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

Form 10-Q

(Mark One)

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

For the quarterly period ended December 27, 2008

or

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

For the transition period from ______ to ______.

Commission file number: 000-10030

Apple Inc.
(Exact name of Registrant as specified in its charter)

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

Registrant's telephone number, including area code: (408) 996-1010

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

Yes ☒ No ☐

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

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

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

Yes ☐ No ☒

890,553,729 shares of common stock issued and outstanding as of January 12, 2009

PART I. FINANCIAL INFORMATION

Item 1. Financial Statements

APPLE INC.

CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS (Unaudited)
(in millions, except share amounts which are reflected in thousands and per share amounts)

	Three Months Ended	
	December 27, 2008	December 29, 2007
Net sales	$ 10,167	$ 9,608
Cost of sales	6,635	6,276
Gross margin	3,532	3,332
Operating expenses:		
Research and development	315	246
Selling, general, and administrative	1,091	960
Total operating expenses	1,406	1,206
Operating income	2,126	2,126
Other income and expense	158	200
Income before provision for income taxes	2,284	2,326
Provision for income taxes	679	745
Net income	$ 1,605	$ 1,581
Earnings per common share:		
Basic	$ 1.81	$ 1.81
Diluted	$ 1.78	$ 1.76
Shares used in computing earnings per share:		
Basic	889,142	875,860
Diluted	901,494	900,054

See accompanying Notes to Condensed Consolidated Financial Statements.

APPLE INC.

CONDENSED CONSOLIDATED BALANCE SHEETS (Unaudited)
(in millions, except share amounts)

	December 27, 2008	September 27, 2008
ASSETS:		
Current assets:		
Cash and cash equivalents	$ 7,236	$ 11,875
Short-term marketable securities	18,411	10,236
Accounts receivable, less allowances of $54 and $47, respectively	2,196	2,422
Inventories	396	509
Deferred tax assets	1,613	1,447
Other current assets	5,311	5,822
Total current assets	35,163	32,311
Long-term marketable securities	2,498	2,379
Property, plant and equipment, net	2,580	2,455
Goodwill	207	207
Acquired intangible assets, net	277	285
Other assets	2,062	1,935
Total assets	$ 42,787	$ 39,572
LIABILITIES AND SHAREHOLDERS' EQUITY:		
Current liabilities:		
Accounts payable	$ 4,715	$ 5,520
Accrued expenses	3,807	3,719
Deferred revenue	6,235	4,853
Total current liabilities	14,757	14,092
Deferred revenue – non-current	3,440	3,029
Other non-current liabilities	1,681	1,421
Total liabilities	19,878	18,542
Commitments and contingencies		
Shareholders' equity:		
Common stock, no par value; 1,800,000,000 shares authorized; 890,414,924 and 888,325,973 shares issued and outstanding, respectively	7,392	7,177
Retained earnings	15,448	13,845
Accumulated other comprehensive income	69	8
Total shareholders' equity	22,909	21,030
Total liabilities and shareholders' equity	$ 42,787	$ 39,572

See accompanying Notes to Condensed Consolidated Financial Statements.

APPLE INC.

CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS (Unaudited)
(in millions)

	Three Months Ended	
	December 27, 2008	December 29, 2007
Cash and cash equivalents, beginning of the period	$ 11,875	$ 9,352
Operating Activities:		
Net income	1,605	1,581
Adjustments to reconcile net income to cash generated by operating activities:		
Depreciation, amortization, and accretion	158	106
Stock-based compensation expense	170	110
Provision for deferred income taxes	(27)	22
Loss on disposition of property, plant, and equipment	7	14
Changes in operating assets and liabilities:		
Accounts receivable, net	226	(302)
Inventories	113	(113)
Other current assets	660	(550)
Other assets	(116)	(253)
Accounts payable	(767)	484
Deferred revenue	1,793	1,048
Other liabilities	116	640
Cash generated by operating activities	3,938	2,787
Investing Activities:		
Purchases of marketable securities	(13,082)	(6,127)
Proceeds from maturities of marketable securities	2,226	2,129
Proceeds from sales of marketable securities	2,668	758
Purchases of other long-term investments	(38)	(9)
Payment for acquisition of property, plant, and equipment	(339)	(224)
Payment for acquisition of intangible assets	(14)	(8)
Other	(60)	19
Cash used in investing activities	(8,639)	(3,462)
Financing Activities:		
Proceeds from issuance of common stock	77	179
Excess tax benefits from stock-based compensation	19	315
Cash used to net share settle equity awards	(34)	(9)
Cash generated by financing activities	62	485
Decrease in cash and cash equivalents	(4,639)	(190)
Cash and cash equivalents, end of the period	$ 7,236	$ 9,162
Supplemental cash flow disclosure:		
Cash paid for income taxes, net	$ 550	$ 251

See accompanying Notes to Condensed Consolidated Financial Statements.

Note 1 – Summary of Significant Accounting Policies

Apple Inc. and its wholly-owned subsidiaries (collectively "Apple" or the "Company") design, manufacture, and market personal computers, portable digital music players, and mobile communication devices and sell a variety of related software, digital content, services, peripherals, and networking solutions. The Company sells its products worldwide through its online stores, its retail stores, its direct sales force, and third-party wholesalers, resellers, and value-added resellers. In addition, the Company sells a variety of third-party Mac, iPod and iPhone compatible products including application software, printers, storage devices, speakers, headphones, and various other accessories and supplies through its online and retail stores. The Company sells to consumer, small and mid-sized business ("SMB"), education, enterprise, government, and creative customers.

Basis of Presentation and Preparation

The accompanying Condensed Consolidated Financial Statements include the accounts of the Company. Intercompany accounts and transactions have been eliminated. The preparation of these Condensed Consolidated Financial Statements in conformity with U.S. generally accepted accounting principles requires management to make estimates and assumptions that affect the amounts reported in these Condensed Consolidated Financial Statements and accompanying notes. Actual results could differ materially from those estimates.

Certain prior year amounts in the Condensed Consolidated Financial Statements and notes thereto have been reclassified to conform to the current period's presentation. In the current period, the Company reclassified $2.4 billion of certain fixed-income securities from short-term marketable securities to long-term marketable securities. The reclassification resulted from a change in accounting presentation for certain investments based on contractual maturity dates, which more closely reflects the Company's assessment of the timing of when such securities will be converted to cash. As a result of this change, marketable securities with maturities less than 12 months are classified as short-term and marketable securities with maturities greater than 12 months are classified as long-term. There have been no changes in the Company's investment policies or practices associated with this change in accounting presentation. See Note 2, "Financial Instruments" of this Form 10-Q for additional information.

These Condensed Consolidated Financial Statements and accompanying notes should be read in conjunction with the Company's annual Consolidated Financial Statements and the notes thereto for the fiscal year ended September 27, 2008, included in its Annual Report on Form 10-K (the "2008 Form 10-K"). Unless otherwise stated, references to particular years or quarters refer to the Company's fiscal years ended in September and the associated quarters of those fiscal years.

Earnings Per Common Share

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

The following table sets forth the computation of basic and diluted earnings per share for the three months ended December 27, 2008 and December 29, 2007 (in thousands, except net income in millions and per share amounts):

	Three Months Ended	
	December 27, 2008	December 29, 2007
Numerator:		
Net income	$ 1,605	$ 1,581
Denominator:		
Weighted-average shares outstanding	889,142	875,860
Effect of dilutive securities	12,352	24,194
Denominator for diluted earnings per share	901,494	900,054
Basic earnings per share	$ 1.81	$ 1.81
Diluted earnings per share	$ 1.78	$ 1.76

Potentially dilutive securities representing approximately 18.8 million and 7.6 million shares of common stock for the quarters ended December 27, 2008 and December 29, 2007, respectively, were excluded from the computation of diluted earnings per share for these periods because their effect would have been antidilutive.

Fair Value Measurements

During the first quarter of fiscal 2009, the Company adopted Financial Accounting Standards Board ("FASB") Statement of Financial Accounting Standard ("SFAS") No. 157, "*Fair Value Measurements*", which defines fair value, establishes guidelines for measuring fair value and expands disclosures regarding fair value measurements. SFAS No. 157 does not require any new fair value measurements, but rather eliminates inconsistencies in guidance found in various other accounting pronouncements. The adoption of SFAS No. 157 did not have a material effect on the Company's financial condition or operating results.

SFAS No. 157 establishes a hierarchy for information and valuations used in measuring fair value, which is broken down into three levels. Level 1 valuations are based on quoted prices in active markets for identical assets or liabilities. Level 2 valuations are based on inputs, other than quoted prices included within Level 1, that are observable, either directly or indirectly. Level 3 valuations are based on information that is unobservable and significant to the overall fair value measurement.

The Company also adopted SFAS No. 159, *The Fair Value Option for Financial Assets and Financial Liabilities—including an amendment of FASB Statement No. 115,* during the first quarter of fiscal 2009. SFAS No. 159 allows companies to choose to measure eligible financial instruments and certain other items at fair value that are not required to be measured at fair value. SFAS No. 159 requires that unrealized gains and losses on items for which the fair value option has been elected be reported in earnings at each reporting date. The Company adopted SFAS No. 159 but has not elected the fair value option for any eligible financial instruments as of December 27, 2008.

Refer to Note 3, "Fair Value Measurements" of this Form 10-Q for additional information on the adoption of SFAS Nos. 157 and 159.

Note 2 – Financial Instruments

Cash, Cash Equivalents and Marketable Securities

The following table summarizes the fair value of the Company's cash and available-for-sale securities held in its marketable securities investment portfolio, recorded as cash, cash equivalents, short-term or long-term marketable securities as of December 27, 2008 and September 27, 2008 (in millions):

	December 27, 2008	September 27, 2008
Cash	$ 416	$ 368
Money market funds	2,270	1,536
U.S. Treasury securities	198	118
U.S. agency securities	1,557	2,798
Certificates of deposit and time deposits	1,644	2,560
Commercial paper	1,151	4,429
Corporate securities	—	66
Total cash equivalents	6,820	11,507
U.S. Treasury securities	918	343
U.S. agency securities	13,761	5,823
Non-U.S. government securities	107	83
Certificates of deposit and time deposits	389	486
Commercial paper	1,185	1,254
Corporate securities	2,051	2,247
Total short-term marketable securities	18,411	10,236
U.S. Treasury securities	114	100
U.S. agency securities	1,098	751
Certificates of deposit and time deposits	—	32
Corporate securities	1,286	1,496
Total long-term marketable securities	2,498	2,379
Total cash, cash equivalents and marketable securities	$ 28,145	$ 24,490

As of December 27, 2008, the Company changed its accounting presentation for certain fixed-income investments, which resulted in the reclassification of certain investments from short-term marketable securities to long-term marketable securities. As a result, prior period balances have been reclassified to conform to the current period's presentation. The Company classifies its marketable securities as either short-term or long-term based on each instrument's underlying contractual maturity date, while its prior classifications were based on the nature of the securities and their availability for use in current operations. As a result of this change, marketable securities with maturities of less than 12 months are classified as short-term and marketable securities with maturities greater than 12 months are classified as long-term. The Company's long-term marketable securities' maturities range from one year to five years. The Company believes this new presentation is preferable as it more closely reflects the Company's assessment of the timing of when such securities will be converted to cash. Accordingly, certain fixed-income investments totaling $2.4 billion have been reclassified from short-term marketable securities to long-term marketable securities in the September 27, 2008 Condensed Consolidated Balance Sheet to conform to the current period's financial statement presentation. There have been no changes in the Company's investment policies or practices associated with this change in accounting presentation.

The Company had net unrealized losses on its investment portfolio of $39 million and $117 million as of December 27, 2008 and September 27, 2008, respectively. In both periods, the net unrealized losses related primarily to long-term marketable securities. The Company may sell its marketable securities prior to their stated maturities for strategic purposes, in anticipation of credit deterioration, or for duration management. The Company recognized no material net gains or losses during the first quarters of 2009 or 2008 related to such sales.

The following table shows the gross unrealized losses and fair value for investments in an unrealized loss position as of December 27, 2008 and September 27, 2008, aggregated by investment category and the length of time that individual securities have been in a continuous loss position (in millions):

	December 27, 2008					
	Less than 12 Months		12 Months or Greater		Total	
Security Description	Fair Value	Unrealized Loss	Fair Value	Unrealized Loss	Fair Value	Unrealized Loss
U.S. Treasury securities	$ 125	$ —	$ —	$ —	$ 125	$ —
U.S. agency securities	2,669	(2)	—	—	2,669	(2)
Non-U.S. government securities	95	—	—	—	95	—
Commercial paper	56	—	—	—	56	—
Corporate securities	1,720	(38)	1,125	(82)	2,845	(120)
Total	$4,665	$ (40)	$1,125	$ (82)	$5,790	$ (122)

	September 27, 2008					
	Less than 12 Months		12 Months or Greater		Total	
Security Description	Fair Value	Unrealized Loss	Fair Value	Unrealized Loss	Fair Value	Unrealized Loss
U.S. Treasury securities	$ 28	$ —	$ —	$ —	$ 28	$ —
U.S. agency securities	6,822	(13)	—	—	6,822	(13)
Non-U.S. government securities	38	—	—	—	38	—
Certificates of deposit and time deposits	26	—	—	—	26	—
Commercial paper	646	—	—	—	646	—
Corporate securities	2,147	(31)	1,148	(77)	3,295	(108)
Total	$9,707	$ (44)	$1,148	$ (77)	$10,855	$ (121)

The Company considers the declines in market value of its marketable securities investment portfolio to be temporary in nature. The unrealized losses on the Company's marketable securities were caused primarily by changes in market interest rates, specifically, widening credit spreads. The Company typically invests in highly-rated securities, and its policy generally limits the amount of credit exposure to any one issuer. The Company's investment policy requires investments to be rated single-A or better, with the objective of minimizing the potential risk of principal loss. Fair values were determined for each individual security in the investment portfolio. When evaluating the investments for other-than-temporary impairment, the Company reviews factors such as the length of time and extent to which fair value has been below cost basis, the financial condition of the issuer, and the Company's ability and intent to hold the investment for a period of time, which may be sufficient for anticipated recovery in market value. During the first quarters of 2009 or 2008, the Company did not recognize any material impairment charges on outstanding securities. As of December 27, 2008, the Company does not consider any of its investments to be other-than-temporarily impaired.

Derivative Financial Instruments

The Company uses derivatives to offset partially its business exposure to foreign exchange risk. The Company uses foreign currency forward and option contracts to offset the foreign exchange risk on certain existing assets and liabilities and to hedge the foreign exchange risk on expected future cash flows on certain forecasted revenue and cost of sales. Generally, the Company's practice is to hedge a majority of its existing material foreign exchange transaction exposures. However, the Company may not hedge certain foreign exchange transaction exposures due to immateriality, prohibitive economic cost of hedging particular exposures, or limited availability of appropriate hedging instruments.

