required to determine the SSP for each distinct performance obligation.

The Company determines SSP by considering its overall pricing objectives and market conditions. Significant pricing practices taken into consideration include the Company's discounting practices, the size and volume of the Company's transactions, the customer demographic, the geographic area where services are sold, price lists, its go-to-market strategy, historical sales and contract prices. The determination of SSP is made through consultation with and approval by the Company's management, taking into consideration the go-to-market strategy. As the Company's go-to-market strategies evolve, the Company may modify its pricing practices in the future, which could result in changes to SSP.

In certain cases, the Company is able to establish SSP based on observable prices of products or services sold separately in comparable circumstances to similar customers. The Company uses a single amount to estimate SSP when it has observable prices.

If SSP is not directly observable, for example when pricing is highly variable, the Company uses a range of SSP. The Company determines the SSP range using information that may include market conditions or other observable inputs. The Company typically has more than one SSP for individual products and services due to the stratification of those products and services by customer size and geography.

Costs Capitalized to Obtain Revenue Contracts

As part of its adoption of ASU 2014-09, the Company capitalizes incremental costs of obtaining a non-cancelable subscription and support revenue contract. The provisions of ASU 2014-09 are significantly different than the Company's previous accounting for deferred commissions. The new guidance results in the capitalization of significantly more costs and longer amortization lives. Under the prior accounting guidance, the Company only capitalized sales commissions that had a direct relationship to a specific new revenue contract and amortized the capitalized amounts over the initial contract period, which was typically 12 to 36 months.

Under the new accounting, the capitalized amounts consist primarily of sales commissions paid to the Company's direct sales force. Capitalized amounts also include (1) amounts paid to employees other than the direct sales force who earn incentive payouts under annual compensation plans that are tied to the value of contracts acquired, (2) commissions paid to employees upon renewals of subscription and support contracts, (3) the associated payroll taxes and fringe benefit costs associated with the payments to the Company's employees, and to a lesser extent (4) success fees paid to partners in emerging markets where the Company has a limited presence.

Costs capitalized related to new revenue contracts are amortized on a straight-line basis over four years, which, although longer than the typical initial contract period, reflects the average period of benefit, including expected contract renewals. In arriving at this average period of benefit, the Company evaluated both qualitative and quantitative factors which included the estimated life cycles of its offerings and its customer attrition. Additionally, the Company amortizes capitalized costs for renewals and success fees paid to partners over two years.

The capitalized amounts are recoverable through future revenue streams under all non-cancelable customer contracts. The Company periodically evaluates whether there have been any changes in its business, the market conditions in which it operates or other events which would indicate that its amortization period should be changed or if there are potential indicators of impairment.

Amortization of capitalized costs to obtain revenue contracts is included in marketing and sales expense in the accompanying condensed consolidated statements of operations.

During the six months ended July 31, 2018, the Company capitalized $264 million of costs to obtain revenue contracts and amortized $371 million to marketing and sales expense. During the same period a year ago, the Company capitalized $318 million of costs to obtain revenue contracts and amortized $289 million to marketing and sales expense. Capitalized costs to obtain a revenue contract, net on the Company's condensed consolidated balance sheets totaled $1.7 billion at July 31, 2018 and $1.8 billion at January 31, 2018.

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Cash and Cash Equivalents

The Company considers all highly liquid investments purchased with an original maturity of three months or less to be cash equivalents. Cash and cash equivalents are stated at fair value.

Marketable Securities

The Company considers all of its marketable debt securities as available for use in current operations, including those with maturity dates beyond one year, and therefore classifies these securities within current assets on the condensed consolidated balance sheets. Securities are classified as available for sale and are carried at fair value, with the change in unrealized gains and losses, net of tax, reported as a separate component on the condensed consolidated statements of comprehensive income until realized. Fair value is determined based on quoted market rates when observable or utilizing data points that are observable, such as quoted prices, interest rates and yield curves. Declines in fair value judged to be other-than-temporary on securities available for sale are included as a reduction to investment income. To determine whether a decline in value is other-than-temporary, the Company evaluates, among other factors: the duration and extent to which the fair value has been less than the carrying value and its intent and ability to retain the investment for a period of time sufficient to allow for any anticipated recovery in fair value. For the purposes of computing realized and unrealized gains and losses, the cost of securities sold is based on the specific-identification method. Interest on securities classified as available for sale is also included as a component of investment income.

Strategic Investments

The Company holds strategic investments in publicly held equity securities and privately held debt and equity securities in which the Company does not have a controlling interest or significant influence. Publicly held equity securities are measured using quoted prices in their respective active markets with changes recorded through net gains on strategic investments on the condensed consolidated statement of operations. Privately held equity securities without a readily determinable fair value are recorded at cost and adjusted for impairments and observable price changes with a same or similar security from the same issuer and are recorded through net gains on strategic investments on the condensed consolidated statement of operations. Privately held debt securities are recorded at fair value with changes in fair value recorded through accumulated other comprehensive income on the condensed consolidated balance sheet. If, based on the terms of these publicly traded and privately held securities, the Company determines that the Company exercises significant influence on the entity to which these securities relate, the Company will apply the equity method of accounting for such investments.

Privately held debt and equity securities are valued using significant unobservable inputs or data in an inactive market and the valuation requires the Company's judgment due to the absence of market prices and inherent lack of liquidity. The carrying value is not adjusted for the Company's privately held equity securities if there are no observable price changes in a same or similar security from the same issuer or if there are no identified events or changes in circumstances that may indicate impairment, as discussed below. In determining the estimated fair value of its strategic investments in privately held companies, the Company utilizes the most recent data available to the Company. Valuations of privately held companies are inherently complex due to the lack of readily available market data. In addition, the determination of whether an orderly transaction is for a same or similar investment requires significant management judgment including: the rights and obligations of the investments, the extent to which those differences would affect the fair values of those investments, and the impact of any differences based on the stage of operational development of the investee.

The Company assesses its strategic investments portfolio quarterly for impairment. The Company’s impairment analysis encompasses an assessment of the severity and duration of the impairment and qualitative and quantitative analysis of other key factors including: the investee’s financial metrics, the investee’s products and technologies meeting or exceeding predefined milestones, market acceptance of the product or technology, other competitive products or technology in the market, general market conditions, management and governance structure of the investee, the investee’s liquidity, debt ratios and the rate at which the investee is using its cash. If the investment is considered to be other-than-temporarily impaired, the Company will record the investment at fair value by recognizing an impairment through the condensed consolidated statement of operations and establishing a new carrying value for the investment.

Derivative Financial Instruments

The Company enters into foreign currency derivative contracts with financial institutions to reduce foreign exchange risk. The Company uses forward currency derivative contracts to minimize the Company's exposure to balances primarily denominated in the Euro, British Pound Sterling, Japanese Yen, Canadian Dollar and Australian Dollar. The Company's foreign currency derivative contracts, which are not designated as hedging instruments, are used to reduce the exchange rate risk associated primarily with intercompany receivables and payables. The Company's derivative financial instruments program is not designated for trading or speculative purposes. As of July 31, 2018 and January 31, 2018, the outstanding foreign currency derivative contracts were recorded at fair value on the condensed consolidated balance sheets.

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Foreign currency derivative contracts are marked-to-market at the end of each reporting period with gains and losses recognized as other expense to offset the gains or losses resulting from the settlement or remeasurement of the underlying foreign currency denominated receivables and payables. While the contract or notional amount is often used to express the volume of foreign currency derivative contracts, the amounts potentially subject to credit risk are generally limited to the amounts, if any, by which the counterparties' obligations under the agreements exceed the obligations of the Company to the counterparties.

Fair Value Measurement

The Company measures its cash and cash equivalents, marketable securities and foreign currency derivative contracts at fair value. The additional disclosures regarding the Company's fair value measurements are included in Note 5 "Fair Value Measurement." In addition, the Company measures its publicly held equity securities at fair value. The additional disclosure regarding the Company's fair value measurements of its strategic investments are included in Note 3 "Investments."

Property and Equipment

Property and equipment are stated at cost. Depreciation is calculated on a straight-line basis over the estimated useful lives of those assets as follows:

Computers, equipment and software	3 to 9 years
Furniture and fixtures	5 years
Leasehold improvements	Shorter of the estimated lease term or 10 years
Building and structural components	Average weighted useful life of 32 years
Building - leased facility	27 years
Building improvements	10 years

When assets are retired or otherwise disposed of, the cost and accumulated depreciation and amortization are removed from their respective accounts and any loss on such retirement is reflected in operating expenses.

Capitalized Software Costs

The Company capitalizes costs related to its enterprise cloud computing services and certain projects for internal use incurred during the application development stage. Costs related to preliminary project activities and post implementation activities are expensed as incurred. Internal-use software is amortized on a straight-line basis over its estimated useful life, which is generally three to five years. Management evaluates the useful lives of these assets on an annual basis and tests for impairment whenever events or changes in circumstances occur that could impact the recoverability of these assets.

Intangible Assets acquired through Business Combinations

Intangible assets are amortized over their estimated useful lives. Each period, the Company evaluates the estimated remaining useful life of its intangible assets and whether events or changes in circumstances warrant a revision to the remaining period of amortization. Management tests for impairment whenever events or changes in circumstances occur that could impact the recoverability of these assets.

Impairment Assessment

The Company evaluates intangible assets and long-lived assets for possible impairment whenever events or changes in circumstances indicate that the carrying amount of such assets may not be recoverable. This includes but is not limited to significant adverse changes in business climate, market conditions, or other events that indicate an asset's carrying amount may not be recoverable. Recoverability of these assets is measured by comparing the carrying amount of each asset to the future undiscounted cash flows the asset is expected to generate. If the undiscounted cash flows used in the test for recoverability are less than the carrying amount of these assets, the carrying amount of such assets is reduced to fair value.

The Company evaluates and tests the recoverability of its goodwill for impairment at least annually during its fourth quarter of each fiscal year or more often if and when circumstances indicate that goodwill may not be recoverable. There were no material impairments of capitalized software, intangible assets, long-lived assets or goodwill during the six months ended July 31, 2018 and 2017.

Business Combinations

The Company uses its best estimates and assumptions to assign fair value to the tangible and intangible assets acquired and liabilities assumed at the acquisition date. The Company's estimates are inherently uncertain and subject to refinement. During the measurement period, which may be up to one year from the acquisition date, the Company may record adjustments

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to the fair value of these tangible and intangible assets acquired and liabilities assumed, with the corresponding offset to goodwill. In addition, uncertain tax positions and tax-related valuation allowances are initially recorded in connection with a business combination as of the acquisition date. The Company continues to collect information and reevaluates these estimates and assumptions quarterly and records any adjustments to the Company's preliminary estimates to goodwill provided that the Company is within the measurement period. Upon the conclusion of the measurement period or final determination of the fair value of assets acquired or liabilities assumed, whichever comes first, any subsequent adjustments are recorded to the Company's condensed consolidated statement of operations.

In the event the Company acquires an entity with which the Company has a preexisting relationship, the Company will recognize a gain or loss to settle that relationship as of the acquisition date, which is recorded in net gains on strategic investments within the condensed consolidated statements of operations. In the event that the Company acquires an entity in which the Company previously held a strategic investment, the difference between the fair value of the shares as of the date of the acquisition and the carrying value of the strategic investment is recorded as a gain or loss and recorded within net gains on strategic investments in the condensed consolidated statement of operations.

Leases and Asset Retirement Obligations

The Company categorizes leases at their inception as either operating or capital leases. In certain lease agreements, the Company may receive rent holidays and other incentives. The Company recognizes lease costs on a straight-line basis once control of the space is achieved, without regard to deferred payment terms such as rent holidays that defer the commencement date of required payments. Additionally, incentives received are treated as a reduction of costs over the term of the agreement.

The Company establishes assets and liabilities for the present value of estimated future costs to retire long-lived assets at the termination or expiration of a lease. Such assets are depreciated over the lease period to operating expense.

In the event the Company is the deemed owner for accounting purposes during construction, the Company records assets and liabilities for the estimated construction costs incurred under build-to-suit lease arrangements to the extent it is involved in the construction of structural improvements or takes construction risk prior to commencement of a lease.

The Company additionally has entered into subleases for unoccupied leased office space. To the extent there are losses associated with the sublease, they are recognized in the period the sublease is executed. Gains are recognized over the sublease life. Any sublease payments received in excess of the straight-line rent payments for the sublease are recorded as an offset to rent expense.

Stock-Based Expense

The Company recognizes stock-based expenses related to stock options and restricted stock awards on a straight-line basis, net of estimated forfeitures, over the requisite service period of the awards, which is generally the vesting term of four years.

The Company recognizes stock-based expenses related to shares issued pursuant to its Amended and Restated 2004 Employee Stock Purchase Plan ("ESPP" or "2004 Employee Stock Purchase Plan") on a straight-line basis over the offering period, which is 12 months. The ESPP allows employees to purchase shares of the Company's common stock at a 15 percent discount and also allows employees to reduce their percentage election once during a six month purchase period (December 15 and June 15 of each fiscal year), but not increase that election until the next one-year offering period. The ESPP also includes a re-set provision for the purchase price if the stock price on the purchase date is less than the stock price on the offering date.

Stock-based expenses related to performance share grants are measured based on grant date fair value and expensed on a straight-line basis, net of estimated forfeitures, over the service period of the awards, which is generally the vesting term of three years.

The Company, at times, grants unvested restricted shares to employee stockholders of certain acquired companies in lieu of cash consideration. These awards are generally subject to continued post-acquisition employment. Therefore, the Company accounts for them as post-acquisition stock-based expense. The Company recognizes stock-based expense equal to the grant date fair value of the restricted stock awards on a straight-line basis over the requisite service period of the awards, which is generally four years.

Income Taxes

The Company uses the asset and liability method of accounting for income taxes. Under this method, deferred tax assets and liabilities are determined based on temporary differences between the financial statement and tax basis of assets and liabilities using enacted tax rates in effect for the year in which the differences are expected to reverse. The effect on deferred tax assets and liabilities of a change in tax laws is recognized in the condensed consolidated statements of operations in the period that includes the enactment date.

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The Company’s tax positions are subject to income tax audits by multiple tax jurisdictions throughout the world. The Company recognizes the tax benefit of an uncertain tax position only if it is more likely than not that the position is sustainable upon examination by the taxing authority, solely based on its technical merits. The tax benefit recognized is measured as the largest amount of benefit which is greater than 50 percent likely to be realized upon settlement with the taxing authority. The Company recognizes interest accrued and penalties related to unrecognized tax benefits in the income tax provision.

Valuation allowances are established when necessary to reduce deferred tax assets to the amounts that are more likely than not expected to be realized based on the weighting of positive and negative evidence. Future realization of deferred tax assets ultimately depends on the existence of sufficient taxable income of the appropriate character (for example, ordinary income or capital gain) within the carryback or carryforward periods available under the applicable tax law. The Company regularly reviews the deferred tax assets for recoverability based on historical taxable income, projected future taxable income, the expected timing of the reversals of existing temporary differences and tax planning strategies. The Company’s judgments regarding future profitability may change due to many factors, including future market conditions and the ability to successfully execute its business plans. Should there be a change in the ability to recover deferred tax assets, the tax provision would increase or decrease in the period in which the assessment is changed.

In December 2017, the Tax Cuts and Jobs Act ("Tax Act") was enacted into law, significantly changing income tax law that affects U.S corporations. Key changes included a corporate tax rate reduction from 35 percent to 21 percent effective January 1, 2018, expensing of certain qualified property, significant changes to the U.S international tax system such as a one-time transition tax on accumulated foreign earnings, and how foreign earnings are subject to U.S. tax. The Company was required to recognize the effects of the tax law changes in the period of enactment, including the determination of the transition tax and the re-measurement of deferred taxes as well as to re-assess the realizability of the deferred tax assets. Subsequent to the enactment of the Tax Act, the SEC staff issued Staff Accounting Bulletin No. 118, Income Tax Accounting Implications of the Tax Cuts and Jobs Act ("SAB 118"), which allows companies to record provisional amounts related to the effects of the Tax Act during a measurement period not to extend beyond one year from the enactment date. Due to the timing of the Tax Act and additional guidance and interpretations that may be issued by the U.S. Treasury Department, the Internal Revenue Service ("IRS") and other standard-setting bodies in the future, the Company has not completed its analysis of the income tax effects of the Tax Act. The provisional estimates will be adjusted during the measurement period defined under SAB 118, based upon the Company's ongoing analysis of its data and tax positions along with new guidance from regulators and interpretations of the law.

Foreign Currency Translation

The functional currency of the Company’s major foreign subsidiaries is generally the local currency. Adjustments resulting from translating foreign functional currency financial statements into U.S. dollars are recorded as a separate component on the condensed consolidated statement of comprehensive income. Foreign currency transaction gains and losses are included in Other income in the condensed consolidated statement of operations for the period. All assets and liabilities denominated in a foreign currency are translated into U.S. dollars at the exchange rate on the balance sheet date. Revenues and expenses are translated at the average exchange rate during the period. Equity transactions are translated using historical exchange rates.

Warranties and Indemnification

The Company’s enterprise cloud computing services are typically warranted to perform in a manner consistent with general industry standards that are reasonably applicable and materially in accordance with the Company’s online help documentation under normal use and circumstances.

The Company’s arrangements generally include certain provisions for indemnifying customers against liabilities if its products or services infringe a third party’s intellectual property rights. To date, the Company has not incurred any material costs as a result of such obligations and has not accrued any material liabilities related to such obligations in the accompanying condensed consolidated financial statements.

The Company has also agreed to indemnify its directors and executive officers for costs associated with any fees, expenses, judgments, fines and settlement amounts incurred by any of these persons in any action or proceeding to

which any of those persons is, or is threatened to be, made a party by reason of the person's service as a director or officer, including any action by the Company, arising out of that person's services as the Company's director or officer or that person's services provided to any other company or enterprise at the Company's request. The Company maintains director and officer insurance coverage that would generally enable the Company to recover a portion of any future amounts paid. The Company may also be subject to indemnification obligations by law with respect to the actions of its employees under certain circumstances and in certain jurisdictions.

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New Accounting Pronouncements Adopted in Fiscal 2019

Topic 606

In May 2014, the FASB issued ASU 2014-09, which in addition to replacing the existing revenue recognition guidance, provides guidance on the recognition of costs related to obtaining customer contracts. The adoption was material to the Company's reported operating results and balance sheet for fiscal 2018 and 2017, as it requires additional types of costs to be capitalized and amortized over a longer period. The Company also recorded the related income tax effects, which did not have a material impact due to the Company's valuation allowance. The adoption had no impact to the Company's operating cash flow.

The adoption of ASU 2014-09 impacted the Company's previously reported results as follows (in millions, except per share data):

	Three Months Ended July 31, 2017			Six Months Ended July 31, 2017		
	As reported	Change	As adjusted	As reported	Change	As adjusted
Total revenues	$2,562	$15	$2,577	$4,949	$25	$4,974
Marketing and sales	1,171	(18)	1,153	2,280	(21)	2,259
Benefit from (provision for) income taxes	(13)	(4)	(17)	1	(7)	(6)
Net income	$18	$28	$46	$9	$38	$47
Diluted net income per share	$0.02	$0.04	$0.06	$0.01	$0.05	$0.06

The number of shares utilized to calculate the three and six months ended July 31, 2017 diluted net income per share was 729 million and 726 million, respectively.

The adoption of ASU 2014-09 impacted the Company's previously reported results as of January 31, 2018 as follows (in millions):

	As reported	Change	As adjusted
Accounts receivable, net	$ 3,918	$ 3	$ 3,921
Costs capitalized to obtain revenue contracts, net	461	210	671
Prepaid expenses and other current assets	390	81	471
Costs capitalized to obtain revenue contracts, noncurrent, net	413	692	1,105
Other assets, net	396	(12)	384
Accounts payable, accrued expenses and other liabilities	2,010	37	2,047
Unearned revenue	7,095	(100)	6,995
Other noncurrent liabilities	796	50	846
Stockholders' equity	9,389	987	10,376

ASU 2016-01

In January 2016, the FASB issued ASU 2016-01, which requires entities to measure equity instruments at fair value and recognize any changes in fair value within the statement of operations. The Company adopted ASU 2016-01 in the first quarter of fiscal 2019 on a prospective basis for privately held equity securities and a modified retrospective basis for publicly held equity investments. Upon adoption of ASU 2016-01, the Company reclassified approximately $13 million of unrealized gains related to its publicly traded equity investments and approximately $6 million reflecting the tax impact, from accumulated other comprehensive loss on the balance sheet to retained earnings. For the six months ended July 31, 2018 the Company recorded net unrealized gains of $344 million, which excludes recognized gains on the sale of investments of $10 million, which were recorded in the condensed consolidated statement of operations, and the Company anticipates additional volatility to the Company's statements of operations in future periods, due to changes in market prices of the Company's investments in publicly held equity investments and the valuation and timing of observable price changes and impairments of its investments in privately held securities.

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ASU 2016-16

In October 2016, the FASB issued ASU 2016-16, which requires entities to recognize the income tax consequences of an intra-entity transfer of an asset, other than inventory, when the transfer occurs. The Company adopted the standard in the first quarter of fiscal 2019 using the modified retrospective transition method and reclassified a cumulative-effect adjustment to reduce retained earnings as of the effective date of approximately $18 million.

Accounting Pronouncements Pending Adoption

In February 2016, the FASB issued Accounting Standards Update No. 2016-02, "Leases (Topic 842)" ("ASU 2016-02"), which requires lessees to record most leases on their balance sheets but recognize the expenses on their statements of operations in a manner similar to current accounting rules. ASU 2016-02 states that a lessee would recognize a lease liability for the obligation to make lease payments and a right-to-use asset for the right to use the underlying asset for the lease term. The new standard is effective for interim and annual periods beginning after December 15, 2018 on a modified retrospective basis. The Company is in the process of implementing changes to its systems, processes and controls, in conjunction with its review of existing lease agreements, in order to adopt the new standard in its first quarter of fiscal 2020. The Company expects its leases designated as operating leases in Note 14, “Commitments,” will be reported on the consolidated balance sheets upon adoption. The Company is currently evaluating the impact to its consolidated financial statements and as it relates to other aspects of the business.

In June 2016, the FASB issued Accounting Standards Update No. 2016-13 (ASU 2016-13) "Financial Instruments-Credit Losses (Topic 326): Measurement of Credit Losses on Financial Instruments," which requires the measurement and recognition of expected credit losses for financial assets held at amortized cost. ASU 2016-13 replaces the existing incurred loss impairment model with an expected loss methodology, which will result in more timely recognition of credit losses. ASU 2016-13 is effective for annual reporting periods, and interim periods within those years, beginning after December 15, 2019, and requires a cumulative effect adjustment to the balance sheet as of the beginning of the first reporting period in which the guidance is effective. The Company is currently in the process of evaluating the impact of the adoption of ASU 2016-13 on its consolidated financial statements in order to adopt the new standard in the first quarter of fiscal 2021.

In March 2018, the FASB issued Accounting Standards Update No. 2018-230 (ASU 2018-230) "Customer’s Accounting for Implementation Costs Incurred in a Cloud Computing Arrangement That Is a Service Contract; Disclosures for Implementation Costs Incurred for Internal-Use Software and Cloud Computing Arrangements," which aligns the accounting for implementation costs incurred in a hosting arrangement that is a service contract with the accounting for implementation costs incurred to develop or obtain internal-use software under ASC 350-40, in order to determine which costs to capitalize and recognize as an asset. ASU 2018-230 is effective for annual reporting periods, and interim periods within those years, beginning after December 15, 2019, and can be applied either prospectively to implementation costs incurred after the date of adoption or retrospectively to all arrangements. The Company is currently in the process of evaluating the impact of the adoption of ASU 2018-230 on its consolidated financial statements.

Reclassifications

Certain reclassifications to fiscal 2018 balances were made to conform to the current period presentation in the condensed consolidated balance sheets and condensed consolidated statement of operations. These reclassifications include other noncurrent liabilities, temporary equity, other income (expense) and gains on strategic investments, net.

2. Revenues

Disaggregation of Revenue

Subscription and Support Revenue by the Company's core service offerings

Subscription and support revenues consisted of the following (in millions):

	Three Months Ended July 31,		Six Months Ended July 31,	
	2018	2017	2018	2017
Sales Cloud	$1,004	$891	$1,969	$1,721
Service Cloud	892	700	1,740	1,356
Salesforce Platform and Other	712	463	1,287	887

Marketing and Commerce Cloud	452	329	874	628
	$3,060	$2,383	$5,870	$4,592

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Total Revenue by Geographic Locations

Revenues by geographical region consisted of the following (in millions):

	Three Months Ended July 31,		Six Months Ended July 31,	
	2018	2017	2018	2017
Americas	$2,338	$1,868	$4,439	$3,633
Europe	629	466	1,235	875
Asia Pacific	314	243	613	466
	$3,281	$2,577	$6,287	$4,974

Revenues by geography are determined based on the region of the Company's contracting entity, which may be different than the region of the customer. Americas revenue attributed to the United States was approximately 96 percent during the three and six months ended July 31, 2018 and 2017, respectively. No other country represented more than ten percent of total revenue during the three and six months ended July 31, 2018 and 2017.