The Company's accounting policies for these instruments are based on whether the instruments are designated as hedge or non-hedge instruments. The Company records all derivatives on the balance sheet at fair value. Derivatives that are not designated as hedges and the ineffective portions of cash flow hedges and net investment hedges are adjusted to fair value through earnings. The effective portions of cash flow hedges are recorded in other comprehensive income until the hedged item is recognized in earnings. The effective portions of net investment hedges are recorded in deferred translation as a component of other comprehensive income. Changes in value of fair value hedges are offset against the changes in fair value of the hedged assets, liabilities, or firm commitments through earnings.

As of December 27, 2008, the Company had a net deferred gain associated with cash flow hedges of approximately $105 million, net of taxes. The portion of the Company's net deferred gain related to products under subscription accounting is expected to be recorded in earnings ratably over a 24-month period beginning when the hedged transaction occurs, while the portion of the net deferred gain related to other products is expected to be recorded in earnings at the time the hedged transaction occurs. As of December 27, 2008, the hedged transactions are expected to occur within six months. As of the end of the first quarter of 2009, the general nature of the Company's risk management activities and the general nature and mix of the Company's derivative financial instruments have not changed materially from the end of 2008.

Note 3 – Fair Value Measurements

In the first quarter of 2009, the Company adopted SFAS No. 157 for all financial assets and liabilities and non-financial assets and liabilities that are recognized or disclosed at fair value in the financial statements on a recurring basis. SFAS No. 157 defines fair value as the price that would be received from selling an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. When determining the fair value measurements for assets and liabilities, which are required to be recorded at fair value, the Company considers the principal or most advantageous market in which the Company would transact and the market-based risk measurements or assumptions that market participants would use in pricing the asset or liability, such as inherent risk, transfer restrictions, and credit risk.

SFAS No. 157 also establishes a fair value hierarchy, which prioritizes the inputs to valuation techniques used to measure fair value into three levels. A financial instrument's categorization within the fair value hierarchy is based upon the lowest level of input that is available and significant to the fair value measurement. SFAS No. 157 establishes and prioritizes three levels of inputs that may be used to measure fair value:

Level 1 - Quoted prices in active markets for identical assets or liabilities.

Level 2 - Observable inputs other than quoted prices in active markets for identical assets and liabilities, quoted prices for identical or similar assets or liabilities in inactive markets, or other inputs that are observable or can be corroborated by observable market data for substantially the full term of the assets or liabilities.

Level 3 - Inputs that are generally unobservable and typically reflect management's estimates of assumptions that market participants would use in pricing the asset or liability.

Assets/Liabilities Measured at Fair Value on a Recurring Basis

The following table presents the Company's assets and liabilities measured at fair value on a recurring basis as of December 27, 2008 (in millions):

	December 27, 2008			
	Quoted Prices in Active Markets for Identical Instruments (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)	Total
Assets:				
Money market funds	$ 2,270	$ —	$ —	$ 2,270
U.S. Treasury securities	—	1,230	—	1,230
U.S. agency securities	—	16,416	—	16,416
Non-U.S. government securities	—	107	—	107
Certificates of deposit and time deposits	—	2,033	—	2,033
Commercial paper	—	2,336	—	2,336
Corporate securities	—	3,337	—	3,337
Marketable equity securities	9	—	—	9
Derivative assets	—	172	—	172
Total assets measured at fair value	$ 2,279	$ 25,631	$ —	$27,910
Liabilities:				
Derivative liabilities	$ —	$ 74	$ —	$ 74
Total liabilities measured at fair value	$ —	$ 74	$ —	$ 74

The following table summarizes the Company's assets and liabilities measured at fair value on a recurring basis presented on the Company's Condensed Consolidated Balance Sheet as of December 27, 2008 (in millions):

	December 27, 2008			
	Quoted Prices in Active Markets for Identical Instruments (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)	Total
Assets:				
Cash equivalents	$ 2,270	$ 4,550	$ —	$ 6,820
Short-term marketable securities	—	18,411	—	18,411
Long-term marketable securities	—	2,498	—	2,498
Other current assets	—	172	—	172
Other assets	9	—	—	9
Total assets measured at fair value	$ 2,279	$ 25,631	$ —	$27,910
Liabilities:				
Other current liabilities	$ —	$ 74	$ —	$ 74
Total liabilities measured at fair value	$ —	$ 74	$ —	$ 74

Note 4 – Condensed Consolidated Financial Statement Details

The following tables show the Company's Condensed Consolidated Financial Statement details as of December 27, 2008 and September 27, 2008 (in millions):

Other Current Assets

	December 27, 2008	September 27, 2008
Deferred costs under subscription accounting - current	$ 2,413	$ 1,931
Vendor non-trade receivables	1,217	2,282
Inventory component prepayments	345	475
Other current assets	1,336	1,134
Total other current assets	$ 5,311	$ 5,822

Property, Plant, and Equipment

	December 27, 2008	September 27, 2008
Land and buildings	$ 888	$ 810
Machinery, equipment, and internal-use software	1,624	1,491
Office furniture and equipment	126	122
Leasehold improvements	1,359	1,324
	3,997	3,747
Accumulated depreciation and amortization	(1,417)	(1,292)
Net property, plant, and equipment	$ 2,580	$ 2,455

Other Assets

	December 27, 2008	September 27, 2008
Deferred costs under subscription accounting - non-current	$ 1,212	$ 1,089
Deferred tax assets - non-current	125	138
Long-term inventory component prepayments	83	208
Capitalized software development costs, net	82	67
Other assets	560	433
Total other assets	$ 2,062	$ 1,935

Accrued Expenses

	December 27, 2008	September 27, 2008
Deferred margin on component sales	$ 471	$ 681
Accrued marketing and distribution	302	329
Accrued warranty and related costs	265	267
Accrued compensation and employee benefits	252	320
Other accrued tax liabilities	100	100
Other current liabilities	2,417	2,022
Total accrued expenses	$ 3,807	$ 3,719

Other Non-Current Liabilities

	December 27, 2008	September 27, 2008
Deferred tax liabilities	$ 865	$ 675
Other non-current liabilities	816	746
Total other non-current liabilities	$ 1,681	$ 1,421

Note 5 – Income Taxes

As of December 27, 2008, the Company recorded gross unrecognized tax benefits of $560 million, of which $247 million, if recognized, would affect the Company's effective tax rate. As of September 27, 2008, the total amount of gross unrecognized tax benefits was $506 million, of which $253 million, if recognized, would affect the Company's effective tax rate. The Company's total gross unrecognized tax benefits are classified as other non-current liabilities in the Condensed Consolidated Balance Sheets. The Company had $247 million and $219 million of gross interest and penalties accrued as of December 27, 2008 and September 27, 2008, respectively, which are classified as other non-current liabilities in the Condensed Consolidated Balance Sheets.

Management believes that an adequate provision has been made for any adjustments that may result from tax examinations. However, the outcome of tax audits cannot be predicted with certainty. If any issues addressed in the Company's tax audits are resolved in a manner not consistent with management's expectations, the Company could be required to adjust its provision for income tax in the period such resolution occurs. Although timing of the resolution and/or closure of audits is highly uncertain, the Company does not believe it is reasonably possible that its unrecognized tax benefits would materially change in the next 12 months.

Note 6 – Shareholders' Equity

Preferred Stock

The Company has five million shares of authorized preferred stock, none of which is issued or outstanding. Under the terms of the Company's Restated Articles of Incorporation, the Board of Directors is authorized to determine or alter the rights, preferences, privileges and restrictions of the Company's authorized but unissued shares of preferred stock.

Comprehensive Income

Comprehensive income consists of two components, net income and other comprehensive income. Other comprehensive income refers to revenue, expenses, gains, and losses that under U.S. generally accepted accounting principles are recorded as an element of shareholders' equity but are excluded from net income. The Company's other comprehensive income consists of foreign currency translation adjustments from those subsidiaries not using the U.S. dollar as their functional currency, the effective portion of foreign currency net investment hedges, unrealized gains and losses on marketable securities categorized as available-for-sale, and net deferred gains and losses on certain derivative instruments accounted for as cash flow hedges.

The following table summarizes the components of total comprehensive income, net of taxes, during the three months ended December 27, 2008 and December 29, 2007 (in millions):

	Three Months Ended	
	December 27, 2008	December 29, 2007
Net income	$ 1,605	$ 1,581
Other comprehensive income:		
Change in unrecognized gains on derivative instruments	86	4
Change in foreign currency translation	(74)	7
Net change in unrealized losses on marketable securities	49	—
Total comprehensive income	$ 1,666	$ 1,592

The following table summarizes activity in other comprehensive income related to derivatives, net of taxes, held by the Company during the three months ended December 27, 2008 and December 29, 2007 (in millions):

	Three Months Ended	
	December 27, 2008	December 29, 2007
Change in fair value of derivatives	$ 107	$ 4
Adjustment for net gains realized and included in net income	(21)	—
Change in unrecognized gains on derivative instruments	$ 86	$ 4

The following table summarizes the components of accumulated other comprehensive income, net of taxes, as of December 27, 2008 and September 27, 2008 (in millions):

	December 27, 2008	September 27, 2008
Unrealized losses on available-for-sale securities	$ (21)	$ (70)
Cumulative foreign currency translation	(15)	59
Net unrecognized gains on derivative instruments	105	19
Accumulated other comprehensive income	$ 69	$ 8

Employee Benefit Plans

Rule 10b5-1 Trading Plans

The following executive officers, Timothy D. Cook, Peter Oppenheimer, Philip W. Schiller, and Bertrand Serlet, have entered into trading plans pursuant to Rule 10b5-1(c)(1) of the Securities Exchange Act of 1934, as amended (the "Exchange Act"), as of January 19, 2009. A trading plan is a written document that pre-establishes the amounts, prices and dates (or formula for determining the amounts, prices and dates) of future purchases or sales of the Company's stock including the exercise and sale of employee stock options and shares acquired pursuant to the Company's employee stock purchase plan and upon vesting of RSUs.

Stock Option Activity

A summary of the Company's stock option activity and related information for the three months ended December 27, 2008 is as follows (in thousands, except per share amounts and contractual term in years):

		Outstanding Options			
	Shares Available for Grant	Number of Shares	Weighted-Average Exercise Price	Weighted-Average Remaining Contractual Term	Aggregate Intrinsic Value
Balance at September 27, 2008	50,572	44,146	$ 74.39		
Restricted stock units granted	(11,668)	—	$ —		
Options granted	(181)	181	$ 96.42		
Options cancelled	417	(417)	$111.85		
Restricted stock units cancelled	490	—	$ —		
Options exercised	—	(819)	$ 30.61		
Plan shares expired	(1)	—	$ —		
Balance at December 27, 2008	39,629	43,091	$ 74.96	4.08	$ 1,334,486
Exercisable at December 27, 2008		26,279	$ 46.10	3.31	$ 1,237,298
Expected to vest after December 27, 2008		16,263	$ 80.03	5.28	$ 94,017

Aggregate intrinsic value represents the value of the Company's closing stock price on the last trading day of the fiscal period in excess of the weighted-average exercise price multiplied by the number of options outstanding or exercisable. The aggregate intrinsic value excludes the effect of stock options that have a zero or negative intrinsic value. The total intrinsic value of options at the time of exercise was $55 million and $887 million for the three months ended December 27, 2008 and December 29, 2007, respectively.

Shares of RSUs granted after April 2005 have been deducted from the shares available for grant under the Company's stock option plans utilizing a factor of two times the number of RSUs granted. Similarly, shares of RSUs cancelled have been added back to the shares available for grant under the Company's stock option plans utilizing a factor of two times the number of RSUs cancelled.

Restricted Stock Units

The Company's Board of Directors has granted RSUs to members of the Company's executive management team, excluding its Chief Executive Officer ("CEO"), as well as various employees within the Company. RSUs generally vest over four years either at the end of the four-year service period, in two equal installments on the second and fourth anniversaries of the date of grant, in equal installments on each of the first through fourth anniversaries of the grant date, or in equal installments on each semi-annual anniversary of the grant date. Upon vesting, the RSUs are generally net share settled to cover the required withholding tax and the remaining amount is converted into an equivalent number of shares of common stock.

Outstanding RSU balances were not included in the outstanding options balances in the preceding table. A summary of the Company's RSU activity and related information for the three months ended December 27, 2008 is as follows (in thousands, except per share amounts):

	Number of Shares	Weighted-Average Grant Date Fair Value	Aggregate Intrinsic Value
Balance at September 27, 2008	7,040	$ 134.91	
Restricted stock units granted	5,834	$ 96.76	
Restricted stock units vested	(874)	$ 150.44	
Restricted stock units cancelled	(245)	$ 120.44	
Balance at December 27, 2008	11,755	$ 115.12	$ 1,008,670

RSUs that vested during the three months ended December 27, 2008 and December 29, 2007 had a fair value of $86 million and $43 million, respectively, as of the vesting date.

Note 7 – Stock-Based Compensation

SFAS No. 123 (revised 2004), *Share-Based Payment*, requires the use of a valuation model to calculate the fair value of stock-based awards. The Company uses the Black-Scholes-Merton ("BSM") option-pricing model to calculate the fair value of stock-based awards. The BSM option-pricing model incorporates various assumptions including expected volatility, expected life, and interest rates. The expected volatility is based on the historical volatility of the Company's common stock over the most recent period commensurate with the estimated expected life of the Company's stock options and other relevant factors including implied volatility in market traded options on the Company's common stock. The Company bases its expected life assumption on its historical experience and on the terms and conditions of the stock awards it grants to employees. Stock-based compensation cost is estimated at the grant date based on the award's fair-value as calculated by the BSM option-pricing model and is recognized as expense ratably on a straight-line basis over the requisite service period.

The compensation expense incurred by the Company for RSUs is based on the closing market price of the Company's common stock on the date of grant and is amortized ratably on a straight-line basis over the requisite service period.

The weighted average assumptions used for the three months ended December 27, 2008 and December 29, 2007 and the resulting estimates of weighted-average fair value per share of options granted and of employee stock purchase plan rights ("stock purchase rights") during those periods are as follows:

	Three Months Ended	
	December 27, 2008	December 29, 2007
Expected life - stock options	3.41 years	3.41 years
Expected life - stock purchase rights	6 months	6 months
Interest rate - stock options	1.76%	3.63%
Interest rate - stock purchase rights	2.16%	4.98%
Expected volatility - stock options	53.40%	45.80%
Expected volatility - stock purchase rights	47.03%	30.92%
Expected dividend yields	—	—
Weighted-average fair value of options granted during the period	$ 38.25	$ 64.22
Weighted-average fair value of stock purchase rights during the period	$ 44.52	$ 28.36

The following table provides a summary of the stock-based compensation expense included in the Condensed Consolidated Statements of Operations for the three months ended December 27, 2008 and December 29, 2007 (in millions):

	Three Months Ended	
	December 27, 2008	December 29, 2007
Cost of sales	$ 28	$ 18
Research and development	60	39
Selling, general, and administrative	82	53
Total stock-based compensation expense	$ 170	$ 110

Stock-based compensation expense capitalized as part of software development costs was not significant as of December 27, 2008 or December 29, 2007. The income tax benefit related to stock-based compensation expense was $66 million and $34 million for the three months ended December 27, 2008 and December 29, 2007, respectively. As of December 27, 2008, the total unrecognized compensation cost related to outstanding stock options and RSUs expected to vest was $1.8 billion, which the Company expects to recognize over a weighted-average period of 3.02 years.

Note 8 – Commitments and Contingencies

Lease Commitments

The Company leases various equipment and facilities, including retail space, under noncancelable operating lease arrangements. The Company does not currently utilize any other off-balance sheet financing arrangements. The major facility leases are for terms of 3 to 20 years and generally provide renewal options for terms of 1 to 5 years. Leases for retail space are generally for terms of 5 to 20 years, the majority of which are for 10 years, and often contain multi-year renewal options. As of September 27, 2008, the Company's total future minimum lease payments under noncancelable operating leases were $1.8 billion, of which $1.4 billion related to leases for retail space. As of December 27, 2008, total future minimum lease payments under noncancelable operating leases related to leases for retail space decreased $44 million to $1.3 billion.

Accrued Warranty and Indemnifications

The following table reconciles changes in the Company's accrued warranties and related costs for the three months ended December 27, 2008 and December 29, 2007 (in millions):

	Three Months Ended	
	December 27, 2008	December 29, 2007
Beginning accrued warranty and related costs	$ 267	$ 230
Cost of warranty claims	(78)	(80)
Accruals for product warranties	76	87
Ending accrued warranty and related costs	$ 265	$ 237

The Company generally does not indemnify end-users of its operating system and application software against legal claims that the software infringes third-party intellectual property rights. Other agreements entered into by the Company sometimes include indemnification provisions under which the Company could be subject to costs and/or damages in the event of an infringement claim against the Company or an indemnified third-party. However, the Company has not been required to make any significant payments resulting from such an infringement claim asserted against it or an indemnified third-party and, in the opinion of management, does not have a potential liability related to unresolved infringement claims subject to indemnification that would have a material adverse effect on its financial condition or operating results. Therefore, the Company did not record a liability for infringement costs as of either December 27, 2008 or September 27, 2008.

Concentrations in the Available Sources of Supply of Materials and Product

Although most components essential to the Company's business are generally available from multiple sources, certain key components including, but not limited to microprocessors, enclosures, certain liquid crystal displays ("LCDs"), certain optical drives, and application-specific integrated circuits ("ASICs") are currently obtained by the Company from single or limited sources, which subjects the Company to significant supply and pricing risks. Many of these and other key components that are available from multiple sources including, but not limited to NAND flash memory, dynamic random access memory ("DRAM"), and certain LCDs, are subject at times to industry-wide shortages and significant commodity pricing fluctuations. In addition, the Company has entered into certain agreements for the supply of key components including, but not limited to microprocessors, NAND flash memory, DRAM and LCDs at favorable pricing, but there is no guarantee that the Company will be able to extend or renew these agreements on similar favorable terms, or at all, upon expiration or otherwise obtain favorable pricing in the future. Therefore, the Company remains subject to significant risks of supply shortages and/or price increases that can have a material adverse effect on its financial condition and operating results.

The Company and other participants in the personal computer, consumer electronics and mobile communication industries also compete for various components with other industries that have experienced increased demand for their products. In addition, the Company uses some custom components that are not common to the rest of the personal computer, consumer electronics and mobile communication industries, and new products introduced by the Company often utilize custom components available from only one source until the Company has evaluated whether there is a need for, and subsequently qualifies, additional suppliers. When a component or product uses new technologies, initial capacity constraints may exist until the suppliers' yields have matured. If the Company's supply of a key single-sourced component for a new or existing product were delayed or constrained, if such components were available only at significantly higher prices, or if a key manufacturing vendor delayed shipments of completed products to the Company, the Company's financial condition and operating results could be materially adversely affected. The Company's business and financial performance could also be adversely affected depending on the time required to obtain sufficient quantities from the original source, or to identify and obtain sufficient quantities from an alternative source. Continued availability of these components at acceptable prices, or at all, may be affected if those suppliers decided to concentrate on the production of common components instead of components customized to meet the Company's requirements.

Significant portions of the Company's Mac computers, iPods, iPhones, logic boards, and other assembled products are now manufactured by outsourcing partners, primarily in various parts of Asia. A significant concentration of this outsourced manufacturing is currently performed by only a few of the Company's outsourcing partners, often in single locations. Certain of these outsourcing partners are the sole-sourced supplier of components and manufacturing outsourcing for many of the Company's key products including but not limited to final assembly of substantially all of the Company's portable Mac computers, iPods, iPhones and most of the Company's iMacs. Although the Company works closely with its outsourcing partners on manufacturing schedules, the Company's operating results could be adversely affected if its outsourcing partners were unable to meet their production commitments. The Company's purchase commitments typically cover its requirements for periods ranging from 30 to 150 days.

Long-Term Supply Agreements

During 2006, the Company entered into long-term supply agreements with Hynix Semiconductor, Inc., Intel Corporation, Micron Technology, Inc., Samsung Electronics Co., Ltd., and Toshiba Corporation to secure supply of NAND flash memory through calendar year 2010. As part of these agreements, the Company prepaid $1.25 billion, which is being applied to certain inventory component purchases made over the life of each respective agreement. During the first quarter of fiscal 2009, the long-term supply agreement with Intel Corporation was terminated and the remaining prepaid balance of $167 million was repaid to the Company. As of December 27, 2008, the Company had $428 million of inventory component prepayments outstanding.

Subsequent to December 27, 2008, the Company entered into a long-term supply agreement with LG Display to purchase LCD panels for five years. As part of the agreement, the Company is required to make a prepayment of $500 million in the second quarter of 2009.

Contingencies

The Company is subject to certain other legal proceedings and claims that have arisen in the ordinary course of business and have not been fully adjudicated. In the opinion of management, the Company does not have a potential liability related to any current legal proceedings and claims that would individually or in the aggregate have a material adverse effect on its financial condition or operating results. However, the results of legal proceedings cannot be predicted with certainty. If the Company failed to prevail in any of these legal matters or if several of these legal matters were resolved against the Company in the same reporting period, the operating results of a particular reporting period could be materially adversely affected.

Production and marketing of products in certain states and countries may subject the Company to environmental, product safety and other regulations including, in some instances, the requirement to provide customers the ability to return product at the end of its useful life, and place responsibility for environmentally safe disposal or recycling with the Company. Such laws and regulations have been passed in several jurisdictions in which the Company operates, including various countries within Europe and Asia, certain Canadian provinces and certain states within the U.S. Although the Company does not anticipate any material adverse effects in the future based on the nature of its operations and the thrust of such laws, there is no assurance that such existing laws or future laws will not have a material adverse effect on the Company's financial condition or operating results.

Note 9 – Segment Information and Geographic Data

In accordance with Statement of Financial Accounting Standards ("SFAS") No. 131, *Disclosures about Segments of an Enterprise and Related Information*, the Company reports segment information based on the "management" approach. The management approach designates the internal reporting used by management for making decisions and assessing performance as the source of the Company's reportable segments.

The Company manages its business primarily on a geographic basis. Accordingly, the Company determined its operating segments, which are generally based on the nature and location of its customers, to be the Americas, Europe, Japan, Asia-Pacific, Retail, and FileMaker operations. The Company's reportable operating segments consist of Americas, Europe, Japan, and Retail operations. Other operating segments include Asia Pacific, which encompasses Australia and Asia except for Japan, and the Company's FileMaker, Inc. subsidiary. The Americas, Europe, Japan, and Asia Pacific segments exclude activities related to the Retail segment. The Americas segment includes both North and South America. The Europe segment includes European countries, as well as the Middle East and Africa. The Retail segment operates Apple-owned retail stores in the U.S. and in international markets. Each reportable operating segment provides similar hardware and software products and similar services to the same types of customers. The accounting policies of the various segments are the same as those described in Note 1, "Summary of Significant Accounting Policies" of this Form 10-Q and in the Notes to Consolidated Financial Statements in the Company's 2008 Form 10-K.

The Company evaluates the performance of its operating segments based on net sales and operating income. Net sales for geographic segments are generally based on the location of customers, while Retail segment net sales are based on sales from the Company's retail stores. Operating income for each segment includes net sales to third parties, related cost of sales, and operating expenses directly attributable to the segment. Advertising expenses are generally included in the geographic segment in which the expenditures are incurred. Operating income for each segment excludes other income and expense and certain expenses managed outside the operating segments. Costs excluded from segment operating income include various corporate expenses, such as manufacturing costs and variances not included in standard costs, research and development, corporate marketing expenses, stock-based compensation expense, income taxes, various nonrecurring charges, and other separately managed general and administrative costs. The Company does not include intercompany transfers between segments for management reporting purposes. Segment assets exclude corporate assets, such as cash, short-term and long-term investments, manufacturing and corporate facilities, miscellaneous corporate infrastructure, goodwill and other acquired intangible assets. Except for the Retail segment, capital asset purchases for long-lived assets are not reported to management by segment. Cash payments for capital asset purchases by the Retail segment were $71 million and $75 million during the first quarters of 2009 and 2008, respectively.

The Company has certain retail stores that have been designed and built to serve as high-profile venues to promote brand awareness and serve as vehicles for corporate sales and marketing activities. Because of their unique design elements, locations and size, these stores require substantially more investment than the Company's more typical retail stores. The Company allocates certain operating expenses associated with its high-profile stores to corporate marketing expense to reflect the estimated Company-wide benefit. The allocation of these operating costs to corporate expense is based on the amount incurred for a high-profile store in excess of that incurred by a more typical Company retail location. The Company had opened a total of 11 high-profile stores as of December 27, 2008. Expenses allocated to corporate marketing resulting from the operations of high-profile stores were $16 million and $11 million in the first quarters of 2009 and 2008, respectively.

Summary information by operating segment for the three months ended December 27, 2008 and December 29, 2007 is as follows (in millions):

	Three Months Ended	
	December 27, 2008	**December 29, 2007**
Americas:		
Net sales	$ 4,501	$ 4,298
Operating income	$ 1,270	$ 1,173
Europe:		
Net sales	$ 2,771	$ 2,471
Operating income	$ 809	$ 760
Japan:		
Net sales	$ 481	$ 400
Operating income	$ 127	$ 108
Retail:		
Net sales	$ 1,740	$ 1,701
Operating income	$ 353	$ 405
Other Segments (a):		
Net sales	$ 674	$ 738
Operating income	$ 184	$ 199

(a) Other Segments consist of Asia-Pacific and FileMaker.

A reconciliation of the Company's segment operating income to the Condensed Consolidated Financial Statements for the three months ended December 27, 2008 and December 29, 2007 is as follows (in millions):

	Three Months Ended	
	December 27, 2008	December 29, 2007
Segment operating income	$ 2,743	$ 2,645
Stock-based compensation expense	(170)	(110)
Other corporate expenses, net (a)	(447)	(409)
Total operating income	$ 2,126	$ 2,126

(a) Other corporate expenses include research and development, corporate marketing expenses, manufacturing costs and variances not included in standard costs, and other separately managed general and administrative expenses, including certain corporate expenses associated with support of the Retail segment.

Note 10 – Related Party Transactions and Certain Other Transactions

The Company entered into a Reimbursement Agreement with its CEO, Steve Jobs, for the reimbursement of expenses incurred by Mr. Jobs in the operation of his private plane when used for Apple business. The Company recognized a total of $4,000 and $550,000 in expenses pursuant to the Reimbursement Agreement during the first quarters of 2009 and 2008, respectively. All expenses recognized pursuant to the Reimbursement Agreement have been included in selling, general, and administrative expenses in the Condensed Consolidated Statements of Operations.

Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations

This section and other parts of this Form 10-Q contain forward-looking statements that involve risks and uncertainties. Forward-looking statements can be identified by words such as "anticipates," "expects," "believes," "plans," "predicts," and similar terms. Forward-looking statements are not guarantees of future performance and the Company's actual results may differ significantly from the results discussed in the forward-looking statements. Factors that might cause such differences include, but are not limited to, those discussed in Part II, Item 1A, "Risk Factors," which are incorporated herein by reference. The following discussion should be read in conjunction with the Company's Annual Report on Form 10-K for the year ended September 27, 2008 (the "2008 Form 10-K") filed with the U.S. Securities and Exchange Commission ("SEC") and the Condensed Consolidated Financial Statements and notes thereto included elsewhere in this Form 10-Q. All information presented herein is based on the Company's fiscal calendar. Unless otherwise stated, references in this report to particular years or quarters refer to the Company's fiscal years ended in September and the associated quarters of those fiscal years. The Company assumes no obligation to revise or update any forward-looking statements for any reason, except as required by law.

Available Information

The Company's Annual Report on Form 10-K, Quarterly Reports on Form 10-Q, Current Reports on Form 8-K, and amendments to reports filed pursuant to Sections 13(a) and 15(d) of the Securities Exchange Act of 1934, as amended ("Exchange Act") are filed with the SEC. Such reports and other information filed by the Company with the SEC are available on the Company's website at http://www.apple.com/investor when such reports are available on the SEC website. The public may read and copy any materials filed by the Company with the SEC at the SEC's Public Reference Room at 100 F Street, NE, Room 1580, Washington, DC 20549. The public may obtain information on the operation of the Public Reference Room by calling the SEC at 1-800-SEC-0330. The SEC maintains an Internet site that contains reports, proxy, and information statements and other information regarding issuers that file electronically with the SEC at http://www.sec.gov. The contents of these websites are not incorporated into this filing. Further, the Company's references to the URLs for these websites are intended to be inactive textual references only.

Executive Overview

The Company designs, manufactures, and markets personal computers, portable digital music players, and mobile communication devices and sells a variety of related software, services, peripherals, and networking solutions. The Company's products and services include the Mac® line of desktop and portable computers, the iPod® line of portable digital music players, iPhone™, Apple TV®, Xserve®, a portfolio of consumer and professional software applications, the Mac OS® X operating system, third-party digital content through the iTunes Store®, and a variety of accessory, service and support offerings. The Company sells its products worldwide through its online stores, its retail stores, its direct sales force, and third-party wholesalers, retailers, and value-added resellers. In addition, the Company sells a variety of third-party Mac, iPod and iPhone compatible products, including application software, printers, storage devices, speakers, headphones, and various other accessories and peripherals through its online and retail stores. The Company sells to consumer, small and mid-sized business ("SMB"), education, enterprise, government, and creative markets. A further description of the Company's products may be found below under the heading "Products" and Part II, Item 1A, "Risk Factors," as well as in Part I, Item 1, "Business," of the Company's 2008 Form 10-K.

The Company is focused on providing innovative products and solutions to consumer, SMB, education, enterprise, government and creative customers that greatly enhance their evolving digital lifestyles and workplace. The Company is the only participant in the personal computer and consumer electronics industries that controls the design and development of the entire personal computer, including the hardware, operating system, and sophisticated software applications, as well as the design and development of portable digital music players, mobile communication devices, and a variety of products and solutions for obtaining and enjoying digital content. The Company is therefore uniquely positioned to offer superior and well-integrated digital lifestyle products and solutions, which are further enhanced by the Company's emphasis on ease-of-use and creative industrial designs.