Contract Balances

As described in Note 1, subscription and support revenue is generally recognized ratably over the contract term beginning on the commencement date of each contract. Under Topic 606 the timing and amount of revenue recognition may differ in certain situations from the revenue recognized under previous accounting guidance, which included a contingent revenue rule that limited subscription and support revenue to the customer invoice amount for the period of service (collectively billings). Under Topic 606, the Company records a contract asset when revenue recognized on a contract exceeds the billings. Contract assets were $228 million at July 31, 2018, which includes the acquired contract asset balance from the May 2018 MuleSoft acquisition. The contract assets were $81 million at January 31, 2018.

Unearned Revenue

Topic 606 introduced the concept of unearned revenue, which is substantially similar to deferred revenue under previous accounting guidance, except for the removal of the limitation on contingent revenue. The unearned revenue balance does not represent the total contract value of annual or multi-year, non-cancelable subscription agreements. Unearned revenue primarily consists of billings or payments received in advance of revenue recognition from subscription services, including software licenses, described above and is recognized as revenue when transfer of control to customers has occurred. The Company generally invoices customers in annual installments. The unearned revenue balance is influenced by several factors, including seasonality, the compounding effects of renewals, invoice duration, invoice timing, dollar size and new business linearity within the quarter.

The changes in unearned revenue were as follows (in millions):

	Three Months Ended July 31, 2018	Three Months Ended April 30, 2018
Unearned revenue, beginning of period	$6,201	$6,995
Billings and other*	2,875	2,211
Contribution from contract asset	31	(6)
Revenue recognized over time	(3,052)	(2,866)
Revenue recognized at a point in time	(229)	(140)
Unearned revenue from business combinations	57	7
Unearned revenue, end of period	$5,883	$6,201

*Other includes, for example, the impact of foreign currency translation

Revenue recognized over time is generally billed in advance and includes cloud services, the related support and fixed fee professional services. The majority of revenue recognized in each quarter for these services is from the beginning of period unearned revenue balance. Revenue recognized at a point in time includes professional services billed on a

time and materials basis, training classes and the portion of software license arrangements allocated to the on-premise performance obligation; these items are primarily billed, delivered and recognized within the same reporting period.

Remaining Performance Obligation (Formerly "Remaining Transaction Price")

Topic 606 also introduced the concept of remaining transaction price, which is different than unbilled deferred revenue under previous accounting guidance. Transaction price allocated to the remaining performance obligations represents

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contracted revenue that has not yet been recognized, which includes unearned revenue and unbilled amounts that will be recognized as revenue in future periods. Transaction price allocated to the remaining performance obligation is influenced by several factors, including seasonality, the timing of renewals, average contract terms and foreign currency exchange rates. Unbilled portions of the remaining performance obligations denominated in foreign currencies are revalued each period based on the period end exchange rates.

The Company applied the practical expedient in accordance with Topic 606 to exclude amounts related to performance obligations that are billed and recognized as they are delivered. This primarily consists of professional services contracts that are on a time-and-material basis.

Remaining performance obligation consisted of the following (in billions):

	Current	Noncurrent	Total
As of July 31, 2018*	$ 9.8	$ 11.2	$21.0

*Includes $200 million of acquired Remaining Performance Obligation from the MuleSoft May 2018 acquisition.

3. Investments

Marketable Securities

At July 31, 2018, marketable securities consisted of the following (in millions):

Investments classified as Marketable Securities	Amortized Cost	Unrealized Gains	Unrealized Losses	Fair Value
Corporate notes and obligations	$ 676	$ 0	$ (9)	$667
U.S. treasury securities	90	0	(2)	88
Mortgage backed obligations	80	0	(2)	78
Asset backed securities	158	0	(2)	156
Municipal securities	39	0	(1)	38
Foreign government obligations	53	0	(1)	52
U.S. agency obligations	4	0	0	4
Covered bonds	25	0	0	25
Total marketable securities	$ 1,125	$ 0	$ (17)	$1,108

At January 31, 2018, marketable securities consisted of the following (in millions):

Investments classified as Marketable Securities	Amortized Cost	Unrealized Gains	Unrealized Losses	Fair Value
Corporate notes and obligations	$ 1,223	$ 1	$ (7)	$1,217
U.S. treasury securities	196	0	(2)	194
Mortgage backed obligations	100	0	(1)	99
Asset backed securities	251	0	(1)	250
Municipal securities	53	0	(1)	52
Foreign government obligations	87	0	(1)	86
U.S. agency obligations	19	0	0	19
Commercial paper	11	0	0	11
Covered bonds	51	0	(1)	50
Total marketable securities	$ 1,991	$ 1	$ (14)	$1,978

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The contractual maturities of the investments classified as marketable securities are as follows (in millions):

	As of	
	July 31, 2018	January 31, 2018
Due within 1 year	$157	$ 395
Due in 1 year through 5 years	948	1,579
Due in 5 years through 10 years	3	4
	$1,108	$ 1,978

As of July 31, 2018, the following marketable securities were in an unrealized loss position (in millions):

	Less than 12 Months		12 Months or Greater		Total	
	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses
Corporate notes and obligations	$584	$ (9)	$38	$ 0	$622	$ (9)
U.S. treasury securities	82	(2)	6	0	88	(2)
Mortgage backed obligations	62	(1)	15	(1)	77	(2)
Asset backed securities	148	(2)	9	0	157	(2)
Municipal securities	27	(1)	10	0	37	(1)
Foreign government obligations	52	(1)	0	0	52	(1)
	$955	$ (16)	$78	$ (1)	$1,033	$ (17)

The unrealized losses for each of the fixed rate marketable securities were less than $1 million. The Company does not believe any of the unrealized losses represent an other-than-temporary impairment based on its evaluation of available evidence as of July 31, 2018, such as the Company's intent to hold and whether it is more likely than not that the Company will be required to sell the investment before recovery of the investment's amortized basis. The Company expects to receive the full principal and interest on all of these marketable securities.

Investment Income

Investment income consists of interest income, realized gains and realized losses on the Company’s cash, cash equivalents and marketable securities. The components of investment income are presented below (in millions):

	Three Months Ended July 31,		Six Months Ended July 31,	
	2018	2017	2018	2017
Interest income	$12	$ 8	$32	$14
Realized gains	0	1	1	1
Realized losses	0	0	(5)	(1)
Investment income	$12	$ 9	$28	$14

Reclassification adjustments out of accumulated other comprehensive income into investment income were immaterial for the three and six months ended July 31, 2018 and 2017.

Strategic Investments

Strategic investments by form and measurement category as of July 31, 2018 were as follows (in millions):

	Measurement Category			Total
	Fair Value	Measurement Alternative	Other (1)	
Equity securities	$430	$ 667	$ 36	$1,133
Debt securities	53	0	16	69
Balance as of July 31, 2018	$483	$ 667	$ 52	$1,202

(1) Other includes the Company's investments accounted for under the equity method of accounting or amortized cost.

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Measurement Alternative Adjustments

Privately held equity investments, which are included in the table above, accounted for under the measurement alternative as of July 31, 2018 were as follows (in millions):

	Three Months Ended July 31, 2018	Six Months Ended July 31, 2018
Carrying amount, beginning of period	$ 554	$ 548
Adjustments related to privately held equity investments:		
Net additions	19	30
Unrealized gains, losses and impairments on strategic investments	94	89
Carrying amount, end of period	$ 667	$ 667

Gains (losses) on strategic investments, net

Gains and losses recognized in the three and six months ended July 31, 2018 and 2017 were as follows (in millions):

	Three Months Ended July 31,		Six Months Ended July 31,	
	2018	2017	2018	2017
Net gains recognized on publicly traded securities	$65	$0	$276	$0
Net gains (losses) recognized on privately held securities	78	(8)	78	(5)
Gains (losses) on strategic investments, net	$143	$(8)	$354	$(5)

Net gains recognized in the three and six months ended July 31, 2018 for investments still held as of July 31, 2018 were $142 million and $344 million, respectively. This excludes recognized gains on the sale of investments for the three and six months ended July 31, 2018 of $1 million and $10 million, respectively.

4. Derivatives

Details on outstanding foreign currency derivative contracts are presented below (in millions):

	As of July 31, 2018	January 31, 2018
Notional amount of foreign currency derivative contracts	$1,566	$1,871
Fair value of foreign currency derivative contracts	(1)	12

The fair value of the Company’s outstanding derivative instruments not designated as hedging instruments are summarized below (in millions):

	Balance Sheet Location	As of July 31, 2018	January 31, 2018
Foreign currency derivative contracts	Prepaid expenses and other current assets	$1	$ 18

Gains/losses on derivative instruments not designated as hedging instruments recorded in Other income in the condensed consolidated statements of operations during the three and six months ended July 31, 2018 and 2017, respectively, are summarized below (in millions):

	Three Months Ended July 31,		Six Months Ended July 31,	
	2018	2017	2018	2017

Foreign currency derivative contracts	$(10)	$ 3	$10	$ 10

5. Fair Value Measurement

The Company uses a three-tier fair value hierarchy, which prioritizes the inputs used in the valuation methodologies in measuring fair value:

Level 1. Quoted prices (unadjusted) in active markets for identical assets or liabilities.

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Level 2. Significant other inputs that are directly or indirectly observable in the marketplace.

Level 3. Significant unobservable inputs which are supported by little or no market activity.

All of the Company's cash equivalents, marketable securities and foreign currency derivative contracts are classified within Level 1 or Level 2 because the Company's cash equivalents, marketable securities and foreign currency derivative contracts are valued using quoted market prices or alternative pricing sources and models utilizing observable market inputs.

The following table presents information about the Company's assets that are measured at fair value as of July 31, 2018 and indicates the fair value hierarchy of the valuation (in millions):

Description	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)	Balance as of July 31, 2018
Cash equivalents (1):				
Time deposits	$ 0	$ 253	$ 0	$ 253
Money market mutual funds	1,364	0	0	1,364
Marketable securities:				
Corporate notes and obligations	0	667	0	667
U.S. treasury securities	0	88	0	88
Mortgage backed obligations	0	78	0	78
Asset backed securities	0	156	0	156
Municipal securities	0	38	0	38
Foreign government obligations	0	52	0	52
U.S. agency obligations	0	4	0	4
Covered bonds	0	25	0	25
Foreign currency derivative contracts (2)	0	1	0	1
Total assets	$ 1,364	$ 1,362	$ 0	$ 2,726

(1)Included in "cash and cash equivalents" in the accompanying condensed consolidated balance sheet as of July 31, 2018, in addition to $702 million of cash.

(2)Included in "prepaid expenses and other current assets" in the accompanying condensed consolidated balance sheet as of July 31, 2018.

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The following table presents information about the Company's assets that are measured at fair value as of January 31, 2018 and indicates the fair value hierarchy of the valuation (in millions):

Description	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)	Balance as of January 31, 2018
Cash equivalents (1):				
Time deposits	$ 0	$ 543	$ 0	$ 543
Money market mutual funds	1,389	0	0	1,389
Marketable securities:				
Corporate notes and obligations	0	1,217	0	1,217
U.S. treasury securities	0	194	0	194
Mortgage backed obligations	0	99	0	99
Asset backed securities	0	250	0	250
Municipal securities	0	52	0	52
Foreign government obligations	0	86	0	86
U.S. agency obligations	0	19	0	19
Commercial paper	0	11	0	11
Covered bonds	0	50	0	50
Foreign currency derivative contracts (2)	0	18	0	18
Total assets	$ 1,389	$ 2,539	$ 0	$ 3,928

(1)Included in "cash and cash equivalents" in the accompanying condensed consolidated balance sheet as of January 31, 2018, in addition to $611 million of cash.

(2)Included in "prepaid expenses and other current assets" in the accompanying condensed consolidated balance sheet as of January 31, 2018.

6. Property and Equipment

Property and Equipment

Property and equipment, net consisted of the following (in millions):

	As of	
	July 31, 2018	January 31, 2018
Land	$184	$184
Buildings and building improvements	629	626
Computers, equipment and software	1,700	1,629
Furniture and fixtures	156	139
Leasehold improvements	952	825
Property and equipment, gross	3,621	3,403
Less accumulated depreciation and amortization	(1,635)	(1,456)
Property and equipment, net	$1,986	$1,947

Depreciation and amortization expense totaled $101 million and $95 million during the three months ended July 31, 2018 and 2017, respectively, and $190 million and $183 million during the six months ended July 31, 2018 and 2017, respectively.

Computers, equipment and software at July 31, 2018 and January 31, 2018 included a total of $709 million and $709 million acquired under capital lease agreements, respectively. Accumulated amortization relating to computers, equipment and software acquired under capital leases totaled $484 million and $450 million, respectively, at July 31, 2018 and January 31, 2018. Amortization of assets acquired under capital leases is included in depreciation and

amortization expense.

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7. Business Combinations

MuleSoft

In May 2018, the Company acquired all outstanding stock of MuleSoft, which provides a platform for building application networks that connect enterprise apps, data and devices, across any cloud and on-premise solution. The Company has included the financial results of MuleSoft in the consolidated financial statements from the date of acquisition. The transaction costs associated with its acquisition for the six months ended July 31, 2018, were approximately $24 million and were recorded in general and administrative expense. The acquisition date fair value of the consideration transferred for MuleSoft was approximately $6.4 billion, which consisted of the following (in millions):

	Fair Value
Cash	$4,860
Common stock issued	1,178
Fair value of stock options and restricted stock awards assumed	387
Total	$6,425

The fair value of the stock options assumed by the Company was determined using the Black-Scholes option pricing model. The share conversion ratio of 0.3680 was applied to convert MuleSoft's outstanding equity awards for MuleSoft's common stock into equity awards for shares of the Company's common stock.

The following table summarizes the fair values of assets acquired and liabilities assumed as of the date of acquisition (in millions):

	Fair Value
Cash and cash equivalents	$59
Marketable securities	231
Accounts receivable	69
Contract asset	122
Other current and noncurrent assets	29
Acquired customer contract asset, current and noncurrent	61
Intangible assets	1,279
Goodwill	4,816
Accounts payable, accrued expenses and other liabilities, current and noncurrent	(40)
Unearned revenue	(57)
Deferred tax liability	(144)
Net assets acquired	$6,425

The excess of purchase consideration over the fair value of net tangible and identifiable intangible assets acquired was recorded as goodwill. The fair values assigned to tangible and identifiable intangible assets acquired and liabilities assumed are based on management's estimates and assumptions. The deferred tax liability established was primarily a result of the difference in the book basis and tax basis related to the identifiable intangible assets. The fair values of assets acquired and liabilities assumed, including current and noncurrent income taxes payable and deferred taxes, may be subject to change as additional information is received and certain tax returns are finalized. Accordingly, the provisional measurements of fair value of the income taxes payable and deferred taxes set forth above are subject to change. The Company expects to finalize the valuation as soon as practicable, but not later than one year from the acquisition date.

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The following table sets forth the components of identifiable intangible assets acquired and their estimated useful lives as of the date of acquisition (in millions):

	Fair Value	Useful Life
Developed technology	$224	4 years
Customer relationships	1,046	8 years
Other purchased intangible assets	9	1 year
Total intangible assets subject to amortization	$1,279	

Developed technology represents the fair value of MuleSoft's Anypoint technology. Customer relationships represent the fair values of the underlying relationships with MuleSoft customers. The goodwill balance is primarily attributed to the assembled workforce and expanded market opportunities when integrating MuleSoft's Anypoint technology with the Company’s other offerings. The goodwill balance is not deductible for U.S. income tax purposes.

The Company assumed unvested options and restricted stock with a fair value of $824 million. Of the total consideration, $387 million was allocated to the purchase consideration and $437 million was allocated to future services and will be expensed over the remaining service periods on a straight-line basis.

The amounts of revenue and pretax income of MuleSoft included in the Company’s condensed consolidated statement of operations from the acquisition date in May 2018 to the period ending July 31, 2018 are as follows (in millions):

Total revenues	$122
Pretax loss	(105)

The following pro forma financial information summarizes the combined results of operations for the Company and MuleSoft, as though the companies were combined as of the beginning of the Company’s fiscal 2017.

The unaudited pro forma financial information was as follows (in millions):

	Three Months Ended July 31,		Six Months Ended July 31,	
	2018	2017	2018	2017
Total revenues	$3,281	$2,645	$6,371	$5,094
Pretax income (loss)	269	(78)	596	(262)
Net income (loss)	201	(96)	486	(134)

The pro forma financial information for all periods presented above has been calculated after adjusting the results of MuleSoft to reflect the business combination accounting effects resulting from this acquisition, including the amortization expense from acquired intangible assets and the stock-based compensation expense for unvested stock options and restricted stock awards assumed as well as the interest expense associated with the Company's issuance of debt prior to the acquisition as though the acquisition occurred as of the beginning of the Company’s fiscal year 2018, which was the driver of the net losses for the three and six months ended July 31, 2017. The historical consolidated financial statements have been adjusted in the pro forma combined financial statements to give effect to pro forma events that are directly attributable to the business combination and factually supportable. The pro forma financial information is for informational purposes only and is not indicative of the results of operations that would have been achieved if the acquisition had taken place at the beginning of the Company’s fiscal 2018.

The pro forma financial information for the six months ended July 31, 2018 and 2017 combines the historical results of the Company for the six months ended July 31, 2018 and 2017, the adjusted historical results of MuleSoft for the six months ended July 31, 2018 and 2017, due to differences in reporting periods and considering the date the Company acquired MuleSoft, and the effects of the pro forma adjustments listed above. Prior to being acquired, MuleSoft's fiscal year concluded on December 31. Net income for the six months ended July 31, 2017 above includes a discrete tax benefit of $139 million, resulting from a partial release of valuation allowance in connection with the acquisition. The net deferred tax liability from the acquisition of MuleSoft provided a source of additional income to support the realizability of the Company's pre-existing deferred tax assets. The deferred tax liability considered the 21 percent corporate tax rate enacted by the Tax Act.

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CloudCraze

In April 2018, the Company acquired all outstanding stock of CloudCraze LLC ("CloudCraze"), for consideration consisting of cash and equity awards assumed. CloudCraze is a commerce platform that allows businesses to generate online revenue and scale for growth. CloudCraze delivers interactions across commerce, sales, marketing and service. The Company has included the financial results of CloudCraze in the consolidated financial statements from the date of acquisition, which have not been material to date. The transaction costs associated with the acquisition were not material.

The acquisition date fair value consideration transferred for CloudCraze was approximately $190 million, which consisted of cash and the fair value of stock options and restricted stock awards assumed. The Company recorded approximately $58 million for developed technology and customer relationships with estimated useful lives of one to seven years. The Company recorded approximately $134 million of goodwill which is primarily attributed to the assembled workforce and expanded market opportunities from integrating CloudCraze's technology with the Company's other offerings. The goodwill balance is deductible for U.S. income tax purposes. The fair value of current and noncurrent income taxes payable and deferred taxes, may be subject to change as additional information is received and certain tax returns are finalized. The Company expects to finalize the valuation as soon as practicable, but not later than one year from the acquisition date.

8. Intangible Assets Acquired Through Business Combinations and Goodwill

Intangible assets acquired through business combinations

Intangible assets acquired through business combinations are as follows (in millions):

	Intangible Assets, Gross			Accumulated Amortization			Intangible Assets, Net		Weighted
	Jan 31, 2018	Additions and retirements, net	July 31, 2018	Jan 31, 2018	Expense and retirements, net	July 31, 2018	Jan 31, 2018	July 31, 2018	Average Remaining Useful Life (Years)
Acquired developed technology	$1,027	$ 241	$1,268	$(677)	$ (91)	$(768)	$350	$500	3.0
Customer relationships	831	1,086	1,917	(359)	(93)	(452)	472	1,465	6.7
Other (1)	53	2	55	(48)	(4)	(44)	5	11	1.9
Total	$1,911	$ 1,329	$3,240	$(1,084)	$ (188)	$(1,264)	$827	$1,976	5.7

(1)Included in other are trade names, trademarks and territory rights.

Amortization of intangible assets resulting from business combinations for the three months ended July 31, 2018 and 2017 was $119 million and $74 million, respectively, and for the six months ended July 31, 2018 and 2017 was $188 million and $149 million, respectively.

The expected future amortization expense for intangible assets as of July 31, 2018 is as follows (in millions):

Fiscal Period:	
Remaining six months of Fiscal 2019	$235
Fiscal 2020	426
Fiscal 2021	368
Fiscal 2022	305
Fiscal 2023	186
Thereafter	456
Total amortization expense	$1,976

Goodwill

The changes in the carrying amounts of goodwill, which is generally not deductible for tax purposes, were as follows (in millions):

Balance as of January 31, 2018	$7,314
CloudCraze Acquisition	134

Mulesoft Acquisition	4,816
Adjustments of acquisition date fair values, including the effect of foreign currency translation	(10)
Balance as of July 31, 2018	$12,254

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9. Debt

The carrying values of the Company's borrowings were as follows (in millions):

Instrument	Date of issuance	Maturity date	Effective interest rate for the three months ended July 31, 2018	July 31, 2018	January 31, 2018
2021 Term Loan	May 2018	May 2021	2.88%	$499	$ 0
2023 Senior Notes	April 2018	April 2023	3.26%	992	0
2028 Senior Notes	April 2018	April 2028	3.70%	1,487	0
2019 Term Loan	July 2016	July 2019	2.87%	499	498
Loan assumed on 50 Fremont	February 2015	June 2023	3.75%	199	199
0.25% Convertible Senior Notes	March 2013	April 2018	2.53% (1)	0	1,023
Total carrying value of debt				3,676	1,720
Less current portion of debt				(503)	(1,025)
Total noncurrent debt				$3,173	$ 695

(1) From February 1, 2018 through maturity, the effective interest rate for the Convertible Senior Notes was 2.53%.

Each of the Company's debt agreements requires it to maintain compliance with certain debt covenants, all of which the Company was in compliance with as of July 31, 2018.

The expected future principal payments for all borrowings as of July 31, 2018 is as follows (in millions):

Fiscal period:	
Remaining six months of Fiscal 2019	$2
Fiscal 2020	504
Fiscal 2021	4
Fiscal 2022	504
Fiscal 2023	4
Thereafter	2,682
Total principal outstanding	$3,700

2021 Term Loan

In April 2018, the Company entered into a new three-year unsecured term loan with Bank of America, N.A. and certain other institutional lenders for $500 million (“2021 Term Loan”) that matures in May 2021. The net proceeds of the 2021 Term Loan were for the purpose of partially funding the acquisition of MuleSoft and were received in May 2018. For the three and six months ended July 31, 2018, total interest expense recognized was $4 million. Accrued interest on the 2021 Term Loan was immaterial as of July 31, 2018. As of July 31, 2018, the noncurrent outstanding principal portion was $500 million.

2023 Senior Notes

In April 2018, the Company issued an aggregate principal amount of $1.0 billion in senior notes that will mature in April 2023 and bear interest at a fixed rate of 3.25 percent per annum ("2023 Senior Notes"). The interest is payable semi-annually in April and October of each year, commencing in October 2018. The Company incurred issuance costs of $8 million in connection with the 2023 Senior Notes that, along with the debt discount upon issuance, are being amortized to interest expense over the term of the 2023 Senior Notes. The 2023 Senior Notes are unsecured and rank equally in right of payment with all of the other senior unsecured indebtedness. For the three and six months ended July 31, 2018, total interest expense recognized was $8 million and $10 million, respectively. Accrued interest on the 2023 Senior Notes was $10 million as of July 31, 2018. As of July 31, 2018, the noncurrent outstanding principal portion was $1.0 billion.

2028 Senior Notes

In April 2018, the Company issued an aggregate principal amount of $1.5 billion in senior notes that will mature in April 2028 and bear interest at a fixed rate of 3.70 percent per annum ("2028 Senior Notes"). The interest is payable semi-annually in April and October of each year, commencing in October 2018. The Company incurred issuance costs of $13 million in connection with the 2028 Senior Notes that, along with the debt discount upon issuance, are being amortized to interest expense over the term of the 2028 Senior Notes. The 2028 Senior Notes are unsecured and rank equally in right of payment with all of the other senior unsecured indebtedness. For the three and six months ended July 31, 2018, total interest expense recognized

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was $14 million and $17 million, respectively. Accrued interest on the 2028 Senior Notes was $17 million as of July 31, 2018. As of July 31, 2018, the noncurrent outstanding principal portion was $1.5 billion.

Bridge Facility

In March 2018, the Company entered into a commitment letter, pursuant to which certain lenders agreed to provide a senior unsecured 364-day bridge loan facility of up to $3.0 billion (the "Bridge Facility") for the purpose of providing the financing to support the Company's acquisition of MuleSoft.