The Company participates in several highly competitive markets, including personal computers with its Mac line of personal computers, consumer electronics with its iPod product families, mobile communications with iPhone, and distribution of third-party digital content through its online iTunes Store. While the Company is widely recognized as a leading innovator in the personal computer and consumer electronics markets as well as a leader in the emerging market for distribution of digital content, these markets are highly competitive and subject to aggressive pricing. To remain competitive, the Company believes that increased investment in research and development and marketing and advertising is necessary to maintain or expand its position in the markets where it competes. The Company's R&D spending is focused on further developing its existing Mac line of personal computers, its operating system, application software, iPhone and iPods; developing new digital lifestyle consumer and professional software applications; and investing in new product areas and technologies. The Company also believes increased investment in marketing and advertising programs is critical to increasing product and brand awareness.

The Company utilizes a variety of direct and indirect distribution channels. The Company believes that sales of its innovative and differentiated products are enhanced by knowledgeable salespersons who can convey the value of the hardware, software, and peripheral integration, demonstrate the unique digital lifestyle solutions that are available on Mac computers, and demonstrate the compatibility of the Mac with the Windows platform and networks. The Company further believes providing a high-quality sales and after-sales support experience is critical to attracting new and retaining existing customers. To ensure a high-quality buying experience for its products in which service and education are emphasized, the Company continues to expand and improve its distribution capabilities by opening its own retail stores in the U.S. and internationally. The Company had 251 stores open as of December 27, 2008.

The Company has also invested in programs to enhance reseller sales, including the Apple Sales Consultant Program, which places Apple employees and contractors at selected third-party reseller locations. The Company believes providing direct contact with its targeted customers is an efficient way to demonstrate the advantages of its Mac computers and other products over those of its competitors. The Company also sells to customers directly through its online stores around the world and through its direct sales force.

The Company's iPods are sold through a significant number of distribution points to provide broad access. iPods can be purchased in certain department stores, member-only warehouse stores, large retail chains, and specialty retail stores, as well as through the channels for Mac distribution listed above.

iPhone is distributed through the Company, its cellular network carriers' distribution channels, and certain third-party resellers. The Company has signed multi-year agreements with various cellular network carriers authorizing them to distribute and provide cellular network services for iPhone 3G. These agreements are generally not exclusive with a specific carrier, except in the U.S., U.K., Germany, Spain, Ireland, and certain other countries. The Company has shipped iPhone 3G in over 70 countries as of December 2008.

Products

The Company offers a range of personal computing products including desktop and portable personal computers, related devices and peripherals, and various third-party hardware and software products. In addition, the Company offers its own software products, including Mac OS X, the Company's proprietary operating system software for the Mac; server software and related solutions; professional application software; and consumer, education, and business oriented application software. The Company also designs, develops, and markets to Mac and Windows users its family of iPod digital music players and its iPhone mobile communication device, along with related accessories and services, including the online distribution of third-party content through the Company's iTunes Store.

In January 2009, the Company announced its redesigned 17-inch MacBook® Pro model, which includes the all-metal unibody enclosure and a new built-in battery that delivers up to eight hours of use and up to 1,000 recharges. The new 17-inch MacBook Pro has a widescreen light-emitting diode display, Intel Core 2 Duo processors running at up to 2.93GHz, and the NVIDIA GeForce 9600M GT graphics processor. The Company expects to begin shipping the new 17-inch MacBook Pro in late January 2009.

In January 2009, the Company announced iLife® '09, which features major upgrades to iPhoto®, iMovie® and GarageBand®, and includes iDVD® and an updated version of iWeb™. iPhoto '09 adds Faces and Places as new ways to easily organize and manage photos, iMovie '09 adds new features including Precision Editor and video stabilization, and GarageBand '09 introduces a new way to help users learn to play the piano and guitar. The Company expects to begin shipping iLife® '09 in late January 2009.

In January 2009, the Company introduced and released iWork® '09, the latest version of its office productivity suite, which features upgrades to Keynote®, Pages® and Numbers®. Among the new features in iWork, Keynote '09 introduces advanced object transitions, Pages '09 features a new full screen view, and Numbers '09 introduces a quick way to group and summarize data and a simplified way to create complex formulas.

A detailed discussion of the Company's other products may be found in Part I, Item 1, "Business," of the Company's 2008 Form 10-K.

Critical Accounting Policies and Estimates

The preparation of financial statements and related disclosures in conformity with U.S. generally accepted accounting principles and the Company's discussion and analysis of its financial condition and operating results require the Company's management to make judgments, assumptions, and estimates that affect the amounts reported in its Condensed Consolidated Financial Statements and accompanying notes. Note 1, "Summary of Significant Accounting Policies" of this Form 10-Q and in the Notes to Consolidated Financial Statements in the Company's 2008 Form 10-K describes the significant accounting policies and methods used in the preparation of the Company's Condensed Consolidated Financial Statements. Management bases its estimates on historical experience and on various other assumptions it believes to be reasonable under the circumstances, the results of which form the basis for making judgments about the carrying values of assets and liabilities. Actual results may differ from these estimates and such differences may be material.

Management believes the Company's critical accounting policies and estimates are those related to revenue recognition, valuation of marketable securities, allowance for doubtful accounts, inventory valuation and inventory purchase commitments, warranty costs, stock-based compensation, income taxes, and legal and other contingencies. Management considers these critical policies because they are both important to the portrayal of the Company's financial condition and operating results, and they require management to make judgments and estimates about inherently uncertain matters. The Company's senior management has reviewed these critical accounting policies and related disclosures with the Audit and Finance Committee of the Company's Board of Directors.

Revenue Recognition

Net sales consist primarily of revenue from the sale of hardware, software, music products, digital content, peripherals, and service and support contracts. The Company recognizes revenue for software products (operating system software and applications software), or any product that is considered to be software-related, in accordance with the guidance in Emerging Issues Task Force ("EITF") No. 03-5, *Applicability of AICPA Statement of Position 97-2 to Non-software Deliverables in an Arrangement Containing More-Than-Incidental Software*, (e.g., Mac computers, iPod portable digital music players and iPhone) pursuant to American Institute of Certified Public Accountants ("AICPA") Statement of Position ("SOP") No. 97-2, *Software Revenue Recognition*, as amended. For products that are not software or software-related, (e.g., digital content sold on the iTunes Store and certain Mac, iPod and iPhone supplies and accessories), the Company recognizes revenue pursuant to the Securities and Exchange Commission ("SEC") Staff Accounting Bulletin ("SAB") No. 104, *Revenue Recognition.*

The Company recognizes revenue when persuasive evidence of an arrangement exists, delivery has occurred, the sales price is fixed or determinable, and collection is probable. Product is considered delivered to the customer once it has been shipped and title and risk of loss have been transferred. For most of the Company's product sales, these criteria are met at the time the product is shipped. For online sales to individuals, for some sales to education customers in the U.S., and for certain other sales, the Company defers revenue until the customer receives the product because the Company retains a portion of the risk of loss on these sales during transit. If at the outset of an arrangement the Company determines the arrangement fee is not, or is presumed not to be, fixed or determinable, revenue is deferred and subsequently recognized as amounts become due and payable and all other criteria for revenue recognition have been met.

For both Apple TV and iPhone, the Company has indicated that from time-to-time it may provide future unspecified features and additional software products free of charge to customers. Therefore, sales of Apple TV and iPhone handsets are recognized under subscription accounting in accordance with SOP No. 97-2. The Company recognizes the associated revenue and cost of goods sold on a straight-line basis over the currently estimated 24-month economic lives of these products, with any loss recognized at the time of sale. Costs incurred by the Company for engineering, sales, marketing, and warranty are expensed as incurred.

The Company records reductions to revenue for estimated commitments related to price protection and for customer incentive programs, including reseller and end-user rebates, and other sales programs and volume-based incentives. For transactions involving price protection, the Company recognizes revenue net of the estimated amount to be refunded, provided the refund amount can be reasonably and reliably estimated and the other conditions for revenue recognition have been met. The Company's policy requires that, if refunds cannot be reliably estimated, revenue is not recognized until reliable estimates can be made or the price protection lapses. For customer incentive programs, the estimated cost of these programs is recognized at the later of the date at which the Company has sold the product or the date at which the program is offered. The Company also records reductions to revenue for expected future product returns based on the Company's historical experience. Future market conditions and product transitions may require the Company to increase customer incentive programs and incur incremental price protection obligations that could result in additional reductions to revenue at the time such programs are offered. Additionally, certain customer incentive programs require management to estimate the number of customers who will actually redeem the incentive based on historical experience and the specific terms and conditions of particular incentive programs. If a greater than estimated proportion of customers redeem such incentives, the Company would be required to record additional reductions to revenue, which would have a negative impact on the Company's results of operations.

Valuation of Marketable Securities

The Company's investments in available-for-sale securities are reported at fair value. Unrealized gains and losses related to changes in the fair value of investments are included in accumulated other comprehensive income, net of tax, as reported in the Company's Condensed Consolidated Balance Sheets. Changes in the fair value of investments impact the Company's net income only when such investments are sold or an other-than-temporary impairment is recognized. Realized gains and losses on the sale of securities are determined by specific identification of each security's cost basis. The Company regularly reviews its investment portfolio to determine if any investment is other-than-temporarily impaired due to changes in credit risk or other potential valuation concerns, which would require the Company to record an impairment charge in the period any such determination is made. In making this judgment, the Company evaluates, among other things, the duration and extent to which the fair value of an investment is less than its cost, the credit rating of the investment and any changes thereto, and the Company's ability and intent to hold the investment until the earlier of market price recovery or maturity. The Company's assessment on whether an investment is other-than-temporarily impaired or not, could change in the future due to new developments or changes in assumptions related to any particular investment.

Allowance for Doubtful Accounts

The Company distributes its products through third-party distributors, cellular network carriers, and resellers and directly to certain education, consumer, and enterprise customers. The Company generally does not require collateral from its customers; however, the Company will require collateral in certain instances to limit credit risk. In addition, when possible the Company does attempt to limit credit risk on trade receivables with credit insurance for certain customers in Latin America, Europe, Asia, and Australia and by arranging with third-party financing companies to provide flooring arrangements and other loan and lease programs to the Company's direct customers. These credit-financing arrangements are directly between the third-party financing company and the end customer. As such, the Company generally does not assume any recourse or credit-risk-sharing related to any of these arrangements. However, considerable trade receivables that are not covered by collateral, third-party flooring arrangements, or credit insurance are outstanding with the Company's distribution and retail channel partners.

The allowance for doubtful accounts is based on management's assessment of the ability to collect specific customer accounts and includes consideration of the credit-worthiness and financial condition of those specific customers. The Company records an allowance to reduce the specific receivables to the amount that it reasonably believes to be collectible. The Company also records an allowance for all other trade receivables based on multiple factors, including historical experience with bad debts, the general economic environment, the financial condition of the Company's distribution channels, and the aging of such receivables. If there is a deterioration of a major customer's financial condition, if the Company becomes aware of additional information related to the credit-worthiness of a major customer, or if future actual default rates on trade receivables in general differ from those currently anticipated, the Company may have to adjust its allowance for doubtful accounts, which would affect earnings in the period the adjustments are made.

Inventory Valuation and Inventory Purchase Commitments

The Company must order components for its products and build inventory in advance of product shipments. The Company records a write-down for inventories of components and products, including third-party products held for resale, which have become obsolete or are in excess of anticipated demand or net realizable value. The Company performs a detailed review of inventory each fiscal quarter that considers multiple factors including demand forecasts, product life cycle status, product development plans, current sales levels, and component cost trends. The personal computer, consumer electronics and mobile communications industries are subject to a rapid and unpredictable pace of product and component obsolescence and demand changes. If future demand or market conditions for the Company's products are less favorable than forecasted or if unforeseen technological changes negatively impact the utility of component inventory, the Company may be required to record additional write-downs, which would negatively affect gross margins in the period when the write-downs were recorded.

The Company accrues reserves for estimated cancellation fees related to component orders that have been cancelled or are expected to be cancelled. Consistent with industry practice, the Company acquires components through a combination of purchase orders, supplier contracts, and open orders based on projected demand information. These commitments typically cover the Company's requirements for periods ranging from 30 to 150 days. If there is an abrupt and substantial decline in demand for one or more of the Company's products or an unanticipated change in technological requirements for any of the Company's products, the Company may be required to record additional reserves for cancellation fees that would negatively affect gross margins in the period when the cancellation fees are identified and recorded.

Warranty Costs

The Company provides for the estimated cost for hardware and software warranties at the time the related revenue is recognized based on historical and projected warranty claim rates, historical and projected cost-per-claim, and knowledge of specific product failures that are outside of the Company's typical experience. Each quarter, the Company reevaluates its estimates to assess the adequacy of its recorded warranty liabilities considering the size of the installed base of products subject to warranty protection and adjusts the amounts as necessary. For products accounted for under subscription accounting pursuant to SOP No. 97-2, the Company recognizes warranty expense as incurred. If actual product failure rates or repair costs differ from estimates, revisions to the estimated warranty liability would be required and could negatively affect the Company's results of operations.

The Company periodically provides updates to its applications and operating system software to maintain the software's compliance with specifications. The estimated cost to develop such updates is accounted for as warranty cost that is recognized at the time related software revenue is recognized. Factors considered in determining appropriate accruals related to such updates include the number of units delivered, the number of updates expected to occur, and the historical cost and estimated future cost of the resources necessary to develop these updates.

Stock-Based Compensation

The Company accounts for stock-based compensation in accordance with Statement of Financial Accounting Standards ("SFAS") No. 123 (revised 2004), *Share-Based Payment*. Under the provisions of SFAS No. 123R, stock-based compensation cost is estimated at the grant date based on the award's fair-value as calculated by the Black-Scholes-Merton ("BSM") option-pricing model and is recognized as expense ratably on a straight-line basis over the requisite service period. The BSM option-pricing model requires various judgmental assumptions including expected volatility, forfeiture rates, and expected option life. Significant changes in any of these assumptions could materially affect the fair value of stock-based awards granted in the future.

Income Taxes

The Company records a tax provision for the anticipated tax consequences of the reported results of operations. In accordance with SFAS No. 109, *Accounting for Income Taxes*, the provision for income taxes is computed using the asset and liability method, under which deferred tax assets and liabilities are recognized for the expected future tax consequences of temporary differences between the financial reporting and tax bases of assets and liabilities, and for operating losses and tax credit carryforwards. Deferred tax assets and liabilities are measured using the currently enacted tax rates that apply to taxable income in effect for the years in which those tax assets are expected to be realized or settled. The Company records a valuation allowance to reduce deferred tax assets to the amount that is believed more likely than not to be realized.

The Company recognizes and measures uncertain tax positions in accordance with the Financial Accounting Standards Board ("FASB") issued Financial Interpretation No. ("FIN") 48, *Accounting for Uncertainty in Income Taxes - an interpretation of FASB Statement No. 109*, whereby the Company only recognizes the tax benefit from an uncertain tax position if it is more likely than not that the tax position will be sustained on examination by the taxing authorities, based on the technical merits of the position. The tax benefits recognized in the financial statements from such positions are then measured based on the largest benefit that has a greater than 50% likelihood of being realized upon ultimate settlement.