Under the terms of the commitment letter, the Bridge Facility was terminated upon execution of the 2023 Senior Notes, 2028 Senior Notes and 2021 Term Loan in April 2018. For the six months ended July 31, 2018, the Company incurred costs in connection with the Bridge Facility of approximately $11 million that were recorded to interest expense.

2019 Term Loan

In July 2016, the Company entered into a credit agreement ("Term Loan Credit Agreement") with Bank of America, N.A. and certain other institutional lenders for a $500 million term loan facility ("2019 Term Loan") that matures in July 2019. In April 2018, the Company modified the Term Loan Credit Agreement with substantially the same terms, including the principal amount and maturity date. The Company accounted for the new 2019 Term Loan as a modification. No incremental fees were paid related to the modification of the 2019 Term Loan.

Interest on the 2019 Term Loan is due and payable in arrears quarterly for loans bearing interest at a rate based on the base rate and at the end of an interest period in the case of loans bearing interest at the adjusted LIBOR rate.

For the three months ended July 31, 2018 and 2017, total interest expense recognized was $4 million and $3 million, respectively. For the six months ended July 31, 2018 and 2017, total interest expense recognized was $7 million and $5 million, respectively. Accrued interest on the 2019 Term Loan was immaterial as of July 31, 2018. As of July 31, 2018, the current outstanding principal portion was $500 million.

Loan Assumed on 50 Fremont

The Company assumed a $200 million loan with the acquisition of 50 Fremont in San Francisco, California ("Loan"). The Loan bears an interest rate of 3.75% per annum and is due in June 2023. Starting in July 2018, principal and interest payments are required, with the remaining principal due at maturity. For the three months ended July 31, 2018 and 2017, total interest expense recognized was $2 million and $2 million, respectively. For the six months ended July 31, 2018 and 2017, total interest expense recognized was $4 million and $4 million, respectively. Accrued interest on the Loan was immaterial as of July 31, 2018. As of July 31, 2018, the current and noncurrent outstanding principal portion was $4 million and $196 million, respectively. The Loan can be prepaid at any time subject to a yield maintenance fee.

Convertible Senior Notes

In March 2013, the Company issued at par value $1.15 billion of 0.25% convertible senior notes (the "0.25% Senior Notes", or "Notes") due in April 2018. The Notes matured in April 2018 and the Company repaid $1.0 billion in cash of principal balance of the Notes during the Company's first quarter of fiscal 2019. The Company also distributed approximately 7 million shares of the Company's common stock to noteholders during fiscal 2019, which represents the conversion value in excess of the principal amount.

To minimize the impact of potential economic dilution upon conversion of the Notes, also in March 2013, the Company entered into convertible note hedge transactions with respect to its common stock. The Company received approximately 7 million shares of the Company's common stock from the exercise of the notes hedges related to the 0.25% Senior Notes during this same period.

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Warrants

In March 2013, the Company entered into a warrants transaction (“0.25% Warrants”), whereby the Company sold warrants to acquire, subject to anti-dilution adjustments, shares of the Company’s common stock. The 0.25% Warrants were separate transactions entered into by the Company and were not part of the terms of the 0.25% Senior Notes or the related note hedges. In June 2018, the Company entered into agreements with each of the 0.25% Warrants counterparties to amend and early settle the 0.25% Warrants prior to their scheduled expiration beginning in July 2018. As a result of this amendment, during the three months ended July 31, 2018, the Company issued, in the aggregate, approximately 6 million shares to the counterparties to settle, via a net share settlement, the entirety of the 0.25% Warrants, which increased the shares used in computing basic net income per share by 2 million and 1 million for the three and six months ended July 31, 2018, respectively.

Revolving Credit Facility

In April 2018, the Company entered into a Second Amended and Restated Credit Agreement ("Revolving Loan Credit Agreement") with Wells Fargo Bank, National Association, and certain other institutional lenders that provides for $1.0 billion unsecured revolving credit facility (“Credit Facility”) that matures in April 2023. The Revolving Loan Credit Agreement amended and restated the Company’s existing revolving credit facility dated July 2016. The Company may use the proceeds of future borrowings under the Credit Facility for refinancing other indebtedness, working capital, capital expenditures and other general corporate purposes, including permitted acquisitions.

There were no outstanding borrowings under the Credit Facility as of July 31, 2018. The Company continues to pay a commitment fee on the available amount of the Credit Facility, which is included within interest expense in the Company's condensed consolidated statement of operations.

Interest Expense on Debt

The following table sets forth total interest expense recognized related to debt (in millions):

	Three Months Ended July 31,		Six Months Ended July 31,	
	2018	2017	2018	2017
Contractual interest expense	$31	$ 6	$42	$ 11
Amortization of debt issuance costs	1	2	13	3
Amortization of debt discount	0	6	4	13
	$32	$ 14	$59	$ 27

10. Other Balance Sheet Accounts

Prepaid Expenses and Other Current Assets

Prepaid expenses and other current assets consisted of the following (in millions):

	As of	
	July 31, 2018	January 31, 2018
Prepaid income taxes	$15	$ 33
Other taxes receivable	39	33
Prepaid expenses and other current assets	672	405
	$726	$ 471

Capitalized Software, net

Capitalized software, net at July 31, 2018 and January 31, 2018 was $145 million and $146 million, respectively. Accumulated amortization relating to capitalized software, net totaled $363 million and $326 million, respectively, at July 31, 2018 and January 31, 2018.

Capitalized internal-use software amortization expense totaled $19 million and $19 million for the three months ended July 31, 2018 and 2017, respectively, and $38 million and $37 million for the six months ended July 31, 2018 and 2017, respectively.

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Other Assets, net

Other assets, net consisted of the following (in millions):

	As of July 31, 2018	January 31, 2018
Deferred income taxes, noncurrent, net	$43	$ 36
Long-term deposits	25	24
Domain names and patents, net	33	23
Customer contract assets resulting from business combinations (1)	170	159
Other	188	142
	$459	$ 384

(1) Customer contract assets resulting from business combinations reflects the fair value of future billings of amounts that are contractually committed by acquired companies' existing customers as of the acquisition date.

Accounts Payable, Accrued Expenses and Other Liabilities

Accounts payable, accrued expenses and other liabilities consisted of the following (in millions):

	As of July 31, 2018	January 31, 2018
Accounts payable	$201	$ 76
Accrued compensation	674	1,001
Accrued income and other taxes payable	303	306
Capital lease obligation, current	205	103
Other current liabilities	700	561
	$2,083	$ 2,047

Other Noncurrent Liabilities

Other noncurrent liabilities consisted of the following (in millions):

	As of July 31, 2018	January 31, 2018
Deferred income taxes and income taxes payable	$136	$ 121
Financing obligation - leased facility	197	198
Long-term lease liabilities and other	320	527
	$653	$ 846

11. Stockholders’ Equity

The Company maintains the following stock plans: the ESPP, the 2013 Equity Incentive Plan and the 2014 Inducement Equity Incentive Plan (“2014 Inducement Plan”).

As of July 31, 2018 and January 31, 2018, $62 million and $63 million, respectively, was withheld on behalf of employees for future purchases under the ESPP and is recorded in accounts payable, accrued expenses and other liabilities.

From February 1, 2006 through July 2013, options issued had a term of five years. After July 2013, options issued have a term of seven years.

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The fair value of each stock option grant was estimated on the date of grant using the Black-Scholes option pricing model with the following assumptions and fair value per share:

	Three Months Ended July 31,		Six Months Ended July 31,	
Stock Options	2018	2017	2018	2017
Volatility	27.8 %	30.8 %	27.8 - 28 %	30.8 - 31.4 %
Estimated life	3.5 years	3.5 years	3.5 years	3.5 years
Risk-free interest rate	2.7 - 2.8 %	1.6 %	2.5 -2.8 %	1.4 - 1.6 %
Weighted-average fair value per share of grants	$32.35	$22.20	$28.69	$21.08

The fair value of each ESPP shares was estimated on the first day of the offering period using the Black-Scholes option pricing model with the following assumptions and fair value per share:

	Three Months Ended July 31,	
ESPP	2018	2017
Volatility	22.5 - 23.5 %	26.8 - 27.6 %
Estimated life	0.75 years	0.75 years
Risk-free interest rate	1.97 - 2.27 %	1.1 - 1.2 %
Weighted-average fair value per share of grants	$32.26	$21.13

The Company estimated its future stock price volatility considering both its observed option-implied volatilities and its historical volatility calculations. Management believes this is the best estimate of the expected volatility over the expected life of its stock options and stock purchase rights.

The estimated life for the stock options was based on an analysis of historical exercise activity. The risk-free interest rate is based on the rate for a U.S. government security with the same estimated life at the time of the option grant and the stock purchase rights.

The estimated forfeiture rate applied is based on historical forfeiture rates. The Company does not anticipate paying any cash dividends in the foreseeable future and therefore uses an expected dividend yield of zero in the option pricing model.

In the first quarter and second quarter of fiscal 2019, the Company granted additional performance-based restricted stock unit awards to certain employees, including the Chairman of the Board and Co-Chief Executive Officer and other senior executives. The performance-based restricted stock unit awards are subject to vesting based on a performance-based condition and a service-based condition. At the end of the three-year service period, based on the Company's share price performance, these performance-based restricted stock units will vest in a percentage of the target number of shares between 0 and 200%, depending on the extent the performance condition is achieved.

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Stock activity excluding the ESPP is as follows:

		Options Outstanding		
	Shares Available for Grant (in thousands)	Outstanding Stock Options (in thousands)	Weighted-Average Exercise Price	Aggregate Intrinsic Value (in millions)
Balance as of January 31, 2018	50,313	21,735	$ 65.96	
Increase in shares authorized:				
2013 Equity Incentive Plan	40,000	0	0.00	
Assumed equity plans	7,434	0	0.00	
Options granted under all plans	(12,571)	12,571	71.51	
Restricted stock activity	(18,637)	0	0.00	
Performance-based restricted stock units	(1,911)	0	0.00	
Stock grants to board and advisory board members	(81)	0	0.00	
Exercised	0	(5,344)	42.84	
Plan shares expired	(49)	0	0.00	
Canceled	794	(794)	81.06	
Balance as of July 31, 2018	65,292	28,168	$ 72.40	$ 1,825
Vested or expected to vest		26,081	$ 70.69	$ 1,735
Exercisable as of July 31, 2018		12,319	$ 54.96	$ 1,013

The total intrinsic value of the options exercised during the six months ended July 31, 2018 and 2017 was $463 million and $235 million, respectively. The intrinsic value is the difference between the current market value of the stock and the exercise price of the stock option.

The weighted-average remaining contractual life of vested and expected to vest options is approximately 5 years.

As of July 31, 2018, options to purchase 12 million shares were vested at a weighted average exercise price of $54.96 per share and had a remaining weighted-average contractual life of approximately 4 years. The total intrinsic value of these vested options as of July 31, 2018 was $1.0 billion.

During the six months ended July 31, 2018, the Company recognized stock-based expense related to its equity plans for employees and non-employee directors of $603 million. As of July 31, 2018, the aggregate stock compensation remaining to be amortized to costs and expenses was approximately $2.9 billion. The Company will amortize this stock compensation balance as follows: $660 million during the remaining six months of fiscal 2019; $1.0 billion during fiscal 2020; $714 million during fiscal 2021; $400 million during fiscal 2022; $67 million during fiscal 2023 and $8 million thereafter. The expected amortization reflects only outstanding stock awards as of July 31, 2018 and assumes no forfeiture activity.

The aggregate stock compensation remaining to be amortized to costs and expenses will be recognized over a weighted average period of 2 years.

The following table summarizes information about stock options outstanding as of July 31, 2018:

	Options Outstanding			Options Exercisable	
Range of Exercise Prices	Number Outstanding (in thousands)	Weighted-Average Remaining Contractual Life (Years)	Weighted-Average Exercise Price	Number of Shares (in thousands)	Weighted-Average Exercise Price
$0.36 to $21.54	3,979	6.7	$ 12.40	2,082	$ 9.87
$22.12 to $59.34	6,980	3.4	53.60	6,101	54.70
$59.37 to $75.01	1,257	5.6	68.84	476	71.04

$75.57	4,326	5.3	75.57	1,362	75.57
$76.48 to $81.88	4,041	4.4	80.70	2,209	80.75
$82.08 to $114.13	1,205	6.1	95.72	89	85.67
$118.04 to $146.87	6,380	6.6	119.27	0	0.00
	28,168	5.3	$ 72.40	12,319	$ 54.96

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Restricted stock activity is as follows:

	Restricted Stock Outstanding		
	Outstanding (in thousands)	Weighted Average Grant Date Fair Value	Aggregate Intrinsic Value (in millions)
Balance as of January 31, 2018	19,018	$ 77.85	
Granted - restricted stock units and awards	10,663	119.88	
Granted - performance-based stock units	453	118.59	
Canceled	(1,050)	84.15	
Vested and converted to shares	(4,180)	74.15	
Balance as of July 31, 2018	24,904	$ 96.86	$ 3,416
Expected to vest	21,319		$ 2,924

The restricted stock, which upon vesting entitles the holder to one share of common stock for each share of restricted stock, has an exercise price of $0.001 per share, which is equal to the par value of the Company’s common stock, and generally vests over four years. The total fair value of shares vested during the six months ended July 31, 2018 and 2017 was $511 million and $338 million, respectively.

Common Stock

The following number of shares of common stock were reserved and available for future issuance at July 31, 2018 (in thousands):

Options outstanding	28,168
Restricted stock awards and units and performance-based stock units outstanding	24,904
Stock available for future grant:	
2013 Equity Incentive Plan	64,912
2014 Inducement Plan	273
Amended and Restated 2004 Employee Stock Purchase Plan	5,743
Acquired equity plans	107
	124,107

12. Income Taxes

Effective Tax Rate

The Company computes its year-to-date provision for income taxes by applying the estimated annual effective tax rate to year to date pretax income or loss and adjusts the provision for discrete tax items recorded in the period. For the six months ended July 31, 2018, the Company reported a tax benefit of $27 million on a pretax income of $616 million, which resulted in a negative effective tax rate of 4 percent. Included in this tax amount was a discrete tax benefit of $139 million from a partial release of the valuation allowance in connection with the acquisition of MuleSoft. The net deferred tax liability from the acquisition of MuleSoft provided a source of additional income to support the realizability of the Company's pre-existing deferred tax assets and as a result, the Company released a portion of its valuation allowance. The tax benefit associated with the release of the valuation allowance was partially offset by income taxes in profitable jurisdictions outside of the United States.

On July 24, 2018, the U.S. Ninth Circuit Court of Appeals reversed the U.S. Tax Court's decision in Altera Corp v. Commissioner, and upheld the regulation that required stock-based compensation to be included in an inter-company cost-sharing arrangement. The decision was withdrawn on August 7, 2018, and the Company reassessed its current tax position, which resulted in a change to its deferred taxes. The related income tax effects were offset by the valuation allowance.

In December 2017, the Tax Act was enacted into law, significantly changing income tax law that affects U.S. corporations. Key changes included a corporate tax rate reduction from 35 percent to 21 percent effective January 1, 2018,

expensing of certain qualified property, significant changes to the U.S international tax system such as a one-time transition tax on accumulated foreign earnings, and how foreign earnings are subject to U.S. tax. Due to the timing of the Tax Act and additional guidance and interpretations that may be issued in the future, the Company has not completed its analysis of the effects of the Tax Act and recorded provisional estimates in the period ended January 31, 2018. The provisional estimates will

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be adjusted during the measurement period defined under SAB 118, based upon the Company's ongoing analysis of its data and tax positions along with new guidance from regulators and interpretations of the law. During the three months ended July 31, 2018, the Company adjusted certain items related to the provisional estimates. These adjustments did not significantly impact the Company's financial statements due to the Company's valuation allowance against U.S. deferred tax assets.

The Company regularly assesses the realizability of the deferred tax assets and establishes a valuation allowance if it is more-likely-than-not that some or all of the Company's deferred tax assets will not be realized. The Company evaluates and weighs all available positive and negative evidence such as historic results, future reversals of existing deferred tax liabilities, projected future taxable income, as well as prudent and feasible tax-planning strategies. The Company will continue to assess the realizability of the deferred tax assets in each of the applicable jurisdictions going forward. The Company may release all or a portion of its valuation allowance if there is sufficient positive evidence that outweighs the negative evidence, for example, if
the trend in profitability continues.

For the six months ended July 31, 2017, the Company reported a tax provision of $6 million on a pretax income of $53 million, which resulted in an effective tax rate of 11 percent. In computing the estimated annual effective tax rate, the Company expected pretax income for the full year and projected tax expense primarily related to profitable jurisdictions outside the United States. In addition, the tax benefit included a discrete benefit relating to the realization of certain U.S. state deferred taxes.

Tax Benefits Related to Stock-Based Compensation

The income tax benefit related to stock-based compensation was $112 million and $139 million for the six months ended July 31, 2018 and 2017, respectively, the majority of which was not recognized as a result of the valuation allowance.

Unrecognized Tax Benefits and Other Considerations

The Company records liabilities related to its uncertain tax positions. Tax positions for the Company and its subsidiaries are subject to income tax audits by multiple tax jurisdictions throughout the world. Certain prior year tax returns are currently being examined or reviewed by various taxing authorities in countries including the United States, United Kingdom and Germany. In March 2017, the Company received the final notice of proposed adjustments primarily related to transfer pricing issues from the Internal Revenue Service and is currently appealing the proposed adjustments. The Company believes that it has provided adequate reserves for its income tax uncertainties in all open tax years. As the outcome of the tax audits cannot be predicted with certainty, if any issues addressed in the Company's tax audits are resolved in a manner inconsistent with management's expectations, the Company could adjust its provision for income taxes in the future. Generally, any adjustments resulting from the U.S. audits should not have a significant impact to the Company's tax provision due to its valuation allowance. In addition, the Company anticipates it is reasonably possible that a decrease of unrecognized tax benefits up to approximately $4 million may occur in the next 12 months, as the applicable statutes of limitations lapse, ongoing examinations are completed, or tax positions meet the conditions of being effectively settled.

13. Earnings Per Share

Basic earnings per share is computed by dividing net income by the weighted-average number of common shares outstanding for the fiscal period. Diluted earnings per share is computed by giving effect to all potential weighted average dilutive common stock, including options, restricted stock units, warrants and the convertible senior notes. The dilutive effect of outstanding awards and convertible securities is reflected in diluted earnings per share by application of the treasury stock method.

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A reconciliation of the denominator used in the calculation of basic and diluted earnings per share is as follows (in millions):

2	Three Months Ended July 31,		Six Months Ended July 31,	
	2018	2017	2018	2017
Numerator:				
Net income	$299	$ 46	$643	$ 47
Denominator:				
Weighted-average shares outstanding for basic earnings per share	747	712	737	709
Effect of dilutive securities:				
Convertible senior notes	0	4	2	4
Employee stock awards	23	13	20	13
Warrants	4	0	4	0
Adjusted weighted-average shares outstanding and assumed conversions for diluted earnings per share	774	729	763	726

The weighted-average number of shares outstanding used in the computation of diluted earnings per share does not include the effect of the following potential outstanding common stock. The effects of these potentially outstanding shares were not included in the calculation of diluted earnings per share because the effect would have been anti-dilutive (in millions):

	Three Months Ended July 31,		Six Months Ended July 31,	
	2018	2017	2018	2017
Employee stock awards	7	13	5	13
Warrants	0	17	0	17

14. Commitments

Letters of Credit

As of July 31, 2018, the Company had a total of $104 million in letters of credit outstanding substantially in favor of certain landlords for office space. These letters of credit renew annually and expire at various dates through December 2030.

Leases

The Company leases facilities space and certain fixed assets under non-cancelable operating and capital leases with various expiration dates.

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As of July 31, 2018, the future minimum lease payments under non-cancelable operating and capital leases are as follows (in millions):

	Capital Leases	Operating Leases	Financing Obligation -Leased Facility (1)
Fiscal Period:			
Remaining six months of Fiscal 2019	$ 12	$ 369	$ 11
Fiscal 2020	202	692	22
Fiscal 2021	0	558	23
Fiscal 2022	0	374	23
Fiscal 2023	0	317	24
Thereafter	0	1,305	187
Total minimum lease payments	214	$ 3,615	$ 290
Less: amount representing interest	(9)		
Present value of capital lease obligations	$ 205		

(1) Total Financing Obligation - Leased Facility noted above represents the total obligation on the lease agreement including amounts allocated to interest and the implied lease for the land. As of July 31, 2018, $217 million of the total $290 million above was recorded to Financing obligation leased facility, of which the current portion is included in "Accounts payable, accrued expenses and other liabilities" and the noncurrent portion is included in “Other noncurrent liabilities” on the condensed consolidated balance sheet.

The Company’s agreements for the facilities and certain services provide the Company with the option to renew. The Company’s future contractual obligations would change if the Company exercised these options.

The terms of the lease agreements provide for rental payments on a graduated basis. The Company recognizes rent expense on a straight-line basis over the lease period and has accrued for rent expense incurred but not paid. Of the total operating lease commitment balance of $3.6 billion, approximately $2.9 billion is related to facilities space. The remaining commitment amount is related to computer equipment and furniture and fixtures.

The Company has entered into various contractual commitments with infrastructure service providers for a total commitment of $2.0 billion. As of July 31, 2018 the total remaining commitment is approximately $1.9 billion and $79 million is remaining to be paid this fiscal year.

15. Legal Proceedings and Claims

In the ordinary course of business, the Company is or may be involved in various legal or regulatory proceedings, claims or purported class actions related to alleged infringement of third-party patents and other intellectual property rights, commercial, corporate and securities, labor and employment, wage and hour, and other claims. The Company has been, and may in the future be put on notice and/or sued by third-parties for alleged infringement of their proprietary rights, including patent infringement.

In general, the resolution of a legal matter could prevent the Company from offering its service to others, could be material to the Company’s financial condition or cash flows, or both, or could otherwise adversely affect the Company’s operating results.

The Company makes a provision for a liability relating to legal matters when it is both probable that a liability has been incurred and the amount of the loss can be reasonably estimated. These provisions are reviewed at least quarterly and adjusted to reflect the impacts of negotiations, estimated settlements, legal rulings, advice of legal counsel and other information and events pertaining to a particular matter. The outcomes of legal proceedings and other contingencies are, however, inherently unpredictable and subject to significant uncertainties. As a result, the Company is not able to reasonably estimate the amount or range of possible losses in excess of any amounts accrued, including losses that could arise as a result of application of non-monetary remedies, with respect to the contingencies it faces, and the Company’s estimates may not prove to be accurate. In management’s opinion, resolution of all current matters is not expected to have a material adverse impact on the Company’s condensed consolidated results of operations, cash flows or financial position. However, depending on the nature and timing of any such dispute or other contingency, an

unfavorable resolution of a matter could materially affect the Company's current or future results of operations or cash flows, or both, in a particular quarter.

In September 2013, one of the Company's subsidiaries, ExactTarget, Inc. ("ExactTarget"), was added as a defendant in a purported class-action lawsuit that alleged that ExactTarget and one of its customers, Simply Fashion Stores, Ltd. ("Simply Fashion"), violated the Telephone Consumer Protection Act ("TCPA") as a result of Simply Fashion's text messaging

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campaigns and alleged failure to opt-out certain Simply Fashion customers from receiving messages. The complaint was subsequently amended to remove Simply Fashion as a defendant and the lawsuit is currently before the United States District Court for the Southern District of Indiana. The complaint seeks statutory damages and injunctive relief. While disputing the allegations of wrongdoing, the Company reached a settlement of the lawsuit for approximately $6 million in fiscal 2018. The parties submitted the settlement agreement to the Court for approval and the Court entered the preliminary approval order. The Court held the final approval hearing on July 20, 2018. The Court has not yet entered a final judgment.

16. Related-Party Transactions

In January 1999, the Salesforce.com Foundation, also referred to as the Foundation, was chartered on an idea of leveraging the Company’s people, technology, and resources to help improve communities around the world. The Company calls this integrated philanthropic approach the 1-1-1 model. Beginning in 2008, Salesforce.org, which is a non-profit public benefit corporation, was established to resell the Company's services to nonprofit organizations and certain higher education organizations.

The Company’s Chairman is the chairman of both the Foundation and Salesforce.org. The Company’s Chairman holds one of the three Foundation board seats. The Company’s Chairman, one of the Company’s employees and one of the Company’s board members hold three of Salesforce.org’s nine board seats. The Company does not control the Foundation’s or Salesforce.org's activities, and accordingly, the Company does not consolidate either of the related entities' statement of activities with its financial results.

Since the Foundation’s and Salesforce.org’s inception, the Company has provided at no charge certain resources to those entities' employees such as office space, furniture, equipment, facilities, services, and other resources. The value of these items was approximately $7 million and $4 million for the six months ended July 31, 2018 and 2017, respectively.