Management believes it is more likely than not that forecasted income, including income that may be generated as a result of certain tax planning strategies, together with the tax effects of the deferred tax liabilities, will be sufficient to fully recover the remaining deferred tax assets. In the event that the Company determines all or part of the net deferred tax assets are not realizable in the future, the Company will make an adjustment to the valuation allowance that would be charged to earnings in the period such determination is made. In addition, the calculation of tax liabilities involves significant judgment in estimating the impact of uncertainties in the application of FIN 48 and other complex tax laws. Resolution of these uncertainties in a manner inconsistent with management's expectations could have a material impact on the Company's financial condition and operating results.

Legal and Other Contingencies

As discussed in Part II, Item 1 of this Form 10-Q under the heading "Legal Proceedings" and in Note 8 "Commitments and Contingencies" in Notes to Condensed Consolidated Financial Statements, the Company is subject to various legal proceedings and claims that arise in the ordinary course of business. In accordance with SFAS No. 5, *Accounting for Contingencies*, the Company records a contingent liability when it is probable that a loss has been incurred and the amount is reasonably estimable. There is significant judgment required in both the probability determination and as to whether an exposure can be reasonably estimated. In management's opinion, the Company does not have a potential liability related to any current legal proceedings and claims that would individually or in the aggregate have a material adverse effect on its financial condition or operating results. However, the outcomes of legal proceedings and claims brought against the Company are subject to significant uncertainty. Should the Company fail to prevail in any of these legal matters or should several of these legal matters be resolved against the Company in the same reporting period, the operating results of a particular reporting period could be materially adversely affected.

Net Sales

The following table summarizes net sales and Mac unit sales by operating segment and net sales and unit sales by product during the three months ended December 27, 2008 and December 29, 2007 (in millions, except unit sales in thousands and per unit amounts):

	Three Months Ended		
	December 27, 2008	December 29, 2007	Change
Net Sales by Operating Segment:			
Americas net sales	$ 4,501	$ 4,298	5%
Europe net sales	2,771	2,471	12%
Japan net sales	481	400	20%
Retail net sales	1,740	1,701	2%
Other Segments net sales (a)	674	738	(9)%
Total net sales	$ 10,167	$ 9,608	6%
Unit Sales by Operating Segment:			
Americas Macintosh unit sales	912	841	8%
Europe Macintosh unit sales	795	705	13%
Japan Macintosh unit sales	99	91	9%
Retail Macintosh unit sales	515	504	2%
Other Segments Macintosh unit sales (a)	203	178	14%
Total Macintosh unit sales	2,524	2,319	9%
Net Sales by Product:			
Desktops (b)	$ 1,043	$ 1,515	(31)%
Portables (c)	2,511	2,037	23%
Total Macintosh net sales	3,554	3,552	— %
iPod	3,371	3,997	(16)%
Other music related products and services (d)	1,011	808	25%
iPhone and related products and services (e)	1,247	241	417%
Peripherals and other hardware (f)	378	382	(1)%
Software, service, and other sales (g)	606	628	(4)%
Total net sales	$ 10,167	$ 9,608	6%
Unit Sales by Product:			
Desktops (b)	728	977	(25)%
Portables (c)	1,796	1,342	34%
Total Macintosh unit sales	2,524	2,319	9%
Net sales per Macintosh unit sold (h)	$ 1,408	$ 1,532	(8)%
iPod unit sales	22,727	22,121	3%
Net sales per iPod unit sold (i)	$ 148	$ 181	(18)%
iPhone unit sales	4,363	2,315	88%

(a) Other Segments include Asia Pacific and FileMaker.
(b) Includes iMac, Mac mini, Mac Pro, and Xserve product lines.
(c) Includes MacBook, MacBook Air, and MacBook Pro product lines.
(d) Consists of iTunes Store sales, iPod services, and Apple-branded and third-party iPod accessories.
(e) Derived from handset sales, carrier agreements, and Apple-branded and third-party iPhone accessories.
(f) Includes sales of Apple-branded and third-party displays, wireless connectivity and networking solutions, and other hardware accessories.
(g) Includes sales of Apple-branded operating system, application software, third-party software, AppleCare, and Internet services.
(h) Derived by dividing total Mac net sales by total Mac unit sales.
(i) Derived by dividing total iPod net sales by total iPod unit sales.

Net sales during the first quarter of 2009 increased $559 million or 6% compared to the same quarter in 2008. Several factors contributed positively to this increase, including the following:

- Net sales of iPhone and related products and services were $1.2 billion in the first quarter of 2009 with iPhone handset unit sales totaling 4.4 million. Unit sales of iPhone increased 2.0 million or 88% during the first quarter of 2009 compared to the same quarter in 2008. iPhone net sales include the portion of handset revenue recognized in accordance with subscription accounting over the product's 24-month estimated economic life, as well as revenue from sales of iPhone accessories and carrier agreements. The Company was shipping iPhone 3G in over 70 countries as of December 2008.
- Net sales of other music related products and services increased $203 million or 25% during the first quarter of 2009 compared to the same quarter in 2008, due primarily to increased net sales from the iTunes Store, which experienced double-digit growth in each of the Company's geographic segments. The Company believes this continued growth is the result of heightened consumer interest in downloading third-party digital content, the expansion of third-party audio and video content available for sale and rent via the iTunes Store, and the launch of the iTunes® App Store. The Company continues to expand its iTunes content offerings around the world.
- Mac net sales were flat year over year, while Mac unit sales increased by 205,000 units or 9% during the first quarter of 2009 compared to the same quarter in 2008. Net sales of the Company's Macs accounted for 35% of the Company's total net revenue. Higher Mac unit sales were attributed primarily to an increase in unit sales of portables, which experienced year-over-year growth in each of the Company's reportable operating segments. The increase in net sales of portables was offset by a decrease in net sales of desktops.

  Net sales and unit sales of the Company's Mac portable systems increased by 23% and 34%, respectively, during the first quarter of 2009 compared to the same quarter in 2008. The growth in Mac portable systems was attributable to strong demand for the MacBook and MacBook Pro, which had year-over-year unit sales growth in each of the Company's reportable operating segments. Conversely, net sales and unit sales of the Company's Mac desktop systems decreased by 31% and 25%, respectively, during the first quarter of 2009 compared to the same quarter in 2008. This decline was due primarily to decreased net sales and unit sales of iMac in each of the Company's reportable operating segments.

Partially offsetting the favorable factors, discussed above, net sales during the first quarter of 2009 were negatively impacted by certain factors, including the following:

- Net sales of iPods decreased $626 million or 16% during the first quarter of 2009 compared to the same quarter in 2008. iPod unit sales totaled 22.7 million in the first quarter of 2009, an increase of 3% over the first quarter of 2008. Net sales per iPod unit sold decreased 18% from $181 in the first quarter of 2008 to $148 in the first quarter of 2009, resulting from lower average selling prices across each of the iPod product lines as a result of the price reductions taken with the introduction of new iPods in September 2008 as well as the price reduction taken on iPod shuffle in February 2008.
- Net sales of software, service, and other sales decreased $22 million or 4% during the first quarter of 2009 compared to the same quarter in 2008. This decline was driven largely by a decrease in Apple-branded and third-party software products, partially offset by an increase in net sales of AppleCare Protection Plan ("APP") extended service and support contracts. During the first quarter of 2008, net sales of software, service, and other sales were largely driven by strong demand for Mac OS X Leopard which was released during that quarter. There were no comparable software releases in the first quarter of 2009.

Segment Operating Performance

The Company manages its business primarily on a geographic basis. The Company's reportable operating segments consist of the Americas, Europe, Japan, and Retail. The Americas, Europe, and Japan reportable segments do not include activities related to the Retail segment. The Americas segment includes both North and South America. The Europe segment includes European countries as well as the Middle East and Africa. The Retail segment operates Apple-owned retail stores in the U.S. and in international markets. Each reportable geographic operating segment and the Retail operating segment provide similar hardware and software products and similar services.

Americas

Net sales in the Americas segment during the first quarter of 2009 increased $203 million or 5% over the first quarter of 2008, while Americas Mac unit sales increased 8% year-over-year. The increase in net sales during the first quarter of 2009 was attributable to higher sales of iPhone, Mac portable systems, and sales from the iTunes Store, which were partially offset by a decrease in sales of iPods, iMac, and software, as well as the weakening of the Canadian dollar against the U.S. dollar. Sales of Mac portable products increased due primarily to strong demand for MacBook and MacBook Pro, both of which were updated in October 2008. The Americas segment represented 44% and 45% of the Company's total net sales in the first quarters of 2009 and 2008, respectively.

Europe

Net sales in Europe increased $300 million or 12% during the first quarter of 2009 compared to the first quarter in 2008. This growth was driven primarily by iPhone, with Mac portable systems and sales from the iTunes Store also contributing to the increase in net sales. The net sales increase was partially offset by lower year-over-year sales of iPods and iMac, as well as the effect of foreign currency movements against the U.S. dollar during the first quarter of 2009. Total Mac unit sales in Europe increased 13% year-over-year, due primarily to an increase in net sales of Mac portable systems, particularly MacBook.

Japan

Japan's net sales increased $81 million or 20% during the first quarter of 2009 compared to the first quarter of 2008, while Mac unit sales increased 9% year-over-year. The key contributors to Japan's net sales growth were increased sales of iPhone, Mac portable systems, and iPods, as well as a weaker U.S. dollar compared to the Japanese yen, which were partially offset by a decrease in sales of iMac. Net sales and unit sales of iPods increased during the first quarter of 2009 compared to the first quarter in 2008, driven primarily by strong demand for iPod nano, which was updated in September 2008.

Retail

Retail net sales increased $39 million or 2% during the first quarter of 2009 compared to the first quarter of 2008, and Mac unit sales increased 2% over the same period. The increase in net sales was due to higher sales of iPhone and Mac portable systems, which were partially offset by lower sales of iPods, iMac, and software. Retail Mac unit sales grew due to increased sales of Mac portable systems, partially offset by lower sales of iMac. The Company opened four new retail stores during the first quarter of 2009, ending the quarter with 251 stores open as compared to 204 stores at the end of the first quarter of 2008. The growth in Retail net sales was less than the growth in the number of stores open. As a result, with an average of 249 stores and 201 stores open during the first quarters of 2009 and 2008, respectively, average revenue per store declined to $7.0 million for the first quarter of 2009 from $8.5 million in the first quarter of 2008. The Retail segment reported operating income of $353 million during the first quarter of 2009 compared to operating income of $405 million during the first quarter in 2008. The year-over-year decrease in operating income is attributable primarily to lower average revenue per store.

Expansion of the Retail segment has required and will continue to require a substantial investment in fixed assets and related infrastructure, operating lease commitments, personnel, and other operating expenses. Capital asset purchases associated with the Retail segment since its inception totaled $1.5 billion through the end of the first quarter of 2009. As of December 27, 2008, the Retail segment had approximately 15,600 full-time equivalent employees and had outstanding lease commitments associated with retail space of $1.3 billion. The Company would incur substantial costs if it were to close multiple retail stores and such costs could adversely affect the Company's financial condition and operating results.

Other Segments

The Company's Other Segments, which consist of its Asia Pacific and FileMaker operations, experienced a decrease in net sales of $64 million, or 9% during the first quarter of 2009 as compared to the same quarter in 2008. The decrease in net sales was due primarily to lower net sales of iPods and iMacs, as well as a strengthening of the U.S. dollar against the Australian dollar and other Asian currencies, which were partially offset by increased net sales of iPhone and Mac portable systems. Mac unit sales increased 14% during the first quarter of 2009 compared to the first quarter of 2008, related primarily to strong demand for the MacBook, which was updated in October 2008.

Gross Margin

Gross margin for the three months ended December 27, 2008 and December 29, 2007 was as follows (in millions, except gross margin percentages):

	Three Months Ended	
	December 27, 2008	December 29, 2007
Net sales	$ 10,167	$ 9,608
Cost of sales	6,635	6,276
Gross margin	$ 3,532	$ 3,332
Gross margin percentage	34.7%	34.7%

Gross margin percentage for the first quarter of 2009 and 2008 was flat at 34.7%.

The Company expects its gross margin percentage to decrease in future periods compared to levels achieved during 2008 and the first quarter of 2009, and anticipates gross margin levels of about 32.5% in the second quarter of 2009 and about 30% in the second half of 2009. This expected decline is due largely to the anticipated impact of product transitions, flat or reduced pricing on new and innovative products that have higher cost structures, both expected and potential future cost increases for key components, a stronger U.S. dollar, and higher logistical costs.

The foregoing statements regarding the Company's expected gross margin percentage are forward-looking and could differ from anticipated levels because of several factors, including but not limited to certain of those set forth below in Part II, Item 1A, "Risk Factors" under the subheading "*Future operating results depend upon the Company's ability to obtain key components including, but not limited to microprocessors, NAND flash memory, DRAM and LCDs at favorable prices and in sufficient quantities*," which is incorporated herein by reference. There can be no assurance that targeted gross margin percentage levels will be achieved. In general, gross margins and margins on individual products will remain under downward pressure due to a variety of factors, including continued industry wide global product pricing pressures, increased competition, compressed product life cycles, product transitions and expected increases in the cost of key components including, but not limited to microprocessors, NAND flash memory, dynamic random access memory ("DRAM") and liquid crystal displays ("LCDs"), as well as potential increases in the costs of outside manufacturing services and a potential shift in the Company's sales mix towards products with lower gross margins. In response to these competitive pressures, the Company expects it will continue to take product pricing actions, which would adversely affect gross margins. Gross margins could also be affected by the Company's ability to manage product quality and warranty costs effectively and to stimulate demand for certain of its products. Due to the Company's significant international operations, financial results can be significantly affected in the short-term by fluctuations in exchange rates.

Operating Expenses

Operating expenses for the three months ended December 27, 2008 and December 29, 2007, were as follows (in millions, except for percentages):

	Three Months Ended	
	December 27, 2008	December 29, 2007
Research and development	$ 315	$ 246
Percentage of net sales	3%	3%
Selling, general, and administrative expenses	$ 1,091	$ 960
Percentage of net sales	11%	10%

Research and Development ("R&D")

Expenditures for R&D increased 28% or $69 million to $315 million in the first quarter of 2009 compared to $246 million in the first quarter of 2008, which was due primarily to higher stock-based compensation expenses and an increase in R&D headcount in the current year to support expanded R&D activities. In addition, $22 million of software development costs were capitalized related to Mac OS X Version 10.6 Snow Leopard and excluded from R&D expense during the first quarter of 2009, while no software development costs were capitalized during the first quarter of 2008. Although total R&D expense increased 28%, it remained flat as a percentage of net sales, which increased 6% in the first quarter of 2009 as compared to the same period in 2008. The Company continues to believe that focused investments in R&D are critical to its future growth and competitive position in the marketplace and are directly related to timely development of new and enhanced products that are central to the Company's core business strategy. As such, the Company expects to continue to invest in R&D to remain competitive.