Additionally, the Company allows Salesforce.org to donate subscriptions of the Company’s services to other qualified non-profit organizations. The Company also allows Salesforce.org to resell the Company’s service to non-profit organizations and certain education entities. The Company does not charge Salesforce.org for these subscriptions, therefore income from subscriptions sold to non-profit organizations is donated back to the community through charitable grants made by the Foundation and Salesforce.org. The value of the subscriptions sold by Salesforce.org pursuant to the reseller agreement, as amended, was approximately $117 million and $83 million for the six months ended July 31, 2018 and 2017, respectively.

17. Subsequent Event

In August 2018, the Company acquired all outstanding stock of Datorama, Inc. ("Datorama"), which provides a platform for enterprises, agencies and publishers to integrate data across marketing channels and data sources. The preliminary acquisition date fair value of the consideration transferred for Datorama is estimated to be approximately $726 million net of cash acquired, which comprised of $121 million in cash, 3.7 million shares of common stock at a conversion price of $143.14 issued, and $93 million related to the fair value of stock options and restricted stock awards assumed.

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ITEM 2. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

This Quarterly Report on Form 10-Q contains forward-looking statements within the meaning of Section 27A of the Securities Act of 1933, as amended ("Securities Act"), and Section 21E of the Securities Exchange Act of 1934, as amended ("Exchange Act"). Words such as "expects," "anticipates," "aims," "projects," "intends," "plans," "believes," "estima "assumes," "may," "should," "could," "would," "foresees," "forecasts," "predicts," "targets," variations of such words and sim expressions are intended to identify such forward-looking statements, which may consist of, among other things, trend analyses and statements regarding future events, future financial performance, anticipated growth and industry prospects. These forward-looking statements are based on current expectations, estimates and forecasts, as well as the beliefs and assumptions of our management, and are subject to risks and uncertainties that are difficult to predict, including: the effect of general economic and market conditions; the impact of foreign currency exchange rate and interest rate fluctuations on our results; our business strategy and our plan to build our business, including our strategy to be the leading provider of enterprise cloud computing applications and platforms; the pace of change and innovation in enterprise cloud computing services; the competitive nature of the market in which we participate; our international expansion strategy; our service performance and security, including the resources and costs required to prevent, detect and remediate potential security breaches; the expenses associated with new data centers and third-party infrastructure providers; additional data center capacity; real estate and office facilities space; our operating results and cash flows; new services and product features; our strategy of acquiring or making investments in complementary businesses, joint ventures, services, technologies and intellectual property rights; the performance and fair value of our investments in complementary businesses through our strategic investment portfolio; our ability to realize the benefits from strategic partnerships and investments; our ability to successfully integrate acquired businesses and technologies; our ability to continue to grow and maintain unearned revenue and remaining performance obligation; our ability to protect our intellectual property rights; our ability to develop our brands; our reliance on third-party hardware, software and platform providers; our dependency on the development and maintenance of the infrastructure of the Internet; the effect of evolving domestic and foreign government regulations, including those related to the provision of services on the Internet, those related to accessing the Internet, and those addressing data privacy, cross-border data transfers and import and export controls; the valuation of our deferred tax assets; the potential availability of additional tax assets in the future; the impact of new accounting pronouncements and tax laws, including the U.S. Tax Cuts and Jobs Act, and interpretations thereof; uncertainties affecting our ability to estimate our tax rate; the impact of future gains or losses from our strategic investment portfolio; the impact of expensing stock options and other equity awards; the sufficiency of our capital resources; factors related to our 2023 and 2028 senior notes, revolving credit facility, 2019 and 2021 term loans and loan associated with 50 Fremont; compliance with our debt covenants and capital lease obligations; current and potential litigation involving us; and the impact of climate change. These and other risks and uncertainties may cause our actual results to differ materially and adversely from those expressed in any forward-looking statements. Readers are directed to risks and uncertainties identified below under "Risk Factors" and elsewhere in this report for additional detail regarding factors that may cause actual results to be different than those expressed in our forward-looking statements. Except as required by law, we undertake no obligation to revise or update publicly any forward-looking statements for any reason.

Overview

We are a leading provider of enterprise cloud computing solutions, with a focus on customer relationship management, or CRM. We introduced our first CRM solution in 2000, and we have since expanded our service offerings with new editions, features and platform capabilities. Our core mission is to empower our customers to connect with their customers in entirely new ways through cloud, mobile, social, Internet of Things ("IoT") and artificial intelligence technologies.

Our Customer Success Platform - including sales force automation, customer service and support, marketing automation, digital commerce, community management, industry-specific solutions, analytics, integration solutions, application development, IoT integration, collaborative productivity tools, our AppExchange, which is our enterprise cloud marketplace, and our professional cloud services - provides the tools customers need to succeed in a digital world. Key elements of our strategy include:

- cross sell and upsell;
- extend existing service offerings;
- reduce customer attrition;
- expand and strengthen the partner ecosystem;
- expand internationally;
- target vertical industries;
- expand into new horizontal markets;
- extend go-to-market capabilities;

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- ensure strong customer adoption; and
- encourage the development of third-party applications on our cloud computing platform.

We are also committed to a sustainable, low-carbon future, advancing equality and diversity, and fostering employee success. We try to integrate social good into everything we do. All of these goals align with our long-term growth strategy and financial and operational priorities.

We believe the factors that will influence our ability to achieve our objectives include: our prospective customers' willingness to migrate to enterprise cloud computing services; our ability to maintain a balanced portfolio of products and customers; the availability, performance and security of our service; our ability to continue to release, and gain customer acceptance of new and improved features; our ability to successfully integrate acquired businesses and technologies; successful customer adoption and utilization of our service; our ability to continue to meet new and evolving privacy laws and regulations, acceptance of our service in markets where we have few customers; the emergence of additional competitors in our market and improved product offerings by existing and new competitors; the location of new data centers that we operate as well as the new locations of services provided by third-party cloud computing platform providers; third-party developers' willingness to develop applications on our platforms; our ability to attract new personnel and retain and motivate current personnel; and general economic conditions which could affect our customers' ability and willingness to purchase our services, delay the customers' purchasing decision or affect attrition rates.

To address these factors, we will need to, among other things, continue to add substantial numbers of paying subscriptions, upgrade our customers to fully featured versions or arrangements such as an Enterprise License Agreement, provide high quality technical support to our customers, encourage the development of third-party applications on our platforms, realize the benefits from our strategic partnerships and continue to focus on retaining customers at the time of renewal. Our plans to invest for future growth include the continuation of the expansion of our data center capacity, whether internally or through the use of third parties, the hiring of additional personnel, particularly in direct sales, other customer-related areas and research and development, the expansion of domestic and international selling and marketing activities, specifically in our top markets, the continued development of our brands, the addition of distribution channels, the upgrade of our service offerings, the continued development of services including Community Cloud, Industry Clouds, Success Cloud and Integration Cloud, the integration of new and acquired technologies such as Commerce Cloud, artificial intelligence technologies and Salesforce Quip, the expansion of our Marketing Cloud, Salesforce Platform core service offerings, Integration Cloud through our May 2018 MuleSoft acquisition and the additions to our global infrastructure to support our growth.

We also regularly evaluate acquisitions or investment opportunities in complementary businesses, joint ventures, services and technologies and intellectual property rights in an effort to expand our service offerings. We expect to continue to make such investments and acquisitions in the future and we plan to reinvest a significant portion of our incremental revenue in future periods to grow our business and continue our leadership role in the cloud computing industry. As part of our growth strategy, we are delivering innovative solutions in new categories, including analytics, e-commerce, artificial intelligence, IoT and collaborative productivity tools. We drive innovation organically and to a lesser extent through acquisitions, such as our May 2018 acquisition of MuleSoft, Inc. ("MuleSoft") and in August 2018 our acquisition of Datorama. We have a disciplined and thoughtful acquisition process where we routinely survey the industry landscape across a wide range of companies. As a result of our aggressive growth plans and integration of our previously acquired businesses, we have incurred significant expenses from equity awards and amortization of purchased intangibles, which have reduced our operating income. We remain focused on improving operating margins in fiscal 2019 and beyond.

Our typical subscription contract term is 12 to 36 months, although terms range from one to 60 months, so during any fiscal reporting period only a subset of active subscription contracts is eligible for renewal. We calculate our attrition rate as of the end of each month. Our attrition rate, including the Marketing Cloud service offering but excluding our Commerce Cloud serving offering, was less than ten percent as of July 31, 2018. While it is difficult to predict, we expect our attrition rate to remain consistent as we continue to expand our enterprise business and invest in customer success and related programs.

We expect marketing and sales costs, which were 45 percent and 45 percent for the six months ended July 31, 2018 and 2017, respectively, to continue to represent a substantial portion of total revenues in the future as we seek to grow our customer base, sell more products to existing customers, and continue to build greater brand awareness.

In May 2018, we acquired MuleSoft, an industry-leading integration platform, to provide our customers the ability to integrate data across platforms. The financial results of MuleSoft are included in our consolidated financial statements from the date of acquisition. The total purchase price for MuleSoft was approximately $6.4 billion.

In August 2018, we acquired all outstanding stock of Datorama, Inc. ("Datorama"), which provides a platform for enterprises, agencies and publishers to integrate data across marketing channels and data sources. The preliminary acquisition date fair value of the consideration transferred for Datorama is estimated to be approximately $726 million net of cash acquired.

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Fiscal Year

Our fiscal year ends on January 31. References to fiscal 2019, for example, refer to the fiscal year ending January 31, 2019.

Adoption of New Accounting Standards

We have adjusted our condensed consolidated financial statements from amounts previously reported due to the adoption of Accounting Standards Update No. 2014-09, "Revenue from Contracts with Customers (Topic 606)" ("ASU 2014-09"). The information presented reflects the adjusted amounts as compared to those previously reported. In addition, we have prospectively adopted Accounting Standards Update No. 2016-01, "Financial Instrument-Overall (Subtopic 825-10)" ("ASU 2016-01") and Accounting Standards Update No. 2016-16, "Income Taxes (Topic 740): Intra-Entity Transfers of Assets Other Than Inventory" ("ASU 2016-16")

Operating Segments

We operate as one operating segment. Operating segments are defined as components of an enterprise for which separate financial information is evaluated regularly by the chief operating decision maker, Marc Benioff, who is the co-chief executive officer and the chairman of the board, in deciding how to allocate resources and assess performance. Over the past few years, we have completed a number of acquisitions. These acquisitions have allowed us to expand our offerings, presence and reach in various market segments of the enterprise cloud computing market. While we have offerings in multiple enterprise cloud computing market segments, including as a result of our acquisitions, our business operates in one operating segment because our offerings operate on its single customer success platform and are deployed in an identical way, and our chief operating decision maker evaluates our financial information and resources and assesses the performance of these resources on a consolidated basis. Since we operate as one operating segment, all required financial segment information can be found in the condensed consolidated financial statements.

In August 2018, we moved to a co-chief executive officer model with the promotion of our vice chairman and chief operating officer. We will continue to assess who the chief operating decision maker is for the purposes of segment reporting in light of this recent change.

Sources of Revenues

We derive our revenues from two sources: (1) subscription revenues, which are comprised of subscription fees from customers accessing our enterprise cloud computing services, software licenses, and from customers paying for additional support beyond the standard support that is included in the basic subscription fees; and (2) related professional services such as process mapping, project management, implementation services and other revenue. “Other revenue” consists primarily of training fees. Subscription and support revenues accounted for approximately 93 percent of our total revenues for the six months ended July 31, 2018. Subscription revenues are driven primarily by the number of paying subscribers, varying service types, and the price of our service and renewals. We define a “customer” as a separate and distinct buying entity (e.g., a company, a distinct business unit of a large corporation, a partnership, etc.) that has entered into a contract to access our enterprise cloud computing services. None of our customers accounted for more than five percent of our revenues during the six months ended July 31, 2018 and 2017. Subscription and support revenues for Cloud Services are recognized ratably over the contract terms beginning on the commencement dates of each contract. Subscription and support services for software licenses are recognized upfront upon the later of when the software is made available. The typical subscription and support term is 12 to 36 months, although terms range from one to 60 months. Our subscription and support contracts are non-cancelable, though customers typically have the right to terminate their contracts for cause if we materially fail to perform.

We generally invoice our customers in advance, in annual installments, and typical payment terms provide that our customers pay us within 30 days of invoice. Amounts that have been invoiced are recorded in accounts receivable and in unearned revenue, or in revenue depending on whether transfer of control to customers has occurred. In general, we collect our billings in advance of the subscription service period.

Professional services and other revenues consist of fees associated with consulting and implementation services and training. Our consulting and implementation engagements are billed on a time and materials, fixed fee or subscription basis. We also offer a number of training classes on implementing, using and administering our service that are billed on a per person, per class basis. Our typical professional services payment terms provide that our customers pay us within 30 days of invoice.

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In determining whether professional services can be accounted for separately from subscription and support revenues, we consider a number of factors, which are described in Note 1 "Summary of Business and Significant Accounting Policies."

Revenue by Cloud Service Offering

The information below is provided on a supplemental basis to give additional insight into the revenue performance of our individual core service offerings. All of the cloud offerings that we offer to customers are grouped into four major cloud service offerings. Subscription and support revenues consisted of the following (in millions):

	Three Months Ended July 31,			Six Months Ended July 31,		
	2018	2017	Variance- Percent	2018	2017	Variance- Percent
Sales Cloud	$1,004	$891	13%	$1,969	$1,721	14%
Service Cloud	892	700	27%	1,740	1,356	28%
Salesforce Platform and Other	712	463	54%	1,287	887	45%
Marketing and Commerce Cloud	452	329	37%	874	628	39%
Total	$3,060	$2,383		$5,870	$4,592	

Subscription and support revenues from the Community Cloud, Quip and our Industry Offerings were not significant in the three and six months ended July 31, 2018. Quip revenue is included with Salesforce Platform and Other in the table above. Our Industry Offerings and Community Cloud revenue are included in either Sales Cloud, Service Cloud or Salesforce Platform and Other depending on the primary service offering purchased. Revenue from our acquisition of MuleSoft in May 2018 is included in Salesforce Platform and Other.

As required under U.S. GAAP, we recorded unearned revenue related to acquired contracts from MuleSoft at fair value on the date of acquisition. As a result, we did not recognize certain revenues related to these acquired contracts that MuleSoft would have otherwise recorded as an independent entity. Of the $1.3 billion subscription and support revenue for Salesforce Platform and Other for the six months ended July 31, 2018, approximately $99.0 million was attributed to MuleSoft.

In situations where a customer purchases multiple cloud offerings, such as through an Enterprise License Agreement, we allocate the contract value to each core service offering based on the customer’s estimated product demand plan, the service that was provided at the inception of the contract, and standalone selling price ("SSP") of those products. We do not update these allocations based on actual product usage during the term of the contract. We have allocated approximately 17 percent and 15 percent of our total subscription and support revenues for the three and six months ended July 31, 2018 and 2017, respectively, based on customers’ estimated product demand plans and these allocated amounts are included in the table above.

Additionally, some of our service offerings have similar features and functions. For example, customers may use the Sales Cloud, the Service Cloud or the Salesforce Platform to record account and contact information, which are similar features across these core service offerings. Depending on a customer’s actual and projected business requirements, more than one core service offering may satisfy the customer’s current and future needs. We record revenue based on the individual products ordered by a customer, not according to the customer’s business requirements and usage. In addition, as we introduce new features and functions within each offering and refine our allocation methodology for changes in our business, we do not expect it to be practical to adjust historical revenue results by service offering for comparability. Accordingly, comparisons of revenue performance by core service offering over time may not be meaningful.

Our Sales Cloud service offering is our most widely distributed service offering and has historically been the largest contributor of subscription and support revenues. As a result, Sales Cloud has the most international exposure and foreign exchange rate exposure relative to the other cloud service offerings. Conversely, revenue for Marketing and Commerce Cloud is primarily derived from the Americas with little impact from foreign exchange rate movement.

The revenue growth rates of each of our core service offerings fluctuate from quarter to quarter and over time. While we are a market leader in each core offering, we manage the total balanced product portfolio to deliver solutions to our customers. Accordingly, the revenue result for each cloud service offering is not necessarily indicative of the results to be expected for any subsequent quarter.

Seasonal Nature of Unearned Revenue, Accounts Receivable and Operating Cash Flow

Unearned revenue primarily consists of billings to customers for our subscription service. Over 90 percent of the value of our billings to customers is for our subscription and support service. We generally invoice our customers in annual cycles. We typically issue renewal invoices in advance of the renewal service period, and depending on timing, the initial invoice for the subscription and services contract and the subsequent renewal invoice may occur in different quarters. This may result in an increase in unearned revenue and accounts receivable. There is a disproportionate weighting toward annual billings in the

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fourth quarter, primarily as a result of large enterprise account buying patterns. Our fourth quarter has historically been our strongest quarter for new business and renewals. The year on year compounding effect of this seasonality in both billing patterns and overall new and renewal business causes the value of invoices that we generate in the fourth quarter for both new business and renewals to increase as a proportion of our total annual billings. Accordingly, because of this billing activity, our first quarter is our largest collections and operating cash flow quarter.

The sequential quarterly changes in accounts receivable and the related unearned revenue and operating cash flow during the first quarter of our fiscal year are not necessarily indicative of the billing activity that occurs for the following quarters as displayed below (in millions):

	July 31, 2018	April 30, 2018
Fiscal 2019		
Accounts receivable, net	$1,980	$1,763
Unearned revenue	5,883	6,201
Operating cash flow (1)	458	1,466

	January 31, 2018	October 31, 2017	July 31, 2017	April 30, 2017
Fiscal 2018				
Accounts receivable, net	$3,921	$1,522	$1,572	$1,442
Unearned revenue	6,995	4,312	4,749	4,969
Operating cash flow (1)	1,051	126	331	1,230

(1) Operating cash flow represents net cash provided by operating activities for the three months ended in the periods stated above.

The unearned revenue balance on our condensed consolidated balance sheets does not represent the total contract value of annual or multi-year, non-cancelable subscription agreements. Transaction price allocated to the remaining performance obligations represents contracted revenue that has not yet been recognized, which includes unearned revenue and unbilled amounts that will be recognized as revenue in future periods. Transaction price allocated to the remaining performance obligation is influenced by several factors, including seasonality, the timing of renewals, average contract terms and foreign currency exchange rates. Unbilled portions of the remaining performance obligation denominated in foreign currencies are revalued each period based on the period end exchange rates. For multi-year subscription agreements billed annually, the associated unbilled balance and corresponding remaining performance obligation is typically high at the beginning of the contract period, zero just prior to renewal, and increases if the agreement is renewed. Low remaining performance obligations attributable to a particular subscription agreement are often associated with an impending renewal and may not be an indicator of the likelihood of renewal or future revenue from such customer.

Remaining performance obligation, formerly referred to as remaining transaction price, consisted of the following (in billions):

	Current	Noncurrent	Total
As of July 31, 2018	$ 9.8	$ 11.2	$21.0
As of April 30, 2018	$ 9.6	$ 10.8	$20.4
As of July 31, 2017	$ 7.7	$ 7.7	$15.4
As of April 30, 2017	$ 7.6	$ 7.4	$15.0

Cost of Revenues and Operating Expenses

Cost of Revenues

Cost of subscription and support revenues primarily consists of expenses related to delivering our service and providing support, the costs of data center capacity, depreciation or operating lease expense associated with computer equipment and software, allocated overhead, amortization expense associated with capitalized software related to our services and acquired developed technologies and certain fees paid to various third parties for the use of their

technology, services and data. We allocate overhead such as IT infrastructure, rent, and occupancy charges based on headcount. Employee benefit costs and taxes are allocated based upon a percentage of total compensation expense. As such, general overhead expenses are reflected in each cost of revenue and operating expense category. Cost of professional services and other revenues consists primarily of

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employee-related costs associated with these services, including stock-based expenses, the cost of subcontractors, certain third-party fees and allocated overhead. The cost of providing professional services is higher as a percentage of the related revenue than for our enterprise cloud computing subscription service due to the direct labor costs and costs of subcontractors.

We intend to continue to invest additional resources in our enterprise cloud computing services. For example, we have invested in additional database software and hardware and we plan to increase the capacity that we are able to offer globally through data centers and third-party infrastructure providers. In addition, we intend to continue to invest additional resources in enhancing our cyber security measures. As we acquire new businesses and technologies, the amortization expense associated with the purchase of acquired developed technology will be included in cost of revenues. Additionally, as we enter into new contracts with third parties for the use of their technology, services or data, or as our sales volume grows, the fees paid to use such technology or services may increase. Finally, we expect the cost of professional services to be approximately in line with revenues from professional services as we believe this investment in professional services facilitates the adoption of our service offerings. The timing of these additional expenses will affect our cost of revenues, both in terms of absolute dollars and as a percentage of revenues, in the affected periods.

Research and Development

Research and development expenses consist primarily of salaries and related expenses, including stock-based expenses, the costs of our development and test data center and allocated overhead. We continue to focus our research and development efforts on adding new features and services, integrating acquired technologies, increasing the functionality and security and enhancing the ease of use of our enterprise cloud computing services. Our proprietary, scalable and secure multi-tenant architecture enables us to provide our customers with a service based on a single version of our application. As a result, we do not have to maintain multiple versions, which enables us to have relatively lower research and development expenses as compared to traditional enterprise software companies.

We expect that in the future, research and development expenses will increase in absolute dollars and may increase as a percentage of total revenues as we invest in adding employees and building the necessary system infrastructure required to support the development of new, and improve existing, technologies and the integration of acquired businesses, technologies and all of our service offerings.

Marketing and Sales

Marketing and sales expenses are our largest cost and consist primarily of salaries and related expenses, including stock-based expenses, for our sales and marketing staff, including commissions, as well as payments to partners, marketing programs and allocated overhead. Marketing programs consist of advertising, events, corporate communications, brand building and product marketing activities.

We plan to continue to invest in marketing and sales by expanding our domestic and international selling and marketing activities, building brand awareness, attracting new customers, and sponsoring additional marketing events. The timing of these marketing events, such as our annual and largest event, Dreamforce, will affect our marketing costs in a particular quarter. In addition, as we acquire new businesses and technologies, a component of the amortization expense associated with this activity will be included in marketing and sales. We expect that in the future, marketing and sales expenses will increase in absolute dollars and continue to be our largest cost. We expect marketing and sales expenses, excluding sales personnel expenses, to grow in line with or at a slower rate than revenues and sales personnel expenses. These may increase as a percentage of total revenues as we invest in additional sales personnel to focus on adding new customers and increasing penetration within our existing customer base.

General and Administrative

General and administrative expenses consist of salaries and related expenses, including stock-based expenses, for finance and accounting, legal, internal audit, human resources and management information systems personnel, legal costs, professional fees, other corporate expenses such as transaction costs for acquisitions and allocated overhead. We expect that in the future, general and administrative expenses will increase in absolute dollars as we invest in our infrastructure and we incur additional employee related costs, professional fees and insurance costs related to the growth of our business and international expansion. We expect general and administrative costs as a percentage of total revenues to either remain flat or decrease for the next several quarters. However, the timing of additional

expenses in a particular quarter, both in terms of absolute dollars and as a percentage of revenues, will affect our general and administrative expenses.

Stock-Based Expenses

Our cost of revenues and operating expenses include stock-based expenses related to equity plans for employees and non-employee directors. We recognize our stock-based compensation as an expense in the statements of operations based on their fair values and vesting periods. These charges have been significant in the past and we expect that they will increase as our stock price increases, as we acquire more companies, as we hire more employees and seek to retain existing employees.

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During the six months ended July 31, 2018, we recognized stock-based expense related to our equity plans for employees and non-employee directors of $603 million. As of July 31, 2018, the aggregate stock compensation remaining to be amortized to costs and expenses was approximately $2.9 billion. We expect this stock compensation balance to be amortized as follows: $660 million during the remaining six months of fiscal 2019; $1.0 billion during fiscal 2020; $714 million during fiscal 2021; $400 million during fiscal 2022; $67 million during fiscal 2023 and $8 million thereafter. The expected amortization reflects only outstanding stock awards as of July 31, 2018 and assumes no forfeiture activity. We expect to continue to issue stock-based awards to our employees in future periods.

Amortization of Purchased Intangible Assets Acquired Through Business Combinations

Our cost of revenues, operating expenses and other expenses include amortization of acquisition-related intangible assets, such as the amortization of the cost associated with an acquired company's developed technology, trade names and trademarks, customer lists, acquired leases and customer relationships. We expect this expense to fluctuate as we acquire more businesses and intangible assets become fully amortized.

Critical Accounting Policies and Estimates

Our condensed consolidated financial statements are prepared in accordance with accounting principles generally accepted in the United States. The preparation of these condensed consolidated financial statements requires us to make estimates and assumptions that affect the reported amounts of assets, liabilities, revenues, costs and expenses, and related disclosures. On an ongoing basis, we evaluate our estimates and assumptions. Our actual results may differ from these estimates under different assumptions or conditions.