Selling, General, and Administrative Expense ("SG&A")

SG&A increased 14% or $131 million to $1.1 billion in the first quarter of 2009 compared to $960 million in the first quarter of 2008. This increase is primarily due to higher stock-based compensation expenses, higher variable selling expenses resulting from the year-over-year increase in total net sales, an increase in SG&A headcount, the Company's continued expansion of its Retail segment, and higher spending on marketing and advertising.

Other Income and Expense

Total other income and expense decreased $42 million or 21% to $158 million during the first quarter of 2009 compared to $200 million in the first quarter of 2008. The overall decrease in other income and expense is attributable to the decline in interest rates during the first quarter of 2009 as compared to the first quarter of 2008, partially offset by the Company's higher cash, cash equivalents and marketable securities balances. The weighted-average interest rate earned by the Company on its cash, cash equivalents and marketable securities decreased to 2.37% in the first quarter of 2009 from 4.94% in the first quarter of 2008.

The Company's investment portfolio had gross unrealized losses of $122 million and $121 million as of December 27, 2008 and September 27, 2008, respectively, which was partially offset by gross unrealized gains of $83 million and $4 million as of December 27, 2008 and September 27, 2008, respectively. In both periods, the gross unrealized losses primarily related to long-term marketable securities. The Company considers the declines in market value of its marketable securities investment portfolio to be temporary in nature. The unrealized losses on the Company's marketable securities were caused primarily by changes in market interest rates, specifically, widening credit spreads. The Company has the intent and ability to hold such investments for a sufficient period of time to allow for recovery of the principal amounts invested. Accordingly, no declines in fair value were recognized in the Company's Condensed Statements of Operations. The Company may sell its marketable securities prior to their stated maturities for strategic purposes, in anticipation of credit deterioration, or for duration management. The Company recognized no material net gains or losses during the first quarters of 2009 or 2008 related to such sales.

Provision for Income Taxes

The Company's effective tax rate for the three months ended December 27, 2008 was approximately 30% compared with approximately 32% for the quarter ended December 29, 2007. The Company's effective rate for both periods differs from the statutory federal income tax rate of 35% due primarily to certain undistributed foreign earnings for which no U.S. taxes are provided because such earnings are intended to be indefinitely reinvested outside the U.S. The lower effective tax rate in the first three months of 2009 as compared to the same quarter in 2008 is due primarily to the Company recording a tax benefit as a result of legislation enacted on October 3, 2008, retroactively reinstating the research and development tax credit.

The Internal Revenue Service (the "IRS") has completed its field audit of the Company's federal income tax returns for the years 2002 through 2003 and proposed certain adjustments. The Company has contested certain of these adjustments through the IRS Appeals Office. All IRS audit issues for years prior to 2002 have been resolved. In addition, the Company is subject to audits by state, local, and foreign tax authorities. Management believes that adequate provision has been made for any adjustments that may result from tax examinations. However, the outcome of tax audits cannot be predicted with certainty. If any issues addressed in the Company's tax audits are resolved in a manner not consistent with management's expectations, the Company could be required to adjust its provision for income tax in the period such resolution occurs.

Recent Accounting Pronouncements

During the first quarter of fiscal 2009, the Company adopted SFAS No. 157, *Fair Value Measurements,* which defines fair value, provides a framework for measuring fair value, and expands the disclosures required for fair value measurements. In February 2008, the FASB issued FASB Staff Position ("FSP") No. FAS 157-2, *Effective Date of FASB Statement No. 157*. FSP 157-2 delays the effective date of SFAS No. 157 to fiscal years beginning after November 15, 2008 for all non-financial assets and non-financial liabilities, except for items that are recognized or disclosed at fair value in the financial statements on a recurring basis (at least annually) and will be adopted by the Company beginning in the first quarter of fiscal 2010. Although the Company will continue to evaluate the application of FSP 157-2, management does not currently believe adoption will have a material impact on the Company's financial condition or operating results.

In December 2007, the Financial Accounting Standards Board ("FASB") issued SFAS No. 141 (revised 2007), *Business Combinations*, which establishes principles and requirements for how an acquirer recognizes and measures in its financial statements the identifiable assets acquired, the liabilities assumed, and any noncontrolling interest in the acquiree in a business combination. SFAS No. 141R also establishes principles around how goodwill acquired in a business combination or a gain from a bargain purchase should be recognized and measured, as well as provides guidelines on the disclosure requirements on the nature and financial impact of the business combination. SFAS No. 141R is effective for fiscal years beginning on or after December 15, 2008 and will be adopted by the Company beginning in the first quarter of fiscal 2010. Although the Company will continue to evaluate the application of SFAS No. 141R, management does not currently believe adoption will have a material impact on the Company's financial condition or operating results.

In March 2008, the FASB issued SFAS No. 161, *Disclosures about Derivative Instruments and Hedging Activities—an amendment of FASB Statement No. 133,* which requires companies to provide additional disclosures about its objectives and strategies for using derivative instruments, how the derivative instruments and related hedged items are accounted for under SFAS No. 133, *Accounting for Derivative Instruments and Hedging Activities*, and related interpretations, and how the derivative instruments and related hedged items affect the Company's financial statements. SFAS No. 161 also requires companies to disclose information about credit risk-related contingent features in their hedged positions. SFAS No. 161 is effective for fiscal years and interim periods beginning after November 15, 2008 and is required to be adopted by the Company beginning in the second quarter of fiscal 2009. Although the Company will continue to evaluate the application of SFAS No. 161, management does not currently believe adoption will have a material impact on the Company's financial condition or operating results.

Liquidity and Capital Resources

The following table presents selected financial information and statistics as of December 27, 2008 and September 27, 2008 (in millions):

	December 27, 2008	September 27, 2008
Cash, cash equivalents, and marketable securities	$ 28,145	$ 24,490
Accounts receivable, net	$ 2,196	$ 2,422
Inventory	$ 396	$ 509
Working capital	$ 20,406	$ 18,219

As of December 27, 2008, the Company had $28.1 billion in cash, cash equivalents, and marketable securities, an increase of $3.7 billion from September 27, 2008. The principal component of this net increase was the cash generated by operating activities of $3.9 billion, which was partially offset by payments for acquisitions of property, plant, and equipment of $339 million. The Company's cash generated by operating activities significantly exceeded its net income due primarily to the increase in deferred revenue, net of deferred costs, associated with subscription accounting for iPhone.

The Company's marketable securities investment portfolio is invested primarily in highly rated securities with a minimum rating of single-A. As of December 27, 2008 and September 27, 2008, $12.7 billion and $11.3 billion, respectively, of the Company's cash, cash equivalents, and marketable securities were held by foreign subsidiaries and are generally based in U.S. dollar-denominated holdings. The Company believes its existing balances of cash, cash equivalents, and marketable securities will be sufficient to satisfy its working capital needs, capital asset purchases, outstanding commitments, and other liquidity requirements associated with its existing operations over the next 12 months.

Capital Assets

The Company's cash payments for capital asset purchases were $339 million during the first quarter of 2009, consisting of approximately $71 million for retail store facilities and $268 million for corporate facilities and infrastructure, including information systems enhancements. The Company anticipates utilizing approximately $1.3 billion for capital asset purchases during 2009, including approximately $350 million for Retail facilities and approximately $950 million for corporate facilities and infrastructure.

Off-Balance Sheet Arrangements and Contractual Obligations

The Company has not entered into any transactions with unconsolidated entities whereby the Company has financial guarantees, subordinated retained interests, derivative instruments or other contingent arrangements that expose the Company to material continuing risks, contingent liabilities, or any other obligation under a variable interest in an unconsolidated entity that provides financing, liquidity, market risk or credit risk support to the Company.

Lease Commitments

As of September 27, 2008, the Company had total outstanding commitments on noncancelable operating leases of $1.8 billion, $1.4 billion of which related to the lease of retail space and related facilities. The Company's major facility leases are generally for terms of 3 to 20 years and generally provide renewal options for terms of 1 to 5 years. Leases for retail space are for terms of 5 to 20 years, the majority of which are for 10 years, and often contain multi-year renewal options. Total outstanding commitments on noncancelable operating leases related to the lease of retail space increased to $1.3 billion as of December 27, 2008.

Purchase Commitments with Contract Manufacturers and Component Suppliers

The Company utilizes several contract manufacturers to manufacture sub-assemblies for the Company's products and to perform final assembly and test of finished products. These contract manufacturers acquire components and build product based on demand information supplied by the Company, which typically covers periods ranging from 30 to 150 days. The Company also obtains individual components for its products from a wide variety of individual suppliers. Consistent with industry practice, the Company acquires components through a combination of purchase orders, supplier contracts, and open orders based on projected demand information. Such purchase commitments typically cover the Company's forecasted component and manufacturing requirements for periods ranging from 30 to 150 days. In addition, the Company has an off-balance sheet warranty obligation for products accounted for under subscription accounting pursuant to SOP No. 97-2 whereby the Company recognizes warranty expense as incurred. As of December 27, 2008, the Company had outstanding off-balance sheet third-party manufacturing commitments, component purchase commitments, and estimated warranty commitments of $3.6 billion.

During 2006, the Company entered into long-term supply agreements with Hynix Semiconductor, Inc., Intel Corporation, Micron Technology, Inc., Samsung Electronics Co., Ltd., and Toshiba Corporation to secure supply of NAND flash memory through calendar year 2010. As part of these agreements, the Company prepaid $1.25 billion, which is being applied to certain inventory component purchases made over the life of each respective agreement. During the first quarter of fiscal 2009, the long-term supply agreement with Intel Corporation was terminated and the remaining prepaid balance of $167 million was repaid to the Company. As of December 27, 2008, the Company had $428 million of inventory component prepayments outstanding.

Subsequent to December 27, 2008, the Company entered into a long-term supply agreement with LG Display to purchase LCD panels for five years. As part of the agreement, the Company is required to make a prepayment of $500 million in the second quarter of 2009.

Asset Retirement Obligations

The Company's asset retirement obligations are associated with commitments to return property subject to operating leases to original condition upon lease termination. As of December 27, 2008, the Company estimated that gross expected future cash flows of approximately $28 million would be required to fulfill these obligations.

Other Obligations

Other outstanding obligations were approximately $371 million as of December 27, 2008, primarily related to advertising, research and development, Internet and telecommunications services, and other obligations.

As of December 27, 2008, the Company had gross unrecognized tax benefits of $560 million and an additional $247 million for gross interest and penalties classified as non-current liabilities in the Condensed Consolidated Balance Sheet. At this time, the Company is unable to make a reasonably reliable estimate of the timing of payments in individual years due to uncertainties in the timing of tax audit outcomes.

Indemnifications

The Company generally does not indemnify end-users of its operating system and application software against legal claims that the software infringes third-party intellectual property rights. Other agreements entered into by the Company sometimes include indemnification provisions under which the Company could be subject to costs and/or damages in the event of an infringement claim against the Company or an indemnified third-party. However, the Company has not been required to make any significant payments resulting from such an infringement claim asserted against it or an indemnified third-party and, in the opinion of management, does not have a liability related to unresolved infringement claims subject to indemnification that would have a material adverse effect on its financial condition or operating results.

Item 3. Quantitative and Qualitative Disclosures About Market Risk

The Company's market risk profile has not changed significantly during the first three months of 2009.

Interest Rate and Foreign Currency Risk Management

The Company regularly reviews its foreign exchange forward and option positions, both on a stand-alone basis and in conjunction with its underlying foreign currency and interest rate related exposures. However, given the effective horizons of the Company's risk management activities and the anticipatory nature of the exposures, there can be no assurance the hedges will offset more than a portion of the financial impact resulting from movements in either foreign exchange or interest rates. In addition, the timing of the accounting for recognition of gains and losses related to mark-to-market instruments for any given period may not coincide with the timing of gains and losses related to the underlying economic exposures and, therefore, may adversely affect the Company's financial condition and operating results.

Interest Rate Risk

While the Company is exposed to interest rate fluctuations in many of the world's leading industrialized countries, the Company's interest income and expense is most sensitive to fluctuations in the general level of U.S. interest rates. As such, changes in U.S. interest rates affect the interest earned on the Company's cash, cash equivalents, and marketable securities, the fair value of those marketable securities, as well as costs associated with foreign currency hedges.

The Company's investment policy and strategy are focused on preservation of capital and supporting the liquidity requirements of the Company. A portion of the Company's cash is managed by external managers within the guidelines of the Company's investment policy and to objective market benchmarks. The Company's internal portfolio is benchmarked against external manager performance.

The Company's exposure to market risk for changes in interest rates relates primarily to the Company's investment portfolio. The Company typically invests in highly rated securities and its policy generally limits the amount of credit exposure to any one issuer. The Company's investment policy requires investments to be rated single-A or better with the objective of minimizing the potential risk of principal loss. All highly liquid investments with initial maturities of three months or less at the date of purchase are classified as cash equivalents. The Company classifies its marketable securities as either short-term or long-term based on each instrument's underlying contractual maturity date. All short-term marketable securities have maturities less than 12 months, while all long-term marketable securities have maturities ranging from one to five years. The Company may sell its investments prior to their stated maturities for strategic purposes, in anticipation of credit deterioration, or for duration management. The Company recognized no material net gains or losses during the first quarter of 2009 or 2008 related to such sales.

Foreign Currency Risk

In general, the Company is a net receiver of currencies other than the U.S. dollar. Accordingly, changes in exchange rates, and in particular a strengthening of the U.S. dollar, will negatively affect the Company's net sales and gross margins as expressed in U.S. dollars. There is also a risk that the Company will have to adjust local currency product pricing due to competitive pressures when there has been significant volatility in foreign currency exchange rates.

The Company may enter into foreign currency forward and option contracts with financial institutions to protect against foreign exchange risks associated with existing assets and liabilities, certain firmly committed transactions, forecasted future cash flows, and net investments in foreign subsidiaries. Generally, the Company's practice is to hedge a majority of its material foreign exchange exposures, typically for three to six months. However, the Company may choose not to hedge certain foreign exchange exposures due to immateriality, prohibitive economic cost of hedging particular exposures, and limited availability of appropriate hedging instruments.

Item 4. Controls and Procedures

Evaluation of Disclosure Controls and Procedures

Based on an evaluation under the supervision and with the participation of the Company's management, the Company's principal executive officer and principal financial officer have concluded that the Company's disclosure controls and procedures as defined in Rules 13a-15(e) and 15d-15(e) under the Securities Exchange Act of 1934, as amended ("Exchange Act") were effective as of December 27, 2008 to ensure that information required to be disclosed by the Company in reports that it files or submits under the Exchange Act is (i) recorded, processed, summarized and reported within the time periods specified in the Securities and Exchange Commission rules and forms and (ii) accumulated and communicated to the Company's management, including its principal executive officer and principal financial officer, as appropriate to allow timely decisions regarding required disclosure.

Changes in Internal Control Over Financial Reporting

There were no changes in the Company's internal control over financial reporting during the first quarter of 2009, which were identified in connection with management's evaluation required by paragraph (d) of Rules 13a-15 and 15d-15 under the Exchange Act, that have materially affected, or are reasonably likely to materially affect, the Company's internal control over financial reporting.