We believe that of our significant accounting policies, which are described in Note 1 "Summary of Business and Significant Accounting Policies" to our condensed consolidated financial statements, the following accounting policies and specific estimates involve a greater degree of judgment and complexity. Accordingly, these are the policies and estimates we believe are the most critical to aid in fully understanding and evaluating our consolidated financial condition and results of operations:

- the SSP of performance obligations for contracts with multiple performance obligations;
- the estimate of variable consideration as part of the adoption of ASU 2014-09;
- the fair value of assets acquired and liabilities assumed for business combinations;
- the recognition, measurement and valuation of current and deferred income taxes;
- the average period of benefit associated with costs capitalized to obtain revenue contracts;
- the fair value of certain stock awards issued;
- the useful lives of intangible assets; and
- the valuation of privately held strategic investments.

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Results of Operations

The following tables set forth selected data for each of the periods indicated (in millions):

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	Three Months Ended July 31,				Six Months Ended July 31,			
	2018	% of Total Revenues	2017 (as adjusted)*	% of Total Revenues	2018	% of Total Revenues	2017 (as adjusted)*	% of Total Revenues
Revenues:								
Subscription and support	$3,060	93 %	$ 2,383	92 %	$5,870	93 %	$ 4,592	92 %
Professional services and other	221	7	194	8	417	7	382	8
Total revenues	3,281	100	2,577	100	6,287	100	4,974	100
Cost of revenues (1)(2):								
Subscription and support	638	20	494	19	1,211	19	957	19
Professional services and other	211	6	176	7	405	7	364	8
Total cost of revenues	849	26	670	26	1,616	26	1,321	27
Gross profit	2,432	74	1,907	74	4,671	74	3,653	73
Operating expenses (1)(2):								
Research and development	463	14	387	15	887	14	763	15
Marketing and sales	1,504	46	1,153	45	2,833	45	2,259	45
General and administrative	350	11	283	11	645	10	543	11
Total operating expenses	2,317	71	1,823	71	4,365	69	3,565	71
Income from operations	115	3	84	3	306	5	88	2
Investment income	12	1	9	0	28	0	14	0
Interest expense	(39)	(1)	(22)	(1)	(73)	(1)	(44)	(1)
Gains (losses) on strategic investments, net	143	4	(8)	0	354	6	(5)	0
Other income	0	0	0	0	1	0	0	0
Income before benefit from (provision for) income taxes	231	7	63	2	616	10	53	1
Benefit from (provision for) income taxes	68	2	(17)	0	27	0	(6)	0
Net income	$299	9 %	$ 46	2 %	$643	10 %	$ 47	1 %

(1) Amounts related to amortization of intangible assets acquired through business combinations, as follows (in millions):

	Three Months Ended July 31,				Six Months Ended July 31,			
	2018	% of Total Revenues	2017 (as adjusted)*	% of Total Revenues	2018	% of Total Revenues	2017 (as adjusted)*	% of Total Revenues
Cost of revenues	$52	2 %	$ 43	2 %	$91	1 %	$ 87	2 %
Marketing and sales	67	2	31	1	97	2	61	1

(2) Amounts related to stock-based expenses, as follows (in millions):

	Three Months Ended July 31,				Six Months Ended July 31,			
	2018	% of Total Revenues	2017 (as adjusted)*	% of Total Revenues	2018	% of Total Revenues	2017 (as adjusted)*	% of Total Revenues
Cost of revenues	$43	1 %	$ 32	1 %	$77	1 %	$ 64	1 %
Research and development	81	2	67	3	147	2	131	3
Marketing and sales	174	5	120	5	294	5	239	5
General and administrative	53	2	37	1	85	1	74	1

*Prior period information has been adjusted for the adoption of Topic 606.

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Three and Six Months Ended July 31, 2018 and 2017

Revenues.

	Three Months Ended July 31,		Variance	
(in millions)	2018	2017	Dollars	Percent
Subscription and support	$3,060	$2,383	$677	28%
Professional services and other	221	194	27	14%
Total revenues	$3,281	$2,577	$704	27%

	Six Months Ended July 31,		Variance	
(in millions)	2018	2017	Dollars	Percent
Subscription and support	$5,870	$4,592	$1,278	28%
Professional services and other	417	382	35	9%
Total revenues	$6,287	$4,974	$1,313	26%

Total revenues were $3.3 billion for the three months ended July 31, 2018, compared to $2.6 billion during the same period a year ago, an increase of $704 million, or 27 percent. Total revenues were $6.3 billion for the six months ended July 31, 2018, compared to $5.0 billion during the same period a year ago, an increase of $1.3 billion, or 26 percent. Subscription and support revenues were $3.1 billion, or 93 percent of total revenues, for the three months ended July 31, 2018, compared to $2.4 billion, or 92 percent of total revenues, during the same period a year ago, an increase of $677 million, or 28 percent. Subscription and support revenues were $5.9 billion, or 93 percent of total revenues, for the six months ended July 31, 2018, compared to $4.6 billion, or 92 percent of total revenues, during the same period a year ago, an increase of $1.3 billion, or 28 percent. The increase in subscription and support revenues was primarily caused by volume-driven increases from new business, which includes new customers, upgrades and additional subscriptions from existing customers. Our acquisition of MuleSoft in May 2018 contributed $99.0 million to total revenues in the three and six months ended July 31, 2018. We continue to invest in a variety of customer programs and initiatives which, along with increasing enterprise adoption, have helped keep our attrition rate, which is approximately 10 percent and consistent to the prior year. Consistent attrition rates play a role in our ability to maintain growth in our subscription and support revenues. Neither changes in the net price per user per month nor foreign currency fluctuations, have been a significant driver of revenue growth for the periods presented. Professional services and other revenues were $221 million, or 7 percent of total revenues, for the three months ended July 31, 2018, compared to $194 million, or 8 percent of total revenues, for the same period a year ago, an increase of $27 million, or 14 percent. Professional services and other revenues were $417 million, or 7 percent of total revenues, for the six months ended July 31, 2018, compared to $382 million, or 8 percent of total revenues, for the same period a year ago, an increase of $35 million, or 9 percent. The increase in professional services and other revenues was due primarily to the higher demand for services from an increased number of customers.

Revenues by geography were as follows:

	Three Months Ended July 31,				
(in millions)	2018	As a % of Total Revenues		2017	As a % of Total Revenues
Americas	$2,338	71	%	$1,868	73 %
Europe	629	19		466	18
Asia Pacific	314	10		243	9
	$3,281	100	%	$2,577	100 %

	Six Months Ended July 31,				
(in millions)	2018	As a % of Total Revenues		2017	As a % of Total Revenues
Americas	$4,439	71	%	$3,633	73 %

Europe	1,235	19		875	18	
Asia Pacific	613	10		466	9	
	$6,287	100	%	$4,974	100	%

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Revenues by geography are determined based on the region of the Salesforce contracting entity, which may be different than the region of the customer. Americas revenue attributed to the United States was approximately 96 percent and 96 percent during the three months ended July 31, 2018 and 2017, respectively, and 96 percent and 96 percent during the six months ended July 31, 2018 and 2017, respectively.

Revenues in Europe and Asia Pacific accounted for $943 million, or 29 percent of total revenues, for the three months ended July 31, 2018, compared to $709 million, or 27 percent of total revenues, during the same period a year ago, an increase of $234 million, or 33 percent. Revenues in Europe and Asia Pacific accounted for $1.8 billion, or 29 percent of total revenues, for the six months ended July 31, 2018, compared to $1.3 billion, or 27 percent of total revenues, during the same period a year ago, an increase of $507 million, or 38 percent.The increase in revenues outside of the Americas was the result of the increasing acceptance of our services, our focus on marketing our services internationally and additional resources.

Cost of Revenues.

	Three Months Ended July 31,		Variance
(in millions)	2018	2017	Dollars
Subscription and support	$638	$494	$ 144
Professional services and other	211	176	35
Total cost of revenues	$849	$670	$ 179
Percent of total revenues	26 %	26 %	

	Six Months Ended July 31,		Variance
(in millions)	2018	2017	Dollars
Subscription and support	$1,211	$957	$ 254
Professional services and other	405	364	41
Total cost of revenues	$1,616	$1,321	$ 295
Percent of total revenues	26 %	27 %	

Cost of revenues was $849 million, or 26 percent of total revenues, for the three months ended July 31, 2018, compared to $670 million, or 26 percent of total revenues, during the same period a year ago, an increase of $179 million. For the three months ended July 31, 2018, the increase in absolute dollars was primarily due to the acquisition of MuleSoft during the three months ended July 31, 2018 and an increase of $38 million in employee-related costs, an increase of $11 million in stock-based expenses, an increase of $87 million in service delivery costs, primarily due to our efforts to increase data center capacity, an increase of $10 million in allocated overhead and by an increase of amortization of purchased intangible assets of $9 million. For the six months ended July 31, 2018, the increase in absolute dollars was primarily due to the acquisition of MuleSoft during the three months ended July 31, 2018 an increase of $74 million in employee-related costs, an increase of $13 million in stock-based expenses, an increase of $159 million in service delivery costs, primarily due to our efforts to increase data center capacity, an increase of $14 million in allocated overhead and by an increase of amortization of purchased intangible assets of $4 million. We have increased our headcount by 15 percent since July 31, 2017 to meet the higher demand for services from our customers, of which a component was also due to the acquisition of MuleSoft in May 2018. We intend to continue to invest additional resources in our enterprise cloud computing services and data center capacity and security. We also plan to add additional employees in our professional services group to facilitate the adoption of our services. The timing of these expenses will affect our cost of revenues, both in terms of absolute dollars and as a percentage of revenues in future periods.

The cost of professional services and other revenues was $211 million and $405 million during the three and six months ended July 31, 2018 resulting in positive gross margins of $10 million and $12 million, respectively. We expect the cost of professional services to be approximately in line with revenues from professional services in future fiscal quarters. We believe that this investment in professional services facilitates the adoption of our service offerings and maintains our attrition rate.

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Operating Expenses.

	Three Months Ended July 31,		Variance
(in millions)	2018	2017	Dollars
Research and development	$463	$387	$ 76
Marketing and sales	1,504	1,153	351
General and administrative	350	283	67
Total operating expenses	$2,317	$1,823	$ 494
Percent of total revenues	71 %	71 %	

	Six Months Ended July 31,		Variance
(in millions)	2018	2017	Dollars
Research and development	$887	$763	$ 124
Marketing and sales	2,833	2,259	574
General and administrative	645	543	102
Total operating expenses	$4,365	$3,565	$ 800
Percent of total revenues	69 %	71 %	

Research and development expenses were $463 million, or 14 percent of total revenues, for the three months ended July 31, 2018, compared to $387 million, or 15 percent of total revenues, during the same period a year ago, an increase of $76 million. Research and development expenses were $887 million, or 14 percent of total revenues, for the six months ended July 31, 2018, compared to $763 million, or 15 percent of total revenues, during the same period a year ago, an increase of $124 million. For the three months ended July 31, 2018, the increase in absolute dollars was primarily due to our MuleSoft acquisition and to an increase of approximately $51 million in employee-related costs, an increase of $14 million in stock-based expenses, an increase in our development and test data center costs and allocated overhead. For the six months ended July 31, 2018, the increase in absolute dollars was primarily due to our MuleSoft acquisition and an increase of approximately $93 million in employee-related costs, an increase of $16 million in stock-based expenses, an increase in our development and test data center costs and allocated overhead. We increased our research and development headcount by 17 percent since July 31, 2017 in order to improve and extend our service offerings, develop new technologies, and integrate previously acquired companies, including our fiscal 2017 acquisitions. We expect that research and development expenses will increase in absolute dollars and may increase as a percentage of revenues in future periods as we continue to invest in additional employees and technology to support the development of new, and improve existing, technologies and the integration of acquired technologies.

Marketing and sales expenses were $1.5 billion, or 46 percent of total revenues, for the three months ended July 31, 2018, compared to $1.2 billion, or 45 percent of total revenues, during the same period a year ago, an increase of $351 million. Marketing and sales expenses were $2.8 billion, or 45 percent of total revenues, for the six months ended July 31, 2018, compared to $2.3 billion, or 45 percent of total revenues, during the same period a year ago, an increase of $574 million. For the three months ended July 31, 2018, the increase was primarily due to our MuleSoft acquisition and an increase of $194 million in employee-related costs and amortization of costs capitalized to obtain revenue contracts, an increase of $54 million in stock-based expenses and an increase of $19 million in advertising expenses. For the six months ended July 31, 2018, the increase was primarily due to an increase of $378 million in employee-related costs and amortization of costs capitalized to obtain revenue contracts, an increase of $55 million in stock-based expenses and an increase of $35 million in advertising expenses. Our marketing and sales headcount increased by 24 percent since July 31, 2017, of which a component was due to the acquisition of MuleSoft in May 2018. The increase in headcount was primarily attributable to hiring additional sales personnel to focus on adding new customers and increasing penetration within our existing customer base.

General and administrative expenses were $350 million, or 11 percent of total revenues, for the three months ended July 31, 2018, compared to $283 million, or 11 percent of total revenues, during the same period a year ago, an increase of $67 million. General and administrative expenses were $645 million, or 10 percent of total revenues, for the six months ended July 31, 2018, compared to $543 million, or 11 percent of total revenues, during the same period

a year ago, an increase of $102 million. The increases were primarily due to an increase in employee-related costs, as well as transaction costs related to the acquisitions of MuleSoft and Datorama. Our general and administrative headcount increased by 22 percent since July 31, 2017 as we added personnel to support our growth as well as an increase due to the acquisition of MuleSoft in May 2018.

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Other income and expense.

(in millions)	Three Months Ended July 31, 2018	2017	Variance Dollars
Investment income	$12	$ 9	$ 3
Interest expense	(39)	(22)	(17)
Gains (losses) on strategic investments, net	143	(8)	151

(in millions)	Six Months Ended July 31, 2018	2017	Variance Dollars
Investment income	$28	$14	$ 14
Interest expense	(73)	(44)	(29)
Gains (losses) on strategic investments, net	354	(5)	359
Other income	1	0	1

Investment income consists of income on our cash and marketable securities balances. Investment income was $12 million for the three months ended July 31, 2018 compared to $9 million during the same period a year ago. Investment income was $28 million for the six months ended July 31, 2018 compared to $14 million during the same period a year ago. The increase was due to greater investment yield on marketable security balances earned in the three and six months ended July 31, 2018.

Interest expense consists of interest on our debt, capital leases, and financing obligation related to 350 Mission. Interest expense was $39 million for the three months ended July 31, 2018 compared to $22 million during the same period a year ago. Interest expense was $73 million for the six months ended July 31, 2018 compared to $44 million during the same period a year ago. The increase was primarily driven by interest expense on the 2021 Term Loan, 2023 Senior Notes and 2028 Senior Notes of approximately 27 million. We expect interest expense to increase in future quarters as a result of the 2023 Senior Notes and 2028 Senior Notes.

Gains (losses) on strategic investments, net consists primarily of mark-to-market adjustments related to our publicly held equity securities, observable price adjustments related to our privately held equity securities, impairments on our privately held equity and debt securities, and any gains or losses as a result of sales. During the three and six months ended July 31, 2018, these adjustments and impairments resulted in net gains of approximately $143 million and $354 million, respectively. The gain for the three and six months ended July 31, 2018 was primarily due to the mark to market of one privately held investment and the fair value adjustment of our publicly held investments as a result of three initial public offerings. For the six months ended July 31, 2018, there were three initial public offerings which resulted in net unrealized gains of $247 million.

Other income primarily consists of non-operating transactions such as gains and losses from foreign exchange rate fluctuations and real estate transactions.

Benefit from (provision for) income taxes.

(in millions)	Three Months Ended July 31, 2018	2017	Variance Dollars
Benefit from (provision for) income taxes	$68	$(17)	$ 85
Effective tax rate	(29)%	27 %	

(in millions)	Six Months Ended July 31, 2018	2017	Variance Dollars

Benefit from (provision for) income taxes	$27	$(6)	$ 33
Effective tax rate	(4)%	11 %	

We recognized a tax benefit of $68 million on a pretax income of $231 million for the three months ended July 31, 2018 and a tax benefit of $27 million on a pretax income of $616 million for the six months ended July 31, 2018. Included in this tax amount was a discrete tax benefit of $139 million from a partial release of the valuation allowance in connection with the acquisition of MuleSoft. The net deferred tax liability from the acquisition of MuleSoft provided a source of additional income to support the realizability of our pre-existing deferred tax assets and, as a result, we released a portion of its valuation allowance. The tax benefit associated with the release of the valuation allowance was partially offset by income taxes in profitable jurisdictions outside of the United States.

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In fiscal 2018, we recorded a tax provision of $17 million on a pretax income of $63 million for the three months ended July 31, 2017 and a tax provision of $6 million on a pretax income of $53 million for the six months ended July 31, 2017. The tax provision recorded was primarily related to income taxes in profitable jurisdictions outside of the United States.

Liquidity and Capital Resources

At July 31, 2018, our principal sources of liquidity were cash, cash equivalents and marketable securities totaling $3.4 billion and accounts receivable of $2.0 billion. Our cash, cash equivalents and marketable securities are comprised primarily of corporate notes and obligations, U.S. treasury securities, asset backed securities, foreign government obligations, mortgage backed obligations, time deposits, money market mutual funds and municipal securities.

For the three and six months ended July 31, 2018 and 2017, our cash flows were as follows (in millions):

2	Three Months Ended July 31,		Six Months Ended July 31,	
	2018	2017	2018	2017
Net cash provided by operating activities	$458	$331	$1,924	$1,561
Net cash used in investing activities	(4,661)	(524)	(4,385)	(1,292)
Net cash provided by financing activities	589	117	2,214	68

Cash provided by operating activities has historically been affected by the amount of net income adjusted for non-cash expense items such as depreciation and amortization; amortization of purchased intangibles from business combinations; the expense associated with stock-based awards; net gains on strategic investments; the timing of employee related costs including commissions and bonus payments; the timing of payments against accounts payable, accrued expenses and other current liabilities; the timing of collections from our customers, which is our largest source of operating cash flows; the timing of business combination activity and the related integration and transaction costs; and changes in working capital accounts. Net cash provided by operating activities was also impacted by payments made during the three and six months ended July 31, 2018 for the transaction fees related to the acquisition of MuleSoft.

Our working capital accounts consist of accounts receivable, costs capitalized to obtain revenue contracts, prepaid assets and other current assets. Claims against working capital include accounts payable, accrued expenses, unearned revenue, and other current liabilities and payments related to our debt obligations. Our working capital may be impacted by factors in future periods such as billings to customers for subscriptions and support services, and the subsequent collection of those billings, certain amounts and timing of which are seasonal. Our working capital in some quarters may be impacted by adverse foreign currency exchange rate movements and this impact may increase as our working capital balances increase in our foreign subsidiaries. Our billings are also influenced by new business linearity within the quarters and across the quarters.

As described above in “Seasonal Nature of Unearned Revenue, Accounts Receivable and Operating Cash Flow,” our fourth quarter has historically been our strongest quarter for new business and renewals and, correspondingly, the first quarter has historically been the strongest for cash collections. The year on year compounding effect of this seasonality in both billing patterns and overall business causes both the value of invoices that we generate in the fourth quarter and cash collections in the first quarter to increase as a proportion of our total annual billings.

We generally invoice our customers for our subscription and services contracts in advance in annual installments. We typically issue renewal invoices in advance of the renewal service period, and depending on timing, the initial invoice for the subscription and services contract and the subsequent renewal invoice may occur in different quarters. Such invoice amounts are initially reflected in accounts receivable and unearned revenue, which is reflected on the balance sheets, and as the next billing cycle approaches, the corresponding unearned revenue decreases to zero. The operating cash flow benefit of increased billing activity generally occurs in the subsequent quarter when we collect from our customers. As such, our first quarter is our largest collections and operating cash flow quarter.

The net cash used in investing activities during the six months ended July 31, 2018 primarily related to the acquisition of MuleSoft and CloudCraze, net of cash acquired for $5.0 billion, sales and maturities of marketable securities of

$1.4 billion offset by purchases of marketable securities of $291 million, which partially facilitated cash outflows relating to the MuleSoft acquisition, purchases of strategic investments of $184 million and new office build outs and capital investments of $292 million. The net cash used in investing activities during the six months ended July 31, 2017 primarily related to purchases of marketable securities of $1.2 billion, new office build-outs and capital investments of $285 million, which were offset by the cash inflows for the period from sales and maturities of marketable securities of $256 million.

Net cash provided by financing activities during the six months ended July 31, 2018 consisted primarily of $3.0 billion from proceeds from issuance of debt, $383 million from proceeds from equity plans offset by $1.0 billion of principal payments on the maturity of the 0.25% Senior Notes. Net cash used in financing activities during the six months ended July 31, 2017 consisted primarily of $200 million in repayments of debt offset by $343 million from proceeds from equity plans.

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As of July 31, 2018, we have senior unsecured debt outstanding due in 2019, 2021, 2023, and 2028 with a total carrying value of $3.5 billion. In addition, we have senior secured notes outstanding related to our loan on 50 Fremont due in 2023 with a total carrying value of $199 million. We were in compliance with all debt covenants as of July 31, 2018.

In March 2013, we issued at par value $1.15 billion of 0.25% convertible senior notes ("0.25% Senior Notes"), due April 2018. During the six months ended July 31, 2018, the outstanding balance of the 0.25% Senior Notes matured and we repaid $1 billion in cash of principal balance. As of July 31, 2018, all 0.25% Senior Notes had been repaid in full and were no longer outstanding.

As of July 31, 2018, we have a total of $104 million in letters of credit outstanding in favor of certain landlords for office space. To date, no amounts have been drawn against the letters of credit, which renew annually and expire at various dates through December 2030.

We do not have any special purpose entities, and other than operating leases for office space and computer equipment, we do not engage in off-balance sheet financing arrangements.

Our principal commitments consist of obligations under leases for office space, co-location data center facilities and our development and test data center, as well as leases for computer equipment, software, furniture and fixtures, excluding all secured and unsecured debt. At July 31, 2018, the future non-cancelable minimum payments under these commitments were as follows (in millions):

	Capital Leases	Operating Leases	Financing Obligation - Leased Facility
Fiscal Period:			
Remaining six months of Fiscal 2019	$ 12	$ 369	$ 11
Fiscal 2020	202	692	22
Fiscal 2021	0	558	23
Fiscal 2022	0	374	23
Fiscal 2023	0	317	24
Thereafter	0	1,305	187
Total minimum lease payments	214	$ 3,615	$ 290
Less: amount representing interest	(9)		
Present value of capital lease obligations	$ 205		

The majority of our operating lease agreements provide us with the option to renew. Our future operating lease obligations would change if we exercised these options and if we entered into additional operating lease agreements as we expand our operations.

The financing obligation - leased facility above represents the total obligation for our lease of approximately 445,000 rentable square feet of office space at 350 Mission St. ("350 Mission") in San Francisco, California. As of July 31, 2018, $217 million of the total obligation noted above was recorded to Financing obligation - leased facility, of which the current portion is included in “Accounts payable, accrued expenses and other liabilities” and the noncurrent portion is included in “Other noncurrent liabilities” on the condensed consolidated balance sheets.

During fiscal 2019 and in future fiscal years, we have made and expect to continue to make additional investments in our infrastructure to scale our operations, increase productivity and enhance our security measures. We plan to upgrade or replace various internal systems to scale with our overall growth. Additionally, we expect capital expenditures to be higher in absolute dollars and remain consistent as a percentage of total revenues in future periods as a result of continued office build-outs, other leasehold improvements and data center investments.

We have entered into various contractual commitments with infrastructure service providers for a total commitment of $2.0 billion. As of July 31, 2018 the total remaining commitment is approximately $1.9 billion and $79 million is remaining to be paid this fiscal year.

In the future, we may enter into arrangements to acquire or invest in complementary businesses, services and technologies, and intellectual property rights. To facilitate these acquisitions or investments, we may seek additional

equity or debt financing, which may not be available on terms favorable to us or at all, which may affect our ability to complete subsequent acquisitions or investments, and which may affect the risks of owning our common stock.

We believe our existing cash, cash equivalents, marketable securities, cash provided by operating activities and, if necessary, our borrowing capacity under our Credit Facility will be sufficient to meet our working capital, capital expenditure and debt repayment needs over the next 12 months. We expect our cash tax payments for the next 12 months, primarily from

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profitable jurisdictions outside of the U.S, to be consistent with those paid in prior years. Additionally, the one-time transition tax under the Tax Act will not have an impact on our cash taxes based on our provisional assessment.

New Accounting Pronouncements

See Note 1 “Summary of Business and Significant Accounting Policies” to the condensed consolidated financial statements for our discussion about new accounting pronouncements adopted and those pending.