PART II. OTHER INFORMATION

Item 1. Legal Proceedings

As of December 27, 2008, the end of the quarterly period covered by this report, the Company was subject to the various legal proceedings and claims discussed below, as well as certain other legal proceedings and claims that have not been fully resolved and that have arisen in the ordinary course of business. In the opinion of management, the Company does not have a potential liability related to any current legal proceedings and claims that would individually or in the aggregate have a material adverse effect on its financial condition or operating results. However, the results of legal proceedings cannot be predicted with certainty. Should the Company fail to prevail in any of these legal matters or should several of these legal matters be resolved against the Company in the same reporting period, the operating results of a particular reporting period could be materially adversely affected. The Company settled certain matters during the first quarter of 2009 that did not individually or in the aggregate have a material impact on the Company's results of operations.

Bader v. Anderson, et al.

Plaintiff filed this purported shareholder derivative action against the Company and each of its then current executive officers and members of its Board of Directors on May 19, 2005 in Santa Clara County Superior Court asserting claims for breach of fiduciary duty, material misstatements and omissions and violations of California Business & Professions Code §17200 (unfair competition). The complaint alleged that the Company's March 14, 2005, proxy statement was false and misleading for failure to disclose certain information relating to the Apple Computer, Inc. Performance Bonus Plan, which was approved by shareholders at the annual meeting held on April 21, 2005. Plaintiff, who ostensibly brought suit on the Company's behalf, made no demand on the Board of Directors and alleged that such demand was excused. The complaint sought injunctive and other relief for purported injury to the Company. On July 27, 2005, plaintiff filed an amended complaint alleging that, in addition to the purported derivative claims, adoption of the bonus plan and distribution of the proxy statement describing that plan also inflicted injury on her directly as an individual shareholder. On January 10, 2006, the Court sustained defendants' demurrer to the amended complaint, with leave to amend. Plaintiff filed a second amended complaint on February 7, 2006, and the Company filed a demurrer. After a hearing on June 13, 2006, the Court sustained the demurrer without leave to amend as to the non-director officers and with leave to amend as to the directors. On July 24, 2006, plaintiff filed a third amended complaint, which purported to bring claims derivatively as well as directly on behalf of a class of common stockholders who have been or will be harmed by virtue of the allegedly misleading proxy statement. In addition to reasserting prior causes of action, the third amended complaint included a claim that the Company violated the terms of the plan, and a claim for waste related to restricted stock unit grants to certain officers in 2003 and 2004 and an option grant to the Company's CEO in January 2000. The Company filed a demurrer to the third amended complaint. On January 30, 2007, the Court sustained the Company's demurrer with leave to amend. On May 8, 2007, plaintiff filed a fourth amended complaint. The Company filed a demurrer to the fourth amended complaint, which the Court sustained, without leave to amend, on October 12, 2007. On October 25, 2007, the Court entered a final judgment in favor of defendant and ordered the case dismissed with prejudice. On November 26, 2007, plaintiff filed a notice of appeal. Plaintiffs' appeal is pending.

Birdsong v. Apple Computer, Inc.

This action alleges that the Company's iPod music players, and the ear bud headphones sold with them, are inherently defective in design and are sold without adequate warnings concerning the risk of noise-induced hearing loss by iPod users. The Birdsong action was initially filed on January 30, 2006 in the United States District Court for the Western District of Louisiana asserting Louisiana causes of action on behalf of a purported Louisiana class of iPod purchasers. A similar action *(Patterson v. Apple Computer, Inc.)* was filed on January 31, 2006 in the United States District Court for the Northern District of California asserting California causes of action on behalf of a purported class of all iPod purchasers within the four-year period before January 31, 2006. The Birdsong action was transferred to the Northern District of California, and the Patterson action was dismissed. An amended complaint was subsequently filed in Birdsong, dropping the Louisiana law-based claims and adding California law-based claims equivalent to those in Patterson. After the Company filed a motion to dismiss on November 3, 2006, plaintiffs agreed not to oppose the motion and filed a second amended complaint on January 16, 2007. That complaint alleges California law-based claims for breaches of implied and express warranties, violations of California Business & Professions Code §17200 (unfair competition), California Business & Professions Code §17500 (false advertising), the Consumer Legal Remedies Act and negligent misrepresentation on behalf of a putative nationwide class and a

Louisiana law-based claim for redhibition for a Louisiana sub-class. On March 1, 2007, the Company filed a motion to dismiss the California law-based claims, which was heard on June 4, 2007. On December 14, 2007, the Court issued an order granting the Company's motion, with leave to amend the complaint. Plaintiffs filed a third amended complaint on January 11, 2008. On February 15, 2008, the Company filed a motion to dismiss the third amended complaint. On June 16, 2008, the Court granted the Company's motion to dismiss the third amended complaint with prejudice. On July 11, 2008, plaintiffs filed a notice of appeal. Plaintiffs' appeal is pending.

A similar complaint, *Royer-Brennan v. Apple Computer, Inc. and Apple Canada, Inc.,* was filed in Montreal, Quebec, Canada, on February 1, 2006, seeking authorization to institute a class action on behalf of iPod purchasers in Quebec. At the request of plaintiffs' counsel, the Court has postponed class certification proceedings in this action indefinitely.

Branning et al. v. Apple Computer, Inc.

Plaintiffs originally filed this purported class action in San Francisco County Superior Court on February 17, 2005. The initial complaint alleged violations of California Business & Professions Code §17200 (unfair competition) and violation of the Consumer Legal Remedies Act regarding a variety of purportedly unfair and unlawful conduct including, but not limited to, allegedly selling used computers as new and failing to honor warranties. Plaintiffs also brought causes of action for misappropriation of trade secrets, breach of contract and violation of the Song-Beverly Consumer Warranty Act. Plaintiffs requested unspecified damages and other relief. On May 2, 2005, plaintiffs filed an amended complaint adding two new named plaintiffs and three new causes of action including a claim for treble damages under the Cartwright Act (California Business & Professions Code §16700 et seq.) and a claim for false advertising. On May 9, 2005, the Court granted the Company's motion to transfer the case to Santa Clara County Superior Court. The Company filed a demurrer to the amended complaint, which the Court sustained in its entirety on November 10, 2005. The Court granted plaintiffs leave to amend and they filed an amended complaint on December 29, 2005. Plaintiffs' amended complaint added three plaintiffs and alleged many of the same factual claims as the previous complaints, such as alleged selling of used equipment as new, alleged failure to honor warranties and service contracts for the consumer plaintiffs, and alleged fraud related to the opening of the Apple retail stores. Plaintiffs continued to assert causes of action for unfair competition (§17200), violations of the Consumer Legal Remedies Act, breach of contract, misappropriation of trade secrets, violations of the Cartwright Act, and alleged new causes of action for fraud, conversion, and breach of the implied covenant of good faith and fair dealing. The Company filed a demurrer to the amended complaint on January 31, 2006, which the Court sustained on March 3, 2006 on sixteen of seventeen causes of action. Plaintiffs filed an amended complaint adding one new plaintiff. The Company filed a demurrer, which was granted in part on September 9, 2006. Plaintiffs filed a further amended complaint on September 21, 2006. On October 2, 2006, the Company filed an answer denying all allegations and asserting numerous affirmative defenses. On November 30, 2007, the Company filed a motion for judgment on the pleadings, which the Court denied. Plaintiffs filed a Fifth Amended Complaint on March 19, 2008 and a Corrected Fifth Amended Complaint on April 1, 2008. The Company filed an answer to the Corrected Fifth Amended Complaint on April 18, 2008. The Company filed a motion for judgment on the pleadings for an order dismissing plaintiffs' fraud claim based upon the statute of limitations, which was granted by the Court on June 24, 2008, with leave to amend. Plaintiffs filed a Sixth Amended Complaint on July 14, 2008 and a Seventh Amended Complaint on August 22, 2008, adding three new reseller plaintiffs. On August 22, 2008, plaintiffs also filed a motion to certify the consumer class. On September 22, 2008, the Company filed its answer to the consumer-related claims denying all allegations and asserting numerous affirmative defenses, and also filed a demurrer to the new reseller claims, which is set for a hearing on January 30, 2009. The Company filed motions for summary adjudication for certain claims of two named plaintiffs', which the Court granted on November 10, 2008. Plaintiffs petitioned the Court of Appeal for a writ of certiorari from the summary adjudication ruling and a motion to stay the class certification hearing, which the Court of Appeal denied on December 17, 2008. On December 19, 2008, the Court held a hearing on plaintiffs' class certification motion. The Court requested further briefing and an additional hearing is set for February 20, 2009.

Gordon v. Apple Computer, Inc.

Plaintiff filed this purported class action on August 31, 2006 in the United States District Court for the Northern District of California, San Jose Division, on behalf of a purported nationwide class of consumers who purchased 65W Power Adapters for iBooks and Powerbooks between November 2002 and the present. The complaint alleges various problems with the 65W Adapter, including fraying, sparking, and premature failure. Plaintiff alleges violations of California Business & Professions Code §17200 (unfair competition), the Consumer Legal Remedies Act, the Song-Beverly Consumer Warranty Act and breach of warranties. The complaint seeks damages and equitable relief. The Company filed an answer on October 20, 2006 denying the material allegations and asserting numerous affirmative defenses. The Company has reached a settlement of this matter and the parties have received final court approval for the settlement.

Harvey v. Apple Inc.

Plaintiff filed this action on August 6, 2007 in the United States District Court for the Eastern District of Texas, Marshall Division, alleging infringement by the Company of U.S. Patent No. 6,753,671 entitled “Recharger for use with a portable electronic device and which includes a proximally located light emitting device” and U.S. Patent No. 6,762,584 entitled “Recharger for use with a portable electronic device and which includes a connector terminus for communicating with rechargeable batteries contained within the device.” The complaint seeks unspecified damages and other relief. The Company filed an answer on October 12, 2007 denying all material allegations and asserting numerous affirmative defenses. The Company also asserted counterclaims for declaratory judgment of non-infringement and invalidity. On April 7, 2008, plaintiff filed an amended complaint further alleging infringement of the reissue patent of U.S. Patent No. 6,753,671. On April 28, 2008, the Company filed an answer denying all material allegations and asserting numerous affirmative defenses. The Company also asserted counterclaims for declaratory judgment of non-infringement and invalidity. The Markman hearing is set for October 28, 2009, and trial is scheduled for April 5, 2010.

Honeywell International, Inc., et al. v. Apple Computer, Inc., et al.

Plaintiffs Honeywell International, Inc. and Honeywell Intellectual Properties, Inc. filed this action on October 6, 2004 in the United States District Court in Delaware alleging infringement by the Company and other defendants of U.S. Patent 5,280,371 entitled “Directional Diffuser for a Liquid Crystal Display.” Plaintiffs seek unspecified damages and other relief. The Company filed an answer on December 21, 2004 denying all material allegations and asserting numerous affirmative defenses. The Company has tendered the case to several liquid crystal display manufacturer suppliers. On May 18, 2005 the Court stayed the case against the Company and the other non-manufacturer defendants. Plaintiffs filed an amended complaint on November 7, 2005 adding additional defendants and expanding the scope of the accused products. The Company’s response to the amended complaint is not yet due. On April 2, 2008, the Court lifted the stay for the purpose of determining whether the liquid crystal display manufacturer suppliers used by the Company and certain other defendants are licensed under the ‘371 patent. On October 31, 2008, the Company filed a motion for summary judgment of non-infringement based on the contention that its suppliers are licensed under the ‘371 patent. A hearing on the motion is scheduled for January 30, 2009.

In re Apple Computer, Inc. Derivative Litigation (formerly Karant v. Jobs, et al. and Related Actions) (Federal Action)

On June 30, 2006, a putative derivative action captioned *Karant v. Jobs, et. al.*, was filed in the United States District Court for the Northern District of California, San Jose Division. A number of related actions were filed in the subsequent weeks and have been consolidated into a single action captioned *In re Apple Computer, Inc. Derivative Litigation*, Master File No. C-06-04128-JF before the Hon. Jeremy Fogel. The actions were filed after the Company’s announcement on June 29, 2006 that an internal investigation had discovered irregularities related to the issuance of certain stock option grants made between 1997 and 2001, that a special committee of the Company’s outside directors had retained independent counsel to perform an investigation and that the Company had informed the Securities and Exchange Commission. The action purports to assert claims on behalf of the Company against several current and former executive officers and members of the Board of Directors alleging improper backdating of stock option grants to maximize certain defendants’ profits, failing to properly account for and take tax deductions for those grants, insider trading, and issuing false financial statements. The Company is named as a nominal defendant. The consolidated complaint alleges various causes of action under federal and California law, including claims for unjust enrichment, breach of fiduciary duty, violation of the California Corporations Code, abuse of control, gross mismanagement, rescission, constructive fraud and waste of corporate assets, as well as claims under Sections 10(b), 14(a) and 20(a) of the Securities Exchange Act. Plaintiffs seek damages, disgorgement, restitution and imposition of a constructive trust. A Consolidated Shareholder Derivative Complaint was filed on December 18, 2006, and a First Amended Shareholder Derivative Complaint was filed on March 6, 2007. On June 12, 2007, the Company’s Board of Directors approved a resolution appointing a Special Litigation Committee to make all decisions relating to options litigation. Defendants filed a motion to dismiss on April 20, 2007, which was heard on September 7, 2007. On November 19, 2007, the Court granted the defendants’ motion to dismiss with leave to amend. Plaintiffs filed an amended complaint on December 19, 2007. Defendants filed motions to dismiss the amended complaint on January 25, 2008. The motions to dismiss were originally scheduled to be heard on April 4, 2008. Pursuant to a joint stipulation filed on April 3, 2008, the Court vacated the hearing date. The parties have reached a settlement, and the Court has granted final approval of the settlement. On November 10, 2008, the Court entered final judgment and dismissed the case.

In re Apple Computer, Inc. Derivative Litigation (formerly Plumbers and Pipefitters v. Jobs, et al. and Related Actions) (State Action); Boston Retirement Board v. Apple Computer, Inc.

On July 5, 2006, a putative derivative action captioned *Plumbers and Pipefitters v. Jobs, et. al.*, was filed in California Superior Court for the County of Santa Clara. A number of related actions were filed in the subsequent weeks, and have been consolidated into a single action captioned *In re Apple Computer, Inc. Derivative Litigation*, No. 1:06CV066692, assigned to the Hon. Joseph Huber. These actions purport to assert claims on behalf of the Company against several current and former executive officers and members of the Board of Directors alleging improper backdating of stock option grants to maximize certain defendants' profits, failing to properly account for and take tax deductions for those grants and issuing false financial statements. The Company is named as a nominal defendant. A consolidated complaint was filed on October 5, 2006, alleging a variety of causes of action under California law, including claims for unjust enrichment, breach of fiduciary duty, violation of the California Corporations Code, abuse of control, accounting, constructive trust, rescission, deceit, gross mismanagement and waste of corporate assets. On December 7, 2006, the Court granted the Company's motion to stay these actions. The parties have reached a settlement, and the Court has granted final approval of the settlement. On November 24, 2008, the Court entered final judgment and dismissed the case.