Environmental, Social and Governance

We believe the business of business is improving the state of the world for all of our stakeholders, including our stockholders, customers, employees, partners, community, environment and society. We are committed to creating a sustainable, low-carbon future by delivering a carbon neutral cloud, operating as a net-zero greenhouse gas emissions company and by working to achieve our goal of 100 percent renewable energy for our global operations. In fiscal 2018, we procured electricity from renewable energy resources equivalent to 50 percent of what we used globally and as of July 31, 2018, the three buildings at our corporate headquarters in San Francisco are sourcing 100 percent renewable energy. In addition, we have spearheaded initiatives to drive equality in four key areas: equal rights, equal pay, equal education and equal opportunity. We also pioneered and have inspired other companies to adopt our 1-1-1 integrated philanthropy model, which leverages one percent of a company’s equity, employee time and product to help improve communities around the world. Together with the Salesforce Foundation, a 501(c)(3) nonprofit organization, and Salesforce.org, a nonprofit social enterprise, which are not included in our consolidated financial statements, we have given approximately $230 million to charitable organizations, logged more than 3.2 million employee volunteer hours around the world and provided more than 37,000 nonprofit and higher education organizations with the use of our service offerings for free or at a discount.

We leverage a number of communications channels and strategic content to better serve and engage our many stakeholders. Our sustainability website, www.salesforce.com/company/sustainability, provides information regarding our environmental and other sustainability efforts, including our annual impact reports and our environmental policy. At our equality portal, www.salesforce.com/company/equality, our stakeholders can gain insights on our approach to equality, see our company profile by gender, and review our most recent Employer Information Report, which provides a snapshot in time of our U.S. demographics based on categories prescribed by the federal government. In addition, stakeholders can learn about equality through one of our many free Trailheads. Our annual proxy statement, as available on the Investor Relations website, https://investor.salesforce.com, or www.sec.gov, provides additional details on our corporate governance practices, including our board composition.

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ITEM 3. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

Foreign Currency Exchange Risk

We primarily conduct our business in the following locations: the United States, Europe, Canada, Asia Pacific and Japan. The expanding global scope of our business exposes us to risk of fluctuations in foreign currency markets. This exposure is the result of selling in multiple currencies, growth in our international investments, including data center expansion, additional headcount in foreign countries, and operating in countries where the functional currency is the local currency. Specifically, our results of operations and cash flows are subject to fluctuations in the following currencies: the Euro, British Pound Sterling, Canadian Dollar, Australian Dollar and Japanese Yen against the United States Dollar ("USD"). These exposures may change over time as business practices evolve and economic conditions change. Changes in foreign currency exchange rates could have an adverse impact on our financial results and cash flows.

Our European revenue, operating expenses and significant balance sheet accounts denominated in currencies other than the USD primarily flow through our United Kingdom subsidiary, which has a functional currency of the British Pound. This results in a two-step currency exchange process wherein the currencies in Europe other than the British Pound are first converted into the British Pound and then British Pounds are translated into USD for our Condensed Consolidated Financial Statements. As an example, costs incurred in France are translated from the Euro to the British Pound and then into the USD. Our statements of operations and balance sheet accounts are also impacted by the re-measurement of non-functional currency transactions such as USD denominated intercompany loans, cash accounts held by our overseas subsidiaries, accounts receivable denominated in foreign currencies and unearned revenue and accounts payable denominated in foreign currencies.

Foreign Currency Transaction Risk

Our foreign currency exposures typically arise from selling annual and multi-year subscriptions in multiple currencies, customer accounts receivable, intercompany transfer pricing arrangements and other intercompany transactions. Our foreign currency management objective is to minimize the effect of fluctuations in foreign exchange rates on selected assets or liabilities without exposing us to additional risk associated with transactions that could be regarded as speculative.

We pursue our objective by utilizing foreign currency forward contracts to offset foreign exchange risk. Our foreign currency forward contracts are generally short-term in duration. We neither use these foreign currency forward contracts for trading purposes nor do we currently designate these forward contracts as hedging instruments pursuant to Accounting Standards Codification 815 ("ASC 815"), Derivatives and Hedging. Accordingly, we record the fair values of these contracts as of the end of our reporting period to our condensed consolidated balance sheets with changes in fair values recorded to our condensed consolidated statements of operations. Given the short duration of the forward contracts, the amount recorded is not significant. Our ultimate realized gain or loss with respect to foreign currency exposures will generally depend on the size and type of cross-currency transactions that we enter into, the currency exchange rates associated with these exposures and changes in those rates, the net realized gain or loss on our foreign currency forward contracts and other factors.

Foreign Currency Translation Risk

Fluctuations in foreign currencies impact the amount of total assets, liabilities, revenues, operating expenses and cash flows that we report for our foreign subsidiaries upon the translation of these amounts into USD. Although the USD fluctuated against certain international currencies over the past several months, the amounts of revenue and unearned revenue that we reported in USD for foreign subsidiaries that transact in international currencies were similar to what we would have reported during the three months using a constant currency rate.

Interest Rate Sensitivity

We had cash, cash equivalents and marketable securities totaling $3.4 billion at July 31, 2018. This amount was invested primarily in money market funds, time deposits, corporate notes and bonds, government securities and other debt securities with credit ratings of at least BBB or better. The cash, cash equivalents and marketable securities are held for general corporate purposes, including acquisitions of, or investments in, complementary businesses, services or technologies, working capital and capital expenditures. Our investments are made for capital preservation purposes. We do not enter into investments for trading or speculative purposes.

Our cash equivalents and our portfolio of marketable securities are subject to market risk due to changes in interest rates. Fixed rate securities may have their market value adversely impacted due to a rise in interest rates, while floating rate securities may produce less income than expected if interest rates fall. Due in part to these factors, our future investment income may fall short of expectation due to changes in interest rates or we may suffer losses in principal if we are forced to sell securities that decline in market value due to changes in interest rates. However because we classify our debt securities as “available for sale,” no gains or losses are recognized due to changes in interest rates unless such securities are sold prior to maturity or declines in fair value are determined to be other-than-temporary.

An immediate increase or decrease in interest rates of 100-basis points at July 31, 2018 could result in a $23 million market value reduction or increase of the same amount. This estimate is based on a sensitivity model that measures market

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value changes when changes in interest rates occur. Fluctuations in the value of our investment securities caused by a change in interest rates (gains or losses on the carrying value) are recorded in other comprehensive income, and are realized only if we sell the underlying securities.

At January 31, 2018, we had cash, cash equivalents and marketable securities totaling $4.5 billion. The fixed-income portfolio was also subject to interest rate risk. Changes in interest rates of 100-basis points would have resulted in market value changes of $34 million.

Market Risk and Market Interest Risk

We deposit our cash with multiple financial institutions.

In addition, we maintain debt obligations that are subject to market interest risk, as follows (in millions):

Instrument	Maturity date	Principal Outstanding as of July 31, 2018	Interest Terms	Effective interest rate for the three months ended July 31, 2018
2021 Term Loan	May 2021	$ 500	Floating	2.88 %
2023 Senior Notes	April 2023	1,000	Fixed	3.26 %
2028 Senior Notes	April 2028	1,500	Fixed	3.70 %
2019 Term Loan	July 2019	500	Floating	2.87 %
Loan assumed on 50 Fremont	June 2023	200	Fixed	3.75 %
Revolving credit facility	April 2023	0	Floating	N/A

The 2021 Term Loan bears interest, at our option, at either a base rate plus a spread of 0.00% to 0.25% or an adjusted LIBOR rate plus a spread of 0.625% to 1.25%, in each case, with such spread being determined based on our credit rating. By entering into the 2021 Term Loan, we have assumed risks associated with variable interest rates based upon a variable base rate or LIBOR. Changes in the overall level of interest rates affect the interest expense that we recognize in our statements of operations. The 2021 Term Loan was signed in April 2018 and funds were received in May 2018.

The 2019 Term Loan bears interest at our option, at either a base rate plus a spread of 0.00% to 0.25% or an adjusted LIBOR rate plus a spread of 0.625% to 1.25%, in each case with such spread being determined based on our credit rating. By entering into the 2019 Term Loan, we have assumed risks associated with variable interest rates based upon a variable base rate or LIBOR. Changes in the overall level of interest rates affect the interest expense that we recognize in our statements of operations.

The borrowings under the Revolving Credit Facility bear interest, at our option, at a base rate plus a spread of 0.00% to 0.375% or an adjusted LIBOR rate plus a spread of 0.75% to 1.375%, in each case with such spread being determined based on the our credit rating. Regardless of what amounts, if any, are outstanding under the revolving credit facility, we are also obligated to pay an ongoing commitment fee on undrawn amounts at a rate of 0.05% to 0.175%, with such rate being based on our public debt rating, payable in arrears quarterly. As of July 31, 2018 there was no outstanding borrowing amount under the Revolving Credit Facility.

The bank counterparties to our derivative contracts potentially expose us to credit-related losses in the event of their nonperformance. To mitigate that risk, we only contract with counterparties who meet the minimum requirements under our counterparty risk assessment process. We monitor ratings, credit spreads and potential downgrades on at least a quarterly basis. Based on our on-going assessment of counterparty risk, we adjust our exposure to various counterparties. We generally enter into master netting arrangements, which reduce credit risk by permitting net settlement of transactions with the same counterparty. However, we do not have any master netting arrangements in place with collateral features.

We have an investment portfolio that includes strategic investments in public and privately held companies, which range from early-stage companies to more mature companies with established revenue streams and business models.

As of July 31, 2018, our portfolio, which consists of investments in over 225 privately held companies and four public companies, is primarily comprised of independent software vendors and system integrators. Our investments in these companies range from $0.1 million to over $100 million, with 19 investments individually equal to or in excess of approximately $10 million as of July 31, 2018.

We invest in early-to-late stage enterprise cloud companies for strategic reasons and to support key business initiatives to grow our ecosystem of partners and accelerate the adoption of cloud technologies. We invest in both domestic and international companies and currently hold investments in all of our regions: the Americas, Europe, and Asia Pacific. We plan to continue to invest in these types of strategic investments, including in companies representing targeted geographies and targeted business and technological initiatives, as opportunities arise that we find attractive.

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The primary purpose of our investments is to create an ecosystem of enterprise cloud companies, accelerate the growth of technology startups and system integrators and create the next generation of mobile applications and connected products. Therefore, we continually evaluate our investments in privately held and publicly traded companies. In certain cases, our ability to sell these investments may be impacted by contractual obligations to hold the securities for a set period of time after a public offering. Currently, three of our publicly held investments are subject to such a contractual obligation, which expire in the third quarter of fiscal 2019.

Upon adoption of ASU 2016-01 in the first fiscal quarter we are now required to record all fair value adjustments of our publicly traded and privately held equity investments through the statement of operations. As such we anticipate additional volatility to our statements of operations in future periods, due to changes in market prices of our investments in publicly held equity investments and the valuation and timing of observable price changes and impairments of our investments in privately held securities. These changes could be material based on market conditions and events.

In addition, the financial success of our investment in any company is typically dependent on a liquidity event, such as a public offering, acquisition or other favorable market event reflecting appreciation to the cost of our initial investment. All of our investments, particularly those in privately held companies, are therefore subject to a risk of partial or total loss of investment capital.

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ITEM 4. CONTROLS AND PROCEDURES

(a) Evaluation of Disclosure Controls and Procedures

Under the supervision and with the participation of our management, including our principal executive officers and principal financial officer, we conducted an evaluation of the effectiveness of the design and operation of our disclosure controls and procedures, as defined in Rules 13a-15(e) and 15d-15(e) under the Securities Exchange Act of 1934, as amended (the "Exchange Act"), as of the end of the period covered by this report.

In designing and evaluating our disclosure controls and procedures, management recognizes that any disclosure controls and procedures, no matter how well designed and operated, can provide only reasonable assurance of achieving the desired control objectives. In addition, the design of disclosure controls and procedures must reflect the fact that there are resource constraints and that management is required to apply its judgment in evaluating the benefits of possible controls and procedures relative to their costs.

Based on management's evaluation, our principal executive officers and principal financial officer concluded that our disclosure controls and procedures are designed to, and are effective to, provide assurance at a reasonable level that the information we are required to disclose in reports that we file or submit under the Exchange Act is recorded, processed, summarized and reported within the time periods specified in Securities and Exchange Commission rules and forms, and that such information is accumulated and communicated to our management, including our co-chief executive officers and chief financial officer, as appropriate, to allow timely decisions regarding required disclosures.

(b) Management's Report on Internal Control Over Financial Reporting

Under the supervision and with the participation of our management, including our principal executive officers and principal financial officer, we conducted an evaluation of any changes in our internal control over financial reporting (as such term is defined in Rules 13a-15(f) and 15d-15(f) under the Exchange Act) that occurred during our most recently completed fiscal quarter. Based on that evaluation, our principal executive officers and principal financial officer concluded that there has not been any material change in our internal control over financial reporting during the quarter covered by this report that materially affected, or is reasonably likely to materially affect, our internal control over financial reporting. We implemented internal controls to ensure we evaluated our controls and assessed the impact on our financial statements from the adoption of Accounting Standards Codification 606, Revenue from Contracts with Customers, effective February 1, 2018. There were no significant changes to our internal control over financial reporting due to the adoption of the new standard.

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PART II. OTHER INFORMATION

ITEM 1. LEGAL PROCEEDINGS

In the ordinary course of business, we are or may be involved in various legal or regulatory proceedings, claims, or purported class actions related to alleged infringement of third-party patents and other intellectual property rights, or alleged violation of commercial, corporate and securities, labor and employment, wage and hour, or other laws or regulations. We have been, and may in the future be put on notice and/or sued by third parties for alleged infringement of their proprietary rights, including patent infringement.

We evaluate all claims and lawsuits with respect to their potential merits, our potential defenses and counterclaims, settlement or litigation potential and the expected effect on us. Our technologies may be subject to injunction if they are found to infringe the rights of a third-party. In addition, many of our subscription agreements require us to indemnify our customers for third-party intellectual property infringement claims, which could increase the cost to us of an adverse ruling on such a claim.

The outcome of any claims or litigation, regardless of the merits, is inherently uncertain. Any claims and other lawsuits, and the disposition of such claims and lawsuits, whether through settlement or litigation, could be time-consuming and expensive to resolve, divert our attention from executing our business plan, result in efforts to enjoin our activities, lead to attempts by third parties to seek similar claims and, in the case of intellectual property claims, require us to change our technology, change our business practices, pay monetary damages or enter into short- or long-term royalty or licensing agreements.

In general, the resolution of a legal matter could prevent us from offering our service to others, could be material to our financial condition or cash flows, or both, or could otherwise adversely affect our operating results.

We make a provision for a liability relating to legal matters when it is both probable that a liability has been incurred and the amount of the loss can be reasonably estimated. These provisions are reviewed at least quarterly and adjusted to reflect the impacts of negotiations, estimated settlements, legal rulings, advice of legal counsel and other information and events pertaining to a particular matter. The outcomes of our legal proceedings and other contingencies are, however, inherently unpredictable and subject to significant uncertainties. As a result, we may not be able to reasonably estimate the amount or range of possible losses in excess of any amounts accrued, including losses that could arise as a result of application of non-monetary remedies, with respect to any contingencies, and our estimates may not prove to be accurate.

In our opinion, resolution of all current matters is not expected to have a material adverse impact on our condensed consolidated results of operations, cash flows or financial position. However, depending on the nature and timing of a given dispute or other contingency, an unfavorable resolution could materially affect our current or future results of operations or cash flows, or both, in a particular quarter.

See also Note 15, “Legal Proceedings and Claims” of the Notes to Condensed Consolidated Financial Statements included in Part I, Item 1 of this Quarterly Report in Form 10-Q.

ITEM 1A. RISK FACTORS

The risks and uncertainties described below are not the only ones facing us. Other events that we do not currently anticipate or that we currently deem immaterial also may affect our results of operations, cash flows and financial condition.

Risks Related to Our Business and Industry

If our security measures or those of our third-party data center hosting facilities, cloud computing platform providers, third-party service partners, or the underlying infrastructure of the internet are breached, and unauthorized access is obtained to a customer’s data, our data or our IT systems, or authorized access is blocked or disabled, our services may be perceived as not being secure, customers may curtail or stop using our services, and we may incur significant legal and financial exposure and liabilities.

Our services involve the storage and transmission of our customers’ and our customers' customers' proprietary and other sensitive data, including financial information and other personally identifiable information. While we have security measures in place, they may be breached as a result of efforts by individuals or groups of hackers and sophisticated organizations, including state-sponsored organizations or nation-states. Furthermore, our services

depend on the many different underlying networks and services that power the internet. Most of this infrastructure is not under our control or that of our vendors, partners, or customers, and it may itself be vulnerable to attacks. Our security measures could also be compromised by employee or contractor error or malfeasance, including through a product update that contains a vulnerability. Additionally, third parties may attempt to fraudulently induce employees or customers into disclosing sensitive information such as user

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names, passwords or other information to gain access to our customers' data, our data or our IT systems. Any of these security breaches or incidents could result in someone obtaining unauthorized access to, or the denial of authorized access to, our IT systems, our customers' data or our data, including our intellectual property and other confidential business information.

Because the techniques used to breach, obtain unauthorized access to, or sabotage IT systems change frequently, grow more complex over time, and generally are not recognized until launched against a target, we may be unable to anticipate or implement adequate measures to prevent against such techniques. Our services operate in conjunction with and are dependent on products and components across a broad ecosystem and, if there is a security vulnerability in one of these components, a security breach could occur. In addition, our internal IT systems continue to evolve and we are often early adopters of new technologies and new ways of sharing data and communicating internally and with partners and customers, which increases the complexity of our IT systems. These risks are mitigated by our ability to maintain and improve business and data governance policies and processes and internal security controls, including our ability to escalate and respond to known and potential risks.

In addition, our customers may authorize third-party technology providers to access their customer data, and some of our customers may not have adequate security measures in place to protect their data that is stored on our servers. Because we do not control our customers or third-party technology providers, or the processing of such data by third-party technology providers, we cannot ensure the integrity or security of such transmissions or processing. Malicious third parties may also conduct attacks designed to temporarily deny customers access to our services.

A security breach could expose us to a risk of loss or inappropriate use of proprietary and sensitive data, or the denial of access to this data. A security breach could also result in a loss of confidence in the security of our services, damage our reputation, negatively impact our future sales, disrupt our business and lead to legal liability. Finally, the detection, prevention and remediation of known or potential security vulnerabilities, including those arising from third-party hardware or software may result in additional direct and indirect costs, for example additional infrastructure capacity to mitigate any system degradation that could result from remediation efforts.

Defects or disruptions in our services could diminish demand for our services and subject us to substantial liability. Because our services are complex and incorporate a variety of hardware, proprietary software and third-party software, our services may have errors or defects that could result in unanticipated downtime for our subscribers and harm to our reputation and our business. Cloud services frequently contain undetected errors when first introduced or when new versions or enhancements are released. We have from time to time found defects in, and experienced disruptions to, our services and new defects or disruptions may occur in the future. Such defects could also create vulnerabilities that could inadvertently permit access to protected customer data. In addition, our customers may use our services in unanticipated ways that may cause a disruption in services for other customers attempting to access their data. As we acquire companies, we may encounter difficulty in incorporating the acquired technologies into our services and in augmenting the technologies to meet the quality standards that are consistent with our brand and reputation. Since our customers use our services for important aspects of their business, any errors, defects, disruptions in service or other performance problems could hurt our reputation and may damage our customers' businesses. As a result, customers could elect to not renew our services or delay or withhold payment to us. We could also lose future sales or customers may make warranty or other claims against us, which could result in an increase in our allowance for doubtful accounts, an increase in collection cycles for accounts receivable or the expense and risk of litigation.

Any interruptions or delays in services from third-parties, including data center hosting facilities, cloud computing platform providers and other hardware and software vendors, or from our inability to adequately plan for and manage service interruptions or infrastructure capacity requirements, could impair the delivery of our services and harm our business.

We currently serve our customers from third-party data center hosting facilities and cloud computing platform providers located in the United States and other countries. We also rely on computer hardware purchased or leased from, software licensed from, and cloud computing platforms provided by, third parties in order to offer our services, including database software, hardware and data from a variety of vendors. Any damage to, or failure of our systems generally, including the systems of our third-party platform providers, could result in interruptions in our services. We

have from time to time experienced interruptions in our services and such interruptions may occur in the future. Interruptions in our services may cause us to issue credits or pay penalties, cause customers to make warranty or other claims against us or to terminate their subscriptions and adversely affect our attrition rates and our ability to attract new customers, all of which would reduce our revenue. Our business would also be harmed if our customers and potential customers believe our services are unreliable.

We use a range of disaster recovery and business continuity arrangements. For many of our offerings, our production environment and customers' data are replicated in near real-time in a separate facility located elsewhere. Certain offerings, including some offerings of companies added through acquisitions, may be served through alternate facilities or arrangements. We do not control the operation of any of these facilities, and they may be vulnerable to damage or interruption from earthquakes, floods, fires, power loss, telecommunications failures and similar events. They may also be subject to break-ins, sabotage, intentional acts of vandalism and similar misconduct, as well as local administrative actions, changes to legal or

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permitting requirements and litigation to stop, limit or delay operation. Despite precautions taken at these facilities, such as disaster recovery and business continuity arrangements, the occurrence of a natural disaster or an act of terrorism, a decision to close the facilities without adequate notice or other unanticipated problems at these facilities could result in lengthy interruptions in our services.

These hardware, software, data and cloud computing platforms may not continue to be available at reasonable prices, on commercially reasonable terms or at all. Any loss of the right to use any of these hardware, software or cloud computing platforms could significantly increase our expenses and otherwise result in delays in the provisioning of our services until equivalent technology is either developed by us, or, if available, is identified, obtained through purchase or license and integrated into our services.

If we do not accurately plan for our infrastructure capacity requirements and we experience significant strains on our data center capacity, our customers could experience performance degradation or service outages that may subject us to financial liabilities, result in customer losses and harm our business. When we add data centers, capacity, and move to cloud computing platform providers, we may move or transfer our data and our customers' data. Despite precautions taken during this process, any unsuccessful data transfers may impair the delivery of our services, which may damage our business.

Privacy concerns and laws such as the European Union's General Data Protection Regulation, evolving regulation of cloud computing, cross-border data transfer restrictions and other domestic or foreign regulations may limit the use and adoption of our services and adversely affect our business.

Regulation related to the provision of services over the Internet is evolving, as federal, state and foreign governments continue to adopt new, or modify existing, laws and regulations addressing data privacy and the collection, processing, storage, transfer and use of data. In some cases, new data privacy laws and regulations, such as the European Union's ("EU") General Data Protection Regulation that took effect in May 2018, impose new obligations directly on Salesforce as both a data controller and a data processor, as well as on many of our customers. These new laws may require us to make changes to our services to enable Salesforce and/or our customers to meet the new legal requirements, and may also increase our potential liability exposure through higher potential penalties for non-compliance. Further, laws such as the European Union's proposed e-Privacy Regulation are increasingly aimed at the use of personal information for marketing purposes, and the tracking of individuals' online activities. These new or proposed laws and regulations are subject to differing interpretations and may be inconsistent among jurisdictions. These and other requirements could reduce demand for our services, require us to take on more onerous obligations in our contracts, restrict our ability to store, transfer and process data or, in some cases, impact our ability to offer our services in certain locations or our customers' ability to deploy our solutions globally. For example, ongoing legal challenges in Europe to the mechanisms allowing companies to transfer personal data from the European Economic Area to the United States could result in further limitations on the ability to transfer data across borders, particularly if governments are unable or unwilling to reach new or maintain existing agreements that support cross-border data transfers, such as the EU-U.S. and Swiss-U.S. Privacy Shield framework. Additionally, certain countries have passed or are considering passing laws requiring local data residency. The costs of compliance with, and other burdens imposed by, privacy laws, regulations and standards may limit the use and adoption of our services, reduce overall demand for our services, make it more difficult to meet expectations from or commitments to customers, lead to significant fines, penalties or liabilities for noncompliance, or slow the pace at which we close sales transactions, any of which could harm our business.

In addition to government activity, privacy advocacy and other industry groups have established or may establish new self-regulatory standards that may place additional burdens on our ability to provide our services globally. Our customers expect us to meet voluntary certification and other standards established by third parties, such as TRUSTe. If we are unable to maintain these certifications or meet these standards, it could adversely affect our ability to provide our solutions to certain customers and could harm our business.

Furthermore, concerns regarding data privacy may cause our customers' customers to resist providing the data necessary to allow our customers to use our services effectively. Even the perception that the privacy of personal information is not satisfactorily protected or does not meet regulatory requirements could inhibit sales of our products or services and could limit adoption of our cloud-based solutions.

Our efforts to expand our services beyond the CRM market and to develop and integrate our existing services in order to keep pace with technological developments may not succeed and may reduce our revenue growth rate and harm our business.

We derive a significant portion of our revenue from subscriptions to our CRM enterprise cloud computing application services, and we expect this will continue for the foreseeable future. Our efforts to expand our services beyond the CRM market may not succeed and may reduce our revenue growth rate. The markets for certain of our offerings remain relatively new and it is uncertain whether our efforts, and related investments, will ever result in significant revenue for us. Further, the introduction of significant platform changes and upgrades, including our conversion to our Lightning platform, and introduction of new

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services beyond the CRM market, may not be successful, and early stage interest and adoption of such new services may not result in long term success or significant revenue for us.

Additionally, if we fail to anticipate or identify significant Internet-related and other technology trends and developments early enough, or if we do not devote appropriate resources to adapting to such trends and developments, our business could be harmed.

If we are unable to develop enhancements to and new features for our existing or new services that keep pace with rapid technological developments, our business could be harmed. The success of enhancements, new features and services depends on several factors, including the timely completion, introduction and market acceptance of the feature, service or enhancement by customers, administrators and developers, as well as our ability to seamlessly integrate all of our service offerings. Failure in this regard may significantly impair our revenue growth as well as negatively impact our operating results if the additional costs are not offset by additional revenues. In addition, because our services are designed to operate over various network technologies and on a variety of mobile devices, operating systems and computer hardware and software platforms using a standard browser, we will need to continuously modify and enhance our services to keep pace with changes in Internet-related hardware, software, communication, browser, app development platform and database technologies, as well as continue to maintain and support our services on legacy systems. We may not be successful in either developing these modifications and enhancements or in bringing them to market timely. Furthermore, uncertainties about the timing and nature of new network platforms or technologies, or modifications to existing platforms or technologies, could increase our research and development or service delivery expenses. Any failure of our services to operate effectively with future network platforms and technologies could reduce the demand for our services, result in customer dissatisfaction and harm our business.

As we acquire and invest in companies or technologies, we may not realize the expected business or financial benefits and the acquisitions could prove difficult to integrate, disrupt our business, dilute stockholder value and adversely affect our operating results and the market value of our common stock.

As part of our business strategy, we periodically make investments in, or acquisitions of, complementary businesses, joint ventures, services and technologies and intellectual property rights, and we expect that we will continue to make such investments and acquisitions in the future. Acquisitions and investments involve numerous risks, including:

- potential failure to achieve the expected benefits of the combination or acquisition;
- difficulties in, and the cost of, integrating operations, technologies, services, platforms and personnel;
- diversion of financial and managerial resources from existing operations;
- the potential entry into new markets in which we have little or no experience or where competitors may have stronger market positions;
- potential write-offs of acquired assets or investments, and potential financial and credit risks associated with acquired customers;
- potential loss of key employees of the acquired company;
- inability to generate sufficient revenue to offset acquisition or investment costs;
- inability to maintain relationships with customers and partners of the acquired business;
- challenges converting the acquired company's revenue recognition policy from service accounting to revenue based on the transfer of control and appropriate allocation of the customer consideration to the individual deliverables;
- difficulty of transitioning the acquired technology onto our existing platforms and customer acceptance of multiple platforms on a temporary or permanent basis;
- augmenting the acquired technologies and platforms to the levels that are consistent with our brand and reputation;
- increasing or maintaining the security standards for acquired technology consistent with our other services;
- potential unknown liabilities associated with the acquired businesses;
- unanticipated expenses related to acquired technology and its integration into our existing technology;
- negative impact to our results of operations because of the depreciation and amortization of amounts related to acquired intangible assets, fixed assets and deferred compensation;
- additional stock based compensation; the loss of acquired unearned revenue and unbilled unearned revenue;
- delays in customer purchases due to uncertainty related to any acquisition;

- ineffective or inadequate controls, procedures and policies at the acquired company may negatively impact our results of operations;
- challenges caused by integrating operations over distance, and across different languages and cultures;

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- currency and regulatory risks associated with foreign countries and potential additional cybersecurity and compliance risks resulting from entry into new markets; and
- the tax effects and costs of any such acquisitions including the related integration into our tax structure.

Any of these risks could harm our business. In addition, to facilitate these acquisitions or investments, we may seek additional equity or debt financing, which may not be available on terms favorable to us or at all, which may affect our ability to complete subsequent acquisitions or investments, and which may affect the risks of owning our common stock. For example, if we finance acquisitions by issuing equity or convertible or other debt securities or loans, our existing stockholders may be diluted, or we could face constraints related to the terms of, and repayment obligation related to, the incurrence of indebtedness that could affect the market price of our common stock.

Industry-specific regulation and other requirements and standards are evolving and unfavorable industry-specific laws, regulations, interpretive positions or standards could harm our business.

Our customers and potential customers conduct business in a variety of industries, including financial services, the public sector, healthcare and telecommunications. Regulators in certain industries have adopted and may in the future adopt regulations or interpretive positions regarding the use of cloud computing and other outsourced services. The costs of compliance with, and other burdens imposed by, industry-specific laws, regulations and interpretive positions may limit our customers' use and adoption of our services and reduce overall demand for our services. Compliance with these regulations may also require us to devote greater resources to support certain customers, which may increase costs and lengthen sales cycles. For example, some financial services regulators have imposed guidelines for use of cloud computing services that mandate specific controls or require financial services enterprises to obtain regulatory approval prior to outsourcing certain functions. If we are unable to comply with these guidelines or controls, or if our customers are unable to obtain regulatory approval to use our services where required, our business may be harmed. In addition, an inability to satisfy the standards of certain voluntary third-party certification bodies that our customers may expect, such as an attestation of compliance with the Payment Card Industry (PCI) Data Security Standards, may have an adverse impact on our business and results. If in the future we are unable to achieve or maintain industry-specific certifications or other requirements or standards relevant to our customers, it may harm our business and adversely affect our results.

Further, in some cases, industry-specific laws, regulations or interpretive positions may also apply directly to us as a service provider. The interpretation of many of these statutes, regulations, and rulings is evolving in the courts and administrative agencies and an inability to comply may have an adverse impact on our business and results. Any failure or perceived failure by us to comply with such requirements could have an adverse impact on our business. For example, there are various statutes, regulations, and rulings relevant to the direct email marketing and text-messaging industries, including the Telephone Consumer Protection Act (TCPA) and related Federal Communication Commission (FCC) orders, which impose significant restrictions on the ability to utilize telephone calls and text messages to mobile telephone numbers as a means of communication, when the prior consent of the person being contacted has not been obtained. We are, and may in the future be, subject to one or more class-action lawsuits, as well as individual lawsuits, containing allegations that one of our businesses or customers violated the TCPA. A determination that we or our customers violated the TCPA or other communications-based statutes could expose us to significant damage awards that could, individually or in the aggregate, materially harm our business.

Supporting our existing and growing customer base could strain our personnel resources and infrastructure, and if we are unable to scale our operations and increase productivity, we may not be able to successfully implement our business plan.

We continue to experience significant growth in our customer base and personnel, which has placed a strain on our management, administrative, operational and financial infrastructure. We anticipate that additional investments in our internal infrastructure, data center capacity, research, customer support and development, and real estate spending will be required to scale our operations and increase productivity, to address the needs of our customers, to further develop and enhance our services, to expand into new geographic areas, and to scale with our overall growth. The additional investments we are making will increase our cost base, which will make it more difficult for us to offset any future revenue shortfalls by reducing expenses in the short term.

We regularly upgrade or replace our various software systems. If the implementations of these new applications are delayed, or if we encounter unforeseen problems with our new systems or in migrating away from our existing applications and systems, our operations and our ability to manage our business could be negatively impacted.

Our success will depend in part upon the ability of our senior management to manage our projected growth effectively. To do so, we must continue to increase the productivity of our existing employees and to hire, train and manage new employees as needed. To manage the expected domestic and international growth of our operations and personnel, we will need to continue to improve our operational, financial and management controls, our reporting systems and procedures, and our utilization of real estate. If we fail to successfully scale our operations and increase productivity, we may be unable to execute our business plan and the fair value of our common stock could decline.

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The market in which we participate is intensely competitive, and if we do not compete effectively, our operating results could be harmed.

The market for enterprise applications and platform services is highly competitive, rapidly evolving and fragmented, and subject to changing technology, shifting customer needs and frequent introductions of new products and services. Many prospective customers have invested substantial personnel and financial resources to implement and integrate their current enterprise software into their businesses and therefore may be reluctant or unwilling to migrate away from their current solution to an enterprise cloud computing application service. Additionally, third-party developers may be reluctant to build application services on our platform since they have invested in other competing technology platforms.

Our current competitors include:

- Vendors of packaged business software, as well as companies offering enterprise apps delivered through on-premises offerings from enterprise software application vendors and cloud computing application service providers, either individually or with others;
- Software companies that provide their product or service free of charge, and only charge a premium for advanced features and functionality;
- Internally developed enterprise applications (by our potential customers' IT departments);
- Marketing vendors, which may be specialized in advertising, targeting, messaging, or campaign automation;
- E-commerce solutions from emerging cloud-only vendors and established on-premises vendors;
- Integration software vendors, integration service providers and API management providers;
- Traditional platform development environment companies and cloud computing development platform companies who may develop toolsets and products that allow customers to build new apps that run on the customers' current infrastructure or as hosted services;
- IoT platforms from large companies that have existing relationships with hardware and software companies; and
- Artificial intelligence solutions from new startups and established companies.

Some of our current and potential competitors may have competitive advantages, such as greater name recognition, longer operating histories, significant installed bases, broader geographic scope, and larger marketing budgets, as well as substantially greater financial, technical, and other resources. In addition, many of our current and potential competitors have established marketing relationships and access to larger customer bases, and have major distribution agreements with consultants, system integrators and resellers. We also experience competition from smaller, younger competitors that may be more agile in responding to customers' demands. As a result, our competitors may be able to respond more quickly and effectively than we can to new or changing opportunities, technologies, standards or customer requirements. Furthermore, because of these advantages, even if our services are more effective than the products and services that our competitors offer, potential customers might select competitive products and services in lieu of purchasing our services. For all of these reasons, we may not be able to compete successfully against our current and future competitors, which could negatively impact our future sales and harm our business.

Our ability to deliver our services is dependent on the development and maintenance of the infrastructure of the Internet by third parties.

The Internet's infrastructure is comprised of many different networks and services that are highly fragmented and distributed by design. This infrastructure is run by a series of independent third-party organizations that work together to provide the infrastructure and supporting services of the Internet under the governance of the Internet Corporation for Assigned Numbers and Names (ICANN) and the Internet Assigned Numbers Authority (IANA), now under the stewardship of ICANN.

The Internet has experienced a variety of outages and other delays as a result of damages to portions of its infrastructure, denial-of-service attacks or related cyber incidents, and it could face outages and delays in the future. These outages and delays could reduce the level of Internet usage or result in fragmentation of the Internet, resulting in multiple separate Internets. These scenarios are not under our control and could reduce the availability of the Internet to us or our customers for delivery of our Internet-based services. Any resulting interruptions in our services or the ability of our customers to access our services could result in a loss of potential or existing customers and harm our business.

In addition, certain countries have implemented (or may implement) legislative and technological actions that either do or can effectively regulate access to the Internet, including the ability of Internet Service Providers to limit access to specific websites or content. These actions could potentially limit or interrupt access to our services from certain countries or Internet Service Providers, impede our growth, result in the loss of potential or existing customers and harm our business.

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We are subject to risks associated with our strategic investments including partial or complete loss of invested capital. Significant changes in the fair value of this portfolio, including changes in the market prices of our investments in public companies and other-than-temporary impairments, could negatively impact our financial results.

We invest in early-to-late stage companies for strategic reasons and to support key business initiatives, and may not realize a return on our strategic investments. Many such companies generate net losses and the market for their products, services or technologies may be slow to develop, and, therefore, are dependent on the availability of later rounds of financing from banks or investors on favorable terms to continue their operations. The financial success of our investment in any company is typically dependent on a liquidity event, such as a public offering, acquisition or other favorable market event reflecting appreciation to the cost of our initial investment. The capital markets for public offerings and acquisitions are dynamic and the likelihood of liquidity events for the companies we have invested in could significantly worsen.

Further, valuations of privately held companies are inherently complex due to the lack of readily available market data. In addition, we may experience additional volatility to our statements of operations due to changes in market prices of our investments in publicly held equity investments and the valuation and timing of observable price changes or impairments of our investments in privately held securities. This volatility has been material to our results in any given quarter and may cause our stock price to decline.

All of our investments, especially our investments in privately held companies, are subject to a risk of a partial or total loss of investment capital.

Our quarterly results are likely to fluctuate, which may cause the value of our common stock to decline substantially.

Our quarterly results are likely to fluctuate. For example, our fiscal fourth quarter has historically been our strongest quarter for new business and renewals. The year-over-year compounding effect of this seasonality in billing patterns and overall new business and renewal activity causes the value of invoices that we generate in the fourth quarter to continually increase in proportion to our billings in the other three quarters of our fiscal year. As a result, our fiscal first quarter is our largest collections and operating cash flow quarter.

Additionally, some of the important factors that may cause our revenues, operating results and cash flows to fluctuate from quarter to quarter include:

- our ability to retain and increase sales to existing customers, attract new customers and satisfy our customers' requirements;
- the attrition rates for our services;
- the rate of expansion and productivity of our sales force;
- the length of the sales cycle for our services;
- new product and service introductions by our competitors;
- our success in selling our services to large enterprises;
- our ability to realize benefits from strategic partnerships, acquisitions or investments;
- general economic conditions, which may adversely affect either our customers' ability or willingness to purchase additional subscriptions or upgrade their services, or delay a prospective customer's purchasing decision, reduce the value of new subscription contracts, or affect attrition rates;
- variations in the revenue mix of our services and growth rates of our cloud subscription and support offerings, such variations in our revenue mix can also include the timing of software license sales and sales offerings that include an on-premise software element for which the revenue allocated to that deliverable is recognized upfront;
- changes in our pricing policies and terms of contracts, whether initiated by us or as a result of competition;
- changes in payment terms and the timing of customer payments and payment defaults by customers;
- changes in unearned revenue and the remaining performance obligation of our customers, due to seasonality, the compounding effects of renewals, invoice duration, size and timing, new business linearity between quarters and within a quarter and fluctuations due to foreign currency movements, all of which may impact implied growth rates;
- the seasonality of our customers' businesses, especially Commerce Cloud customers, including retailers and branded manufacturers;
- changes in foreign currency exchange rates such as with respect to the British Pound;
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- the amount and timing of operating costs and capital expenditures related to the operations and expansion of our business;
- the number of new employees;

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- the timing of commission, bonus, and other compensation payments to employees;
- the cost, timing and management effort for the introduction of new features to our services;
- the costs associated with acquiring new businesses and technologies and the follow-on costs of integration and consolidating the results of acquired businesses;
- expenses related to our real estate, our office leases and our data center capacity and expansion;
- timing of additional investments in our enterprise cloud computing application and platform services and in our consulting services;
- expenses related to significant, unusual or discrete events, which are recorded in the period in which the events occur;
- extraordinary expenses such as litigation or other dispute-related settlement payments;
- income tax effects, including the impact of changes in U.S. federal and state and international tax laws applicable to corporate multinationals;
- the timing of payroll and other withholding tax expenses, which are triggered by the payment of bonuses and when employees exercise their vested stock awards;
- technical difficulties or interruptions in our services;
- changes in interest rates and our mix of investments, which would impact the return on our investments in cash and marketable securities;
- conditions, particularly sudden changes, in the financial markets, which have impacted and may continue to impact the value of and liquidity of our investment portfolio;
- changes in the fair value of our strategic investments in early-to-late stage privately held and public companies, which have been and could continue to be material in a particular quarter;
- equity issuances, including as consideration in acquisitions;
- the timing of stock awards to employees and the related adverse financial statement impact of having to expense those stock awards on a straight-line basis over their vesting schedules;
- evolving regulations of cloud computing and cross-border data transfer restrictions and similar regulations;
- regulatory compliance costs; and
- the impact of new accounting pronouncements and associated system implementations, for example, the adoption of Accounting Standards Update No. 2014-09, “Revenue from Contracts with Customers (Topic 606)” (“ASU 2014-09”), which includes the accounting for revenue recognized and capitalized costs.

Many of these factors are outside of our control, and the occurrence of one or more of them might cause our operating results to vary widely. If we fail to meet or exceed operating results expectations or if securities analysts and investors have estimates and forecasts of our future performance that are unrealistic or that we do not meet, the market price of our common stock could decline. In addition, if one or more of the securities analysts who cover us adversely change their recommendation regarding our stock, the market price of our common stock could decline.

If we experience significant fluctuations in our rate of anticipated growth and fail to balance our expenses with our revenue forecasts, our business could be harmed and the market price of our common stock could decline.

Due to the pace of change and innovation in enterprise cloud computing services, the unpredictability of future general economic and financial market conditions, the impact of foreign currency exchange rate fluctuations, the growing complexity of our business, including the use of multiple pricing and packaging models, and our increasing focus on enterprise cloud computing services, we may not be able to realize our projected revenue growth plans. We plan our expense levels and investment on estimates of future revenue and future anticipated rate of growth. We may not be able to adjust our spending appropriately if the addition of new subscriptions or the renewals of existing subscriptions fall short of our expectations. A portion of our expenses may also be fixed in nature for some minimum amount of time, such as with costs capitalized to obtain revenue contracts, data center contracts or office leases, so it may not be possible to reduce costs in a timely manner, or at all, without the payment of fees to exit certain obligations early. As a result, we expect that our revenues, operating results and cash flows may fluctuate significantly on a quarterly basis and revenue growth rates may not be sustainable and may decline in the future, and we may not be able to provide continued operating margin expansion, which could harm our business and cause the market price of our common stock to decline.

Sales to customers outside the United States expose us to risks inherent in international operations.

We sell our services throughout the world and are subject to risks and challenges associated with international business. We intend to continue to expand our international sales efforts. The risks and challenges associated with sales to customers outside the United States or those that can affect international operations generally, include:

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- localization of our services, including translation into foreign languages and associated expenses;
- regulatory frameworks or business practices favoring local competitors;
- pressure on the creditworthiness of sovereign nations, particularly in Europe, where we have customers and a balance of our cash, cash equivalents and marketable securities;
- evolving domestic and international tax environments;
- liquidity issues or political actions by sovereign nations, which could result in decreased values of these balances or potential difficulties protecting our foreign assets or satisfying local obligations;
- foreign currency fluctuations and controls, which may make our services more expensive for international customers and could add volatility to our operating results;
- compliance with multiple, conflicting, ambiguous or evolving governmental laws and regulations, including employment, tax, privacy, anti-corruption, import/export, antitrust, data transfer, storage and protection, and industry-specific laws and regulations, including rules related to compliance by our third-party resellers;
- regional data privacy laws and other regulatory requirements that apply to outsourced service providers and to the transmission of our customers' data across international borders;
- treatment of revenue from international sources and changes to tax codes, including being subject to foreign tax laws and being liable for paying withholding income or other taxes in foreign jurisdictions;
- different pricing environments;
- difficulties in staffing and managing foreign operations;
- different or lesser protection of our intellectual property;
- longer accounts receivable payment cycles and other collection difficulties;
- natural disasters, acts of war, terrorism, pandemics or security breaches; and
- regional economic and political conditions.

Any of these factors could negatively impact our business and results of operations. The above factors may also negatively impact our ability to successfully expand into emerging market countries, where we have little or no operating experience, where it can be costly and challenging to establish and maintain operations, including hiring and managing required personnel, and difficult to promote our brand, and where we may not benefit from any first-to-market advantage or otherwise succeed.

Because we recognize revenue from subscriptions for our services over the term of the subscription, downturns or upturns in new business may not be immediately reflected in our operating results.

We generally recognize revenue from customers ratably over the terms of their subscription agreements, which are typically 12 to 36 months. As a result, most of the revenue we report in each quarter is the result of subscription agreements entered into during previous quarters. Consequently, a decline in new or renewed subscriptions in any one quarter may not be reflected in our revenue results for that quarter. Any such decline, however, will negatively impact our revenue in future quarters. Accordingly, the effect of significant downturns in sales and market acceptance of our services, and potential changes in our attrition rate, may not be fully reflected in our results of operations until future periods. Our subscription model also makes it difficult for us to rapidly increase our revenue through additional sales in any period, as revenue from new customers must be recognized over the applicable subscription term.

If our customers do not renew their subscriptions for our services or reduce the number of paying subscriptions at the time of renewal, our revenue could decline and our business may suffer. If we cannot accurately predict subscription renewals or upgrade rates, we may not meet our revenue targets, which may adversely affect the market price of our common stock.

Our customers have no obligation to renew their subscriptions for our services after the expiration of their contractual subscription period, which is typically 12 to 36 months, and in the normal course of business, some customers have elected not to renew. In addition, our customers may renew for fewer subscriptions, renew for shorter contract lengths, or switch to lower cost offerings of our services. It is difficult to predict attrition rates given our varied customer base of enterprise and small and medium size business customers and the number of multi-year subscription contracts. Our attrition rates may increase or fluctuate as a result of a number of factors, including customer dissatisfaction with our services, customers' spending levels, mix of customer base, decreases in the number of users at our customers, competition, pricing increases or changes and deteriorating general economic conditions.

Our future success also depends in part on our ability to sell additional features and services, more subscriptions or enhanced editions of our services to our current customers. This may also require increasingly sophisticated and costly sales efforts that are targeted at senior management. Similarly, the rate at which our customers purchase new or enhanced services

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depends on a number of factors, including general economic conditions and that our customers do not react negatively to any price changes related to these additional features and services.

If customers do not renew their subscriptions, do not purchase additional features or enhanced subscriptions or if attrition rates increase, our business could be harmed.

If third-party developers and providers do not continue to embrace our technology delivery model and enterprise cloud computing services, or if our customers seek warranties from us for third-party applications, integrations, data and content, our business could be harmed.

Our success depends on the willingness of a growing community of third-party developers and technology providers to build applications and provide integrations, data and content that are complementary to our services. Without the continued development of these applications and provision of such integrations, data and content, both current and potential customers may not find our services sufficiently attractive, which could impact future sales. In addition, for those customers who authorize a third-party technology partner access to their data, we do not provide any warranty related to the functionality, security and integrity of the data transmission or processing. Despite contract provisions to protect us, customers may look to us to support and provide warranties for the third-party applications, integrations, data and content, even though not developed or sold by us, which may expose us to potential claims, liabilities and obligations, all of which could harm our business.

We are exposed to fluctuations in currency exchange rates that could negatively impact our financial results and cash flows from changes in the value of the U.S. Dollar versus local currencies and the Euro versus the Pound Sterling.

We conduct our business in the following regions: the Americas, Europe and Asia Pacific. The expanding global scope of our business exposes us to risk of fluctuations in foreign currency markets. This exposure is the result of selling in multiple currencies, growth in our international investments, including data center expansion, additional headcount in foreign locations, and operating in countries where the functional currency is the local currency. Specifically, our results of operations and cash flows are subject to fluctuations primarily in British Pound Sterling, Euro, Japanese Yen, Canadian Dollar and Australian Dollar against the U.S. Dollar as well as the Euro against the Pound Sterling. These exposures may change over time as business practices evolve, economic conditions change and evolving tax regulations come into effect. The fluctuations of currencies in which we conduct business can both increase and decrease our overall revenue and expenses for any given fiscal period. Additionally, global political events, including the United Kingdom’s 2016 vote in favor of exiting the European Union, or “Brexit,” and similar geopolitical developments and fluctuating commodity prices, have caused global economic uncertainty, which could amplify the volatility of currency fluctuations. Such volatility, even when it increases our revenues or decreases our expenses, impacts our ability to predict our future results and earnings accurately. Although we attempt to mitigate some of this volatility and related risks through foreign currency hedging, our hedging activities are limited in scope and may not effectively offset the adverse financial impacts that may result from unfavorable movements in foreign currency exchange rates, which could adversely affect our financial condition or results of operations.

As more of our sales efforts are targeted at larger enterprise customers, our sales cycle may become more time-consuming and expensive, we may encounter pricing pressure and implementation and configuration challenges, and we may have to delay revenue recognition for some complex transactions, all of which could harm our business and operating results.

As we target more of our sales efforts at larger enterprise customers, including governmental entities, we may face greater costs, longer sales cycles, greater competition and less predictability in completing some of our sales. In this market segment, the customer’s decision to use our services may be an enterprise-wide decision and, if so, these types of sales would require us to provide greater levels of education regarding the use and benefits of our services, as well as education regarding privacy and data protection laws and regulations to prospective customers with international operations. In addition, larger customers and governmental entities may demand more configuration, integration services and features. As a result of these factors, these sales opportunities may require us to devote greater sales support and professional services resources to individual customers, driving up costs and time required to complete sales and diverting our own sales and professional services resources to a smaller number of larger transactions, while potentially requiring us to delay revenue recognition on some of these transactions until the technical or implementation requirements have been met.

Pricing and packaging strategies for enterprise and other customers for subscriptions to our existing and future service offerings may not be widely accepted by other new or existing customers. Our adoption of such new pricing and packaging strategies may harm our business.

For large enterprise customers, professional services may also be performed by a third party or a combination of our own staff and a third-party. Our strategy is to work with third parties to increase the breadth of capability and depth of capacity for delivery of these services to our customers. If a customer is not satisfied with the quality of work performed by us or a third-party or with the type of services or solutions delivered, then we could incur additional costs to address the situation, the profitability of that work might be impaired, and the customer's dissatisfaction with our services could damage our ability to obtain additional work from that customer. In addition, negative publicity related to our customer relationships, regardless of its

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accuracy, may further damage our business by affecting our ability to compete for new business with current and prospective customers.

We have been and may in the future be sued by third parties for various claims including alleged infringement of proprietary rights.

We are involved in various legal matters arising from the normal course of business activities. These may include claims, suits, government investigations and other proceedings involving alleged infringement of third-party patents and other intellectual property rights, commercial, corporate and securities, labor and employment, class actions, wage and hour, and other matters.

The software and Internet industries are characterized by the existence of a large number of patents, trademarks and copyrights and by frequent litigation based on allegations of infringement or other violations of intellectual property rights. We have received in the past and may receive in the future communications from third parties, including practicing entities and non-practicing entities, claiming that we have infringed their intellectual property rights.

In addition, we have been, and may in the future be, sued by third parties for alleged infringement of their claimed proprietary rights. Our technologies may be subject to injunction if they are found to infringe the rights of a third-party or we may be required to pay damages, or both. Further, many of our subscription agreements require us to indemnify our customers for third-party intellectual property infringement claims, which would increase the cost to us of an adverse ruling on such a claim.

Our exposure to risks associated with various claims, including the use of intellectual property, may be increased as a result of acquisitions of other companies. For example, we may have a lower level of visibility into the development process with respect to intellectual property or the care taken to safeguard against infringement risks with respect to the acquired company or technology. In addition, third parties may make infringement and similar or related claims after we have acquired technology that had not been asserted prior to our acquisition.

The outcome of any claims or litigation, regardless of the merits, is inherently uncertain. Any claims and lawsuits, and the disposition of such claims and lawsuits, whether through settlement or licensing discussions, or litigation, could be time-consuming and expensive to resolve, divert management attention from executing our business plan, result in efforts to enjoin our activities, lead to attempts on the part of other parties to pursue similar claims and, in the case of intellectual property claims, require us to change our technology, change our business practices, pay monetary damages or enter into short- or long-term royalty or licensing agreements.

Any adverse determination related to intellectual property claims or other litigation could prevent us from offering our services to others, could be material to our financial condition or cash flows, or both, or could otherwise adversely affect our operating results. In addition, depending on the nature and timing of any such dispute, an unfavorable resolution of a legal matter could materially affect our current or future results of operations or cash flows in a particular quarter.

Any failure to protect our intellectual property rights could impair our ability to protect our proprietary technology and our brand, cause us to incur significant expenses and harm our business.

If we fail to protect our intellectual property rights adequately, our competitors may gain access to our technology, affecting our brand, causing us to incur significant expenses and harming our business. Any of our patents, trademarks or other intellectual property rights may be challenged by others or invalidated through administrative process or litigation. While we have many U.S. patents and pending U.S. and international patent applications, we may be unable to obtain patent protection for the technology covered in our patent applications or the patent protection may not be obtained quickly enough to meet our business needs. In addition, our existing patents and any patents issued in the future may not provide us with competitive advantages, or may be successfully challenged by third parties. Furthermore, legal standards relating to the validity, enforceability and scope of protection of intellectual property rights are uncertain, and we also may face proposals to change the scope of protection for some intellectual property rights in the U.S. Effective patent, trademark, copyright and trade secret protection may not be available to us in every country in which our services are available. The laws of some foreign countries may not be as protective of intellectual property rights as those in the U.S., and mechanisms for enforcement of intellectual property rights may be inadequate. Also, our involvement in standard setting activity or the need to obtain licenses from others may require us to license our intellectual property. Accordingly, despite our efforts, we may be unable to prevent third parties from

using our intellectual property.

We may be required to spend significant resources and expense to monitor and protect our intellectual property rights. We may initiate claims or litigation against third parties for infringement of our proprietary rights or to establish the validity of our proprietary rights. If we fail to protect our intellectual property rights, it could impact our ability to protect our technology and brand. Furthermore, any litigation, whether or not it is resolved in our favor, could result in significant expense to us, cause us to divert time and resources and harm our business.

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Our continued success depends on our ability to maintain and enhance our brands.

We believe that the brand identities we have developed have significantly contributed to the success of our business. Maintaining and enhancing the Salesforce brand and our other brands are critical to expanding our base of customers, partners and employees. Our brand strength will depend largely on our ability to remain a technology leader and continue to provide high-quality innovative products, services, and features securely, reliably and in a manner that enhances our customers' success. In order to maintain and enhance our brands, we may be required to make substantial investments that may later prove to be unsuccessful. In addition, positions we take on social issues may be unpopular with some customers or potential customers, which may impact our ability to attract or retain such customers. Our brand is also associated with our public commitments to sustainability and equality, and any perceived changes in our dedication to these commitments could adversely impact our relationships with our customers. In addition, we have secured the naming rights to facilities controlled by third parties, such as office towers and a transit center, and any negative events or publicity arising from these facilities could adversely impact our brand. If we fail to maintain and enhance our brands, or if we incur excessive expenses in our efforts to do so, our business, operating results and financial condition may be materially and adversely affected.

We may lose key members of our management team or development and operations personnel, and may be unable to attract and retain employees we need to support our operations and growth.

Our success depends substantially upon the continued services of our executive officers and other key members of management, particularly our co-chief executive officers. From time to time, there may be changes in our executive management team resulting from the hiring or departure of executives. Such changes in our executive management team may be disruptive to our business. We are also substantially dependent on the continued service of our existing development and operations personnel because of the complexity of our services and technologies. We do not have employment agreements with any of our executive officers, key management, development or operations personnel and they could terminate their employment with us at any time. The loss of one or more of our key employees or groups could seriously harm our business.

In the technology industry, there is substantial and continuous competition for engineers with high levels of experience in designing, developing and managing software and Internet-related services, as well as competition for sales executives, data scientists and operations personnel. We may not be successful in attracting and retaining qualified personnel. We have from time to time experienced, and we expect to continue to experience, difficulty in hiring and retaining highly skilled employees with appropriate qualifications. These difficulties may be amplified by evolving restrictions on immigration, travel or availability of visas for skilled technology workers. If we fail to attract new personnel or fail to retain and motivate our current personnel, our business and future growth prospects could be severely harmed.

In addition, we believe in the importance of our corporate culture of Ohana, which fosters dialogue, collaboration, recognition and a sense of family. As our organization grows and expands globally, and as employees’ workplace expectations develop, we may find it increasingly difficult to maintain the beneficial aspects of our corporate culture. This could negatively impact our ability to attract and retain employees and negatively impact our future growth.

Any failure in our delivery of high-quality technical support services may adversely affect our relationships with our customers and our financial results.

Our customers depend on our support organization to resolve technical issues relating to our applications. We may be unable to respond quickly enough to accommodate short-term increases in customer demand for support services. Increased customer demand for these services, without corresponding revenues, could increase costs and adversely affect our operating results. In addition, our sales process is highly dependent on our applications and business reputation and on positive recommendations from our existing customers. Any failure to maintain high-quality technical support, or a market perception that we do not maintain high-quality support, could adversely affect our reputation, our ability to sell our service offerings to existing and prospective customers, and our business, operating results and financial position.

Periodic changes to our sales organization can be disruptive and may reduce our rate of growth.

We periodically change and make adjustments to our sales organization in response to market opportunities, competitive threats, management changes, product introductions or enhancements, acquisitions, sales performance,

increases in sales headcount, cost levels and other internal and external considerations. Any such future sales organization changes may result in a temporary reduction of productivity, which could negatively impact our rate of growth. In addition, any significant change to the way we structure our compensation of our sales organization may be disruptive and may affect our revenue growth.

Unanticipated changes in our effective tax rate and additional tax liabilities may impact our financial results.

We are subject to income taxes in the United States and various jurisdictions outside of the United States. Our effective tax rate could fluctuate due to changes in the mix of earnings and losses in countries with differing statutory tax rates. Our tax expense could also be impacted by changes in non-deductible expenses, changes in excess tax benefits of stock-based compensation, changes in the valuation of deferred tax assets and liabilities and our ability to utilize them, the applicability of withholding taxes and effects from acquisitions.

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We are subject to tax examinations in multiple jurisdictions. While we regularly evaluate new information that may change our judgment resulting in recognition, derecognition or change in measurement of a tax position taken, there can be no assurance that the final determination of any examinations will not have an adverse effect on our operating results and financial position.

Our tax provision could also be impacted by changes in accounting principles, and changes in U.S. federal and state or international tax laws applicable to corporate multinationals. For example, the 2017 U.S. Tax Cuts and Jobs Act ("Tax Act") significantly changed income tax law that affect U.S. corporations. We made significant judgments and assumptions in the interpretation of this new law and in our calculations of the provisional amounts reflected in our financial statements. The U.S. Treasury Department, the Internal Revenue Service ("IRS"), and other standard-setting bodies may issue guidance on how the provisions of the Tax Act will be applied or otherwise administered, and additional accounting guidance or interpretations may be issued in the future that is different from our current interpretation. As we further analyze the new law, and collect relevant information to complete our computations of the related accounting impact, we may make adjustments to the provisional amounts that could materially affect our provision for income taxes in the period in which the adjustments are made. In addition, other countries are considering fundamental tax law changes. Any changes in taxing jurisdictions' administrative interpretations, decisions, policies and positions could also impact our tax liabilities.

We may also be subject to additional tax liabilities and penalties due to changes in non-income based taxes resulting from changes in federal, state or international tax laws, changes in taxing jurisdictions' administrative interpretations, decisions, policies, and positions, results of tax examinations, settlements or judicial decisions, changes in accounting principles, changes to the business operations, including acquisitions, as well as the evaluation of new information that results in a change to a tax position taken in a prior period.

Our debt service obligations and operating lease commitments may adversely affect our financial condition and cash flows from operations.

We have a substantial level of debt, including the 2023 and 2028 Senior Notes we issued in April 2018 ("Senior Notes") due April 2023 and April 2028, the loan we assumed when we purchased an office building located at 50 Fremont Street in San Francisco, California ("50 Fremont") due June 2023, the $500.0 million term loan to finance our acquisition of Demandware, due July 2019 (the "2019 term loan"), the $500.0 million term loan to finance our acquisition of MuleSoft, due May 2021 ("2021 term loan") and capital lease arrangements. Additionally, we have significant contractual commitments in operating lease arrangements, which are not reflected on our condensed consolidated balance sheets. In addition, we have a financing obligation for a leased facility of which we are deemed the owner for accounting purposes. In April 2018, we amended and restated our revolving credit facility under which we can draw down up to $1.0 billion. Maintenance of our indebtedness and contractual commitments and any additional issuances of indebtedness could:

- impair our ability to obtain additional financing in the future for working capital, capital expenditures, acquisitions, general corporate or other purposes;
- cause us to dedicate a substantial portion of our cash flows from operations towards debt service obligations and principal repayments; and
- make us more vulnerable to downturns in our business, our industry or the economy in general.

Our ability to meet our expenses and debt obligations will depend on our future performance, which will be affected by financial, business, economic, regulatory and other factors. We will not be able to control many of these factors, such as economic conditions and governmental regulations. Further, our operations may not generate sufficient cash to enable us to service our debt or contractual obligations resulting from our leases. If we fail to make a payment on our debt, we could be in default on such debt. If we are at any time unable to generate sufficient cash flows from operations to service our indebtedness when payment is due, we may be required to attempt to renegotiate the terms of the instruments relating to the indebtedness, seek to refinance all or a portion of the indebtedness or obtain additional financing. There can be no assurance that we would be able to successfully renegotiate such terms, that any such refinancing would be possible or that any additional financing could be obtained on terms that are favorable or acceptable to us.

Our senior unsecured notes and senior unsecured credit agreements impose restrictions on us and require us to maintain compliance with specified covenants. Our ability to comply with these covenants may be affected by events beyond our control. A failure to comply with the covenants and other provisions of our outstanding debt could result in events of default under such instruments, which could permit acceleration of all of our debt and borrowings. Any required repayment of our debt or revolving credit facility as a result of a fundamental change or other acceleration would lower our current cash on hand such that we would not have those funds available for use in our business. New lease accounting guidance will require that we record operating lease activity on our condensed consolidated balance sheet no later than fiscal 2020, which will result in an increase in both our assets and financing obligations. The implementation of this guidance may impact our ability to obtain the necessary financing from financial institutions at

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commercially viable rates or at all as this new guidance will result in a higher financing obligation on our condensed consolidated balance sheet.

Weakened global economic conditions may adversely affect our industry, business and results of operations.

Our overall performance depends in part on worldwide economic and geopolitical conditions. The United States and other key international economies have experienced cyclical downturns from time to time in which economic activity was impacted by falling demand for a variety of goods and services, restricted credit, poor liquidity, reduced corporate profitability, volatility in credit, equity and foreign exchange markets, bankruptcies and overall uncertainty with respect to the economy. These economic conditions can arise suddenly and the full impact of such conditions can remain uncertain. In addition, geopolitical developments, such as potential trade wars, can increase levels of political and economic unpredictability globally and increase the volatility of global financial markets. Moreover, these conditions can affect the rate of information technology spending and could adversely affect our customers' ability or willingness to purchase our enterprise cloud computing services, delay prospective customers' purchasing decisions, reduce the value or duration of their subscription contracts, or affect attrition rates, all of which could adversely affect our future sales and operating results.

Natural disasters and other events beyond our control could materially adversely affect us.

Natural disasters or other catastrophic events may cause damage or disruption to our operations, international commerce and the global economy, and thus could have a strong negative effect on us. Our business operations are subject to interruption by natural disasters, fire, power shortages, pandemics and other events beyond our control. Although we maintain crisis management and disaster response plans, such events could make it difficult or impossible for us to deliver our services to our customers, and could decrease demand for our services. Our corporate headquarters, and a significant portion of our research and development activities, information technology systems, and other critical business operations, are located near major seismic faults in the San Francisco Bay Area. Because we do not carry earthquake insurance for direct quake-related losses, with the exception of the building that we own in San Francisco, and significant recovery time could be required to resume operations, our financial condition and operating results could be materially adversely affected in the event of a major earthquake or catastrophic event.

Climate change may have a long-term impact on our business.

While we seek to partner with organizations that mitigate their business risks associated with climate change, we recognize that there are inherent climate related risks wherever business is conducted. Access to clean water and reliable energy in the communities where we conduct our business, whether for our offices, vendors, customers or other stakeholders, is a priority. Any of our primary locations may be vulnerable to the adverse effects of climate change. Climate related events have the potential to disrupt our business, including the business of our customers, and may cause us to experience higher attrition, losses and additional costs to resume operations.

Current and future accounting pronouncements and other financial reporting standards, especially but not only concerning revenue recognition, cost capitalization and lease accounting, may negatively impact our financial results.

We regularly monitor our compliance with applicable financial reporting standards and review new pronouncements and drafts thereof that are relevant to us. As a result of new standards, changes to existing standards and changes in their interpretation, we have been required to change our accounting policies, particularly concerning revenue recognition and the capitalized incremental costs to obtain a customer contract, to alter our operational policies, to implement new or enhance existing systems so that they reflect new or amended financial reporting standards, and to adjust our published financial statements. We will have similar requirements related to future accounting pronouncements, such as lease accounting. Such changes may have an adverse effect on our business, financial position, and operating results, or cause an adverse deviation from our revenue and operating profit target, which may negatively impact our financial results.

We may be subject to risks related to government contracts and related procurement regulations.

Our contracts with federal, state, local, and foreign government entities are subject to various procurement regulations and other requirements relating to their formation, administration and performance. We may be subject to audits and investigations relating to our government contracts, and any violations could result in various civil and criminal penalties and administrative sanctions, including termination of contract, refunding or suspending of payments, forfeiture of profits, payment of fines, and suspension or debarment from future government business. In addition,

such contracts may provide for termination by the government at any time, without cause. Any of these risks related to contracting with governmental entities could adversely impact our future sales and operating results.

We are subject to governmental export and import controls that could impair our ability to compete in international markets and subject us to liability if we are not in full compliance with applicable laws.

Our solutions are subject to export and import controls, including the Commerce Department's Export Administration Regulations, U.S. Customs regulations and various economic and trade sanctions regulations established by the Treasury Department's Office of Foreign Assets Control. If we fail to comply with these U.S. export control laws and import laws we

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and certain of our employees could be subject to substantial civil or criminal penalties, including the possible loss of export or import privileges; fines, which may be imposed on us and responsible employees or managers; and, in extreme cases, the incarceration of responsible employees or managers. Obtaining the necessary authorizations, including any required license, may be time-consuming, is not guaranteed and may result in the delay or loss of sales opportunities. Furthermore, the U.S. export control laws and economic sanctions laws prohibit the shipment of certain products and services to U.S. embargoed or sanctioned countries, governments and persons. Even though we take precautions to prevent our solutions from being provisioned or provided to U.S. sanctions targets, our solutions could be provisioned to those targets or provided by our resellers despite such precautions. Any such sales could have negative consequences, including government investigations, penalties and reputational harm. Changes in our solutions or changes in export and import regulations may create delays in the introduction, sale and deployment of our solutions in international markets or prevent the export or import of our solutions to certain countries, governments or persons altogether. Any decreased use of our solutions or limitation on our ability to export or sell our solutions would likely adversely affect our business, financial condition and results of operations.

The market price of our common stock is likely to be volatile and could subject us to litigation.

The trading prices of the securities of technology companies have historically been highly volatile. Accordingly, the market price of our common stock has been and is likely to continue to be subject to wide fluctuations. Factors affecting the market price of our common stock include:

- variations in our operating results, earnings per share, cash flows from operating activities, unearned revenue, remaining performance obligation, year-over-year growth rates for individual core service offerings and other financial metrics and non-financial metrics, such as transaction usage volumes and other usage metrics, and how those results compare to analyst expectations;
- variations in, and limitations of, the various financial and other metrics and modeling used by analysts in their research and reports about our business;
- forward-looking guidance to industry and financial analysts related to, for example, future revenue, unearned revenue, remaining performance obligation, cash flows from operating activities and earnings per share;
- changes in the estimates of our operating results or changes in recommendations by securities analysts that elect to follow our common stock;
- announcements of technological innovations, new services or service enhancements, strategic alliances or significant agreements by us or by our competitors;
- announcements by us or by our competitors of mergers or other strategic acquisitions, or rumors of such transactions involving us or our competitors;
- announcements of customer additions and customer cancellations or delays in customer purchases;
- the coverage of our common stock by the financial media, including television, radio and press reports and blogs;
- recruitment or departure of key personnel;
- disruptions in our service due to computer hardware, software, network or data center problems;
- the economy as a whole, market conditions in our industry and the industries of our customers;
- trading activity by a limited number of stockholders who together beneficially own a significant portion of our outstanding common stock;
- the issuance of shares of common stock by us, whether in connection with an acquisition or a capital raising transaction; and
- issuance of debt or other convertible securities.

In addition, if the market for technology stocks or the stock market in general experiences uneven investor confidence, the market price of our common stock could decline for reasons unrelated to our business, operating results or financial condition. The market price of our common stock might also decline in reaction to events that affect other companies within, or outside, our industry even if these events do not directly affect us. Some companies that have experienced volatility in the trading price of their stock have been the subject of securities class action litigation. If we are the subject of such litigation, it could result in substantial costs and a diversion of management’s attention and resources.

Provisions in our amended and restated certificate of incorporation and bylaws and Delaware law might discourage, delay or prevent a change of control of our company or changes in our management and, therefore, depress the market price of our common stock.

Our amended and restated certificate of incorporation and bylaws contain provisions that could depress the market price of our common stock by acting to discourage, delay or prevent a change in control of our company or changes in our management that the stockholders of our company may deem advantageous. These provisions among other things:

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- permit the board of directors to establish the number of directors;
- provide that directors may only be removed with the approval of holders of 66 2/3 percent of our outstanding capital stock;
- require super-majority voting to amend some provisions in our amended and restated certificate of incorporation and bylaws;
- authorize the issuance of "blank check" preferred stock that our board could use to implement a stockholder rights plan (also known as a "poison pill");
- prohibit stockholder action by written consent, which requires all stockholder actions to be taken at a meeting of our stockholders;
- provide that the board of directors is expressly authorized to make, alter or repeal our bylaws; and
- establish advance notice requirements for nominations for election to our board or for proposing matters that can be acted upon by stockholders at annual stockholder meetings.

In addition, Section 203 of the Delaware General Corporation Law may discourage, delay or prevent a change in control of our company. Section 203 imposes certain restrictions on merger, business combinations and other transactions between us and holders of 15 percent or more of our common stock.

ITEM 2. UNREGISTERED SALES OF EQUITY SECURITIES AND USE OF PROCEEDS

In connection with the acquisition of MetaMind, Inc. in April 2016, the Company issued 13,449 shares of Company common stock on July 2, 2018. This issuance was made in reliance on one or more of the following exemptions or exclusions from the registration requirements of the Securities Act of 1933, as amended (the "Securities Act"): Section 4(a)(2) of the Securities Act, Regulation D promulgated under the Securities Act, and Regulation S promulgated under the Securities Act.

ITEM 3. DEFAULTS UPON SENIOR SECURITIES

Not applicable.

ITEM 4. MINE SAFETY DISCLOSURES

Not applicable.

ITEM 5. OTHER INFORMATION

Not applicable.

ITEM 6. EXHIBITS

The documents listed in the Index to Exhibits of this quarterly report on Form 10-Q are incorporated by reference or are filed with this quarterly report on Form 10-Q, in each case as indicated therein (numbered in accordance with Item 601 of Regulation S-K).

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Index to Exhibits

Exhibit No.	Exhibit Description	Provided Herewith	Incorporated by Reference			
			Form	SEC File No.	Exhibit	Filing Date
3.1	Amended and Restated Certificate of Incorporation of salesforce.com, inc.		8-K	001-32224	3.1	6/13/2018
3.2	Amended and Restated Bylaws of salesforce.com, inc.		8-K	001-32224	3.1	8/8/2018
10.1	Amended and Restated 2013 Equity Incentive Plan		8-K	001-32224	10.1	6/13/2018
10.2	Settlement Agreement between salesforce.com, inc. and BNP Paribas, dated June 12, 2018		8-K	001-32224	10.1	6/15/2018
10.3	Settlement Agreement between salesforce.com, inc. and Bank of America, N.A., dated June 12, 2018		8-K	001-32224	10.2	6/15/2018
10.4	Settlement Agreement between salesforce.com, inc. and Morgan Stanley & Co. International plc, dated June 12, 2018		8-K	001-32224	10.3	6/15/2018
31.1	Certification of Co-Chief Executive Officer, Marc Benioff, pursuant to Exchange Act Rule 13a-14(a) or 15(d)-14(a), as adopted pursuant to Section 302 of the Sarbanes-Oxley Act of 2002	X				
31.2	Certification of Co-Chief Executive Officer, Keith Block, pursuant to Exchange Act Rule 13a-14(a) or 15(d)-14(a), as adopted pursuant to Section 302 of the Sarbanes-Oxley Act of 2002	X				
31.3	Certification of Chief Financial Officer pursuant to Exchange Act Rule 13a-14(a) or 15(d)-14(a), as adopted pursuant to Section 302 of the Sarbanes-Oxley Act of 2002	X				
32.1	Certification of Co-Chief Executive Officers and Chief Financial Officer pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002	X				
101.INS	XBRL Instance Document					
101.SCH	XBRL Taxonomy Extension Schema Document					
101.CAL	XBRL Taxonomy Extension Calculation Linkbase Document					
101.DEF	XBRL Extension Definition					
101.LAB	XBRL Taxonomy Extension Label Linkbase Document					
101.PRE	XBRL Taxonomy Extension Presentation Linkbase Document					

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SIGNATURES

Pursuant to the requirements of Section 13 or 15(d) of the Securities Exchange Act of 1934, the registrant has duly caused this report to be signed on its behalf by the undersigned thereunto duly authorized.

Dated: August 31, 2018

salesforce.com, inc.

By: /S/ MARK J. HAWKINS
Mark J. Hawkins
President and
Chief Financial Officer
(Principal Financial Officer)

Dated: August 31, 2018

salesforce.com, inc.

By: /S/ JOE ALLANSON
Joe Allanson
Executive Vice President,
Chief Accounting Officer
and Corporate Controller
(Principal Accounting Officer)