On November 3, 2006, the Boston Retirement Board, a purported shareholder, filed a petition for writ of mandate against the Company in California Superior Court for the County of Santa Clara (*Boston Retirement Board v. Apple Computer Inc.*). The petition sought to compel the Company to allow inspection of certain corporate records relating to the Company's option practices and the Special Committee's investigation. Following a trial held on September 24, 2007, the Court granted the petition for inspection but narrowed the scope of the records to be produced. On April 16, 2008, the Boston Retirement Board filed a derivative action in California Superior Court for the County of Santa Clara. On July 31, 2008, Boston Retirement Board attempted to serve the new complaint on the Company. On September 15, 2008, defendants filed a motion to quash service of summons. On October 17, 2008, the Court denied defendants' motion to quash. On October 20, 2008, defendants requested consolidation of this action with *In re Apple Computer, Inc. Derivative Litigation*, No. 1:06CV066692, and a stay of the action. On November 6, 2008, Boston Retirement Board filed a motion for fees. On November 7, 2008, the Court issued an order relating this action to the State Derivative Litigation. A stipulation for dismissal was filed on December 10, 2008, in which Boston Retirement Board agrees to dismiss the case with prejudice upon a final order regarding its fees motion. On January 15, 2009, the Court denied Boston Retirement Board's motion for fees.

In re Apple iPod Nano Products Liability Litigation (formerly Wimmer v. Apple Computer, Inc.; Moschella, et al., v. Apple Computer, Inc.; Calado, et al. v. Apple Computer, Inc.; Kahan, et al., v. Apple Computer, Inc.; Jennings, et al., v. Apple Computer, Inc.; Rappel v. Apple Computer, Inc.; Mayo v. Apple Computer, Inc.; Valencia v. Apple Computer, Inc.; Williamson v. Apple Computer, Inc.; Sioson v. Apple Computer, Inc.

Beginning on October 19, 2005, eight complaints were filed in various United States District Courts and two complaints were filed in California State Court alleging that the Company's iPod nano was defectively designed so that it scratches excessively during normal use, rendering the screen unreadable.

The federal actions were coordinated in the United States District Court for the Northern District of California and assigned to the Hon. Ronald Whyte pursuant to an April 17, 2006 order of the Judicial Panel on Multidistrict Litigation. Plaintiffs filed a First Consolidated and Amended Master Complaint on September 21, 2006, alleging violations of California and other states' consumer protection and warranty laws and claiming unjust enrichment. The Master Complaint alleges two putative plaintiff classes: (1) all U.S. residents (excluding California residents) who purchased an iPod nano that was not manufactured or designed using processes necessary to ensure normal resistance to scratching of the screen; and (2) all iPod nano purchasers other than U.S. residents who purchased an iPod nano that was not manufactured or designed using processes necessary to ensure normal resistance to scratching of the screen. The Company answered the Master Complaint on November 20, 2006.

The two California State Court actions were coordinated on May 4, 2006, and assigned to the Hon. Carl West in Los Angeles Superior Court. Plaintiffs filed a Consolidated Amended Class Action Complaint on June 8, 2006, alleging violations of California state consumer protection, unfair competition, false advertising and warranty laws and claiming unjust enrichment. The Consolidated Complaint alleges a putative plaintiff class of all California residents who own an iPod nano containing a manufacturing defect that results in the nano being susceptible to excessive scratching. The Company answered the Consolidated Amended Complaint on October 6, 2006. The parties have reached a settlement and the Court has granted preliminary approval of the settlement. The parties' request for final approval of the settlement is pending.

Individual Networks, LLC v. Apple, Inc.

Plaintiff filed this action against the Company on April 24, 2007 in the United States District Court for the Eastern District of Texas, Marshall Division, alleging infringement of U.S. Patent No. 7,117,516, entitled "Method and System for Providing a Customized Media List." Plaintiff alleges certain features of the iTunes store infringe the patent. The complaint seeks unspecified damages and other relief. The Company filed an answer on July 2, 2007, denying all material allegations and asserting numerous affirmative defenses. The Company also asserted counterclaims for declaratory judgment of non-infringement and invalidity, as well as a counterclaim against Individual Networks LLC for infringement of U.S. Patent No. 5,724,567. The trial is scheduled for November 9, 2009. The Company has filed a petition with the United States Patent and Trademark Office requesting reexamination of U.S. Patent No. 7,117,516. The Markman hearing took place on October 8, 2008, and the Court issued its Markman ruling on January 12, 2009.

Mediostream, Inc. v. Acer America Corp. et al.

Plaintiff filed this action against the Company, Acer America Corp., Dell, Inc. and Gateway, Inc. on August 28, 2007 in the United States District Court for the Eastern District of Texas, Marshall Division, alleging infringement of U.S. Patent No. 7,009,655, entitled "Method and System for Direct Recording of Video Information onto a Disk Medium." An amended complaint was served on November 7, 2007. The amended complaint seeks unspecified damages and other relief. On January 25, 2008, the Company filed an answer to the complaint denying all material allegations and asserting numerous affirmative defenses and also filed a motion to transfer the case to the Northern District of California, which the Court denied. On December 4, 2008, the Company moved for reconsideration of the Court's denial of the motion to transfer. The Markman hearing is set for August 4, 2010 and trial is scheduled for January 4, 2011.

OPTi Inc. v. Apple Inc.

Plaintiff filed this action against the Company on January 16, 2007 in the United States District Court for the Eastern District of Texas, Marshall Division, alleging infringement of U.S. Patent Nos. 5,710,906, 5,813,036 and 6,405,291, all entitled "Predictive Snooping of Cache Memory for Master-Initiated Accesses." The complaint seeks unspecified damages and other relief. The Company filed an answer on April 17, 2007 denying all material allegations and asserting numerous affirmative defenses. The Company also asserted counterclaims for declaratory judgment of non-infringement and invalidity. The Markman hearing took place on November 26, 2008 and the Court issued its Markman ruling on December 5, 2008. Trial is scheduled for April 6, 2009.

Saito Shigeru Kenchiku Kenkyusho (Shigeru Saito Architecture Institute) v. iPod; Apple Japan Inc. v. Shigeru Saito Architecture Institute

Plaintiff Saito filed a petition in the Japan Customs Office in Tokyo on January 23, 2007 alleging infringement by the Company of Japanese Patent No. 3852854, entitled "Touch Operation Input Device and Electronic Parts Thereof." The petition sought an order barring the importation into Japan of fifth generation iPods and second generation iPod nanos. The Customs Office held a hearing on March 22, 2007. The Customs Office rejected the petition to bar importation and dismissed plaintiff's case.

Apple Japan, Inc. filed a Declaratory Judgment action against Saito on February 6, 2007 in the Tokyo District Court, seeking a declaration that the '854 patent is invalid and not infringed. Saito filed a Counter Complaint for infringement seeking damages.

St-Germain v. Apple Canada, Inc.

Plaintiff filed this case in Montreal, Quebec, Canada, on August 5, 2005, seeking authorization to institute a class action for the refund by the Company of the Canadian Private Copying Levy that was applied to the iPod purchase price in Quebec between December 12, 2003 and December 14, 2004 but later declared invalid by the Canadian Court. The Company has completed a refund program for this levy. A class certification hearing took place January 13, 2006. On February 24, 2006, the Court granted class certification and notice was published during the last week of March 2006. The trial was conducted on October 15 and 16, 2007. On January 11, 2008, the Court issued a ruling in plaintiff's favor. The Court ruled that despite the Company's good faith efforts with the levy refund program, the Company must pay the amount claimed, and that the class is comprised of 20,000 persons who purchased an iPod in

Quebec between December 12, 2003 and December 14, 2004. The Court ordered the Company to submit a statement of account showing the amount received by the Canadian Private Copying Collective, and the amount that has already been paid to class members in Quebec under the Company's levy refund program. The Court also ordered the parties to submit further briefing regarding the collective recovery award by February 23, 2008. On February 11, 2008, the Company filed an appeal. The Company's appeal is pending.

Texas MP3 Technologies Ltd v. Apple Inc. et al.

Plaintiff filed this action against the Company and other defendants on February 16, 2007 in the United States District Court for the Eastern District of Texas, Marshall Division, alleging infringement of U.S. Patent No. 7,065,417 entitled "MPEG Portable Sound Reproducing System and A Reproducing Method Thereof." The complaint seeks unspecified damages and other relief. On July 12, 2007, the Company filed a petition for reexamination of the patent, which the U.S. Patent and Trademark Office granted. Plaintiff filed an amended complaint on August 1, 2007, adding the iPhone as an accused device. On August 2, 2007, the Company filed a motion to stay the litigation pending the outcome of the reexamination, which the Court denied. The Company filed an answer on August 20, 2007, denying all material allegations and asserting numerous affirmative defenses. The Company also asserted counterclaims for declaratory judgment of non-infringement and invalidity. The Markman hearing is set for March 12, 2009, and trial is scheduled for July 6, 2009.

The Apple iPod iTunes Antitrust Litigation (formerly Charoensak v. Apple Computer, Inc. and Tucker v. Apple Computer, Inc.); Somers v. Apple Inc.

The first-listed action is a consolidated case combining two cases previously pending under the names *Charoensak v. Apple Computer Inc. (formerly Slattery v. Apple Computer Inc.)* and *Tucker v. Apple Computer, Inc*. The original plaintiff (Slattery) in the Charoensak case filed a purported class action on January 3, 2005 in the United States District Court for the Northern District of California alleging various claims including alleged unlawful tying of music purchased on the iTunes Store with the purchase of iPods and unlawful acquisition or maintenance of monopoly market power. Plaintiff's complaint alleged violations of §§1 and 2 of the Sherman Act (15 U.S.C. §§1 and 2), California Business & Professions Code §16700 et seq. (the Cartwright Act), California Business & Professions Code §17200 (unfair competition), common law unjust enrichment and common law monopolization. Plaintiff sought unspecified damages and other relief. The Company filed a motion to dismiss on February 10, 2005. On September 9, 2005, the Court denied the motion in part and granted it in part. Plaintiff filed an amended complaint on September 23, 2005 and the Company filed an answer on October 18, 2005. In August 2006, the Court dismissed Slattery without prejudice and allowed plaintiffs to file an amended complaint naming two new plaintiffs (Charoensak and Rosen). On November 2, 2006, the Company filed an answer to the amended complaint denying all material allegations and asserting numerous affirmative defenses.

The Tucker case was filed as a purported class action on July 21, 2006 in the United States District Court for the Northern District of California alleging various claims including alleged unlawful tying of music and videos purchased on the iTunes Store with the purchase of iPods and vice versa and unlawful acquisition or maintenance of monopoly market power. The complaint alleges violations of §§1 and 2 of the Sherman Act (15 U.S.C. §§1 and 2), California Business & Professions Code §16700 et seq. (the Cartwright Act), California Business & Professions Code §17200 (unfair competition) and the California Consumer Legal Remedies Act. Plaintiff sought unspecified damages and other relief. On November 3, 2006, the Company filed a motion to dismiss the complaint. On December 20, 2006, the Court denied the motion to dismiss. On January 11, 2007, the Company filed an answer denying all material allegations and asserting numerous defenses.

On March 20, 2007, the Court consolidated the two cases. Plaintiffs filed a consolidated complaint on April 19, 2007. On June 6, 2007, the Company filed an answer to the consolidated complaint denying all material allegations and asserting numerous affirmative defenses. On July 17, 2008, plaintiffs filed a motion for class certification and on October 17, 2008, the Company filed its opposition to plaintiffs' motion. The class certification hearing took place on December 16, 2008. On December 22, 2008, the Court granted certification of the monopolization claims and denied without prejudice certification of the tying claims pending reconsideration of its denial of the Company's motion to dismiss.

A related class action complaint, *Somers v. Apple Inc.*, was filed on December 31, 2007 in the United States District Court for the Northern District of California, alleging various claims including alleged unlawful tying of music and videos purchased on the iTunes Store with the purchase of iPods and vice versa and unlawful acquisition or maintenance of monopoly market power. The complaint alleges violations of §§1 and 2 of the Sherman Act (15

U.S.C. §§1 and 2), California Business & Professions Code §16700 et seq. (the Cartwright Act), California Business & Professions Code §17200 (unfair competition) and the California Consumer Legal Remedies Act. Plaintiff seeks unspecified damages and other relief. On February 21, 2008, the Company filed an answer denying all material allegations and asserting numerous defenses. The Court has scheduled the class certification hearing for June 1, 2009.

Tse v. Apple Computer, Inc. et al.

Plaintiff Ho Keung Tse filed this action against the Company and other defendants on August 5, 2005 in the United States District Court for the District of Maryland alleging infringement of U.S. Patent No. 6,665,797 entitled "Protection of Software Again [sic] Against Unauthorized Use." The complaint seeks unspecified damages and other relief. The Company filed an answer on October 31, 2005 denying all material allegations and asserting numerous affirmative defenses. On October 28, 2005, the Company and the other defendants filed a motion to transfer the case to the Northern District of California, which was granted on August 31, 2006. On July 24, 2007, the Company filed a petition for reexamination of the patent, which the U.S. Patent and Trademark Office granted. On July 25, 2007, the Company filed a motion to stay the litigation pending the outcome of the reexamination, which the Court granted on October 4, 2007.

Union Fédérale des Consummateurs - Que Choisir v. Apple Computer France S.à.r.l. and iTunes S.à.r.l.

Plaintiff, a consumer association in France, filed this complaint on February 9, 2005 alleging that the above-listed entities are violating consumer law by (1) omitting to mention that the iPod is allegedly not compatible with music from online music services other than the iTunes Store and that the music from the iTunes Store is only compatible with the iPod and (2) allegedly tying the sales of iPods to the iTunes Store and vice versa. Plaintiff seeks damages, injunctive relief and other relief. The first hearing on the case took place on May 24, 2005. The Company's response to the complaint was served on November 8, 2005. Plaintiff's responsive pleading was filed on February 10, 2006. The Company filed a reply on June 6, 2006 and UFC filed a response on September 19, 2006.

Vitt v. Apple Computer, Inc.

Plaintiff filed this purported class action on November 7, 2006 in the United States District Court for the Central District of California on behalf of a purported nationwide class of all purchasers of the iBook G4 alleging that the computer's logic board fails at an abnormally high rate. The complaint alleges violations of California Business & Professions Code §17200 (unfair competition) and California Business & Professions Code §17500 (false advertising). Plaintiff seeks unspecified damages and other relief. The Company filed a motion to dismiss on January 19, 2007, which the Court granted on March 13, 2007. Plaintiffs filed an amended complaint on March 26, 2007. The Company filed a motion to dismiss on August 16, 2007, which was heard on October 4, 2007. The Court has not yet issued a ruling.

Vogel v. Jobs et al. (2006 Action)

Plaintiffs filed this purported class action on August 24, 2006, in the United States District Court for the Northern District of California against the Company and certain of the Company's current and former officers and directors alleging improper backdating of stock option grants to maximize certain defendants' profits, failing to properly account for those grants and issuing false financial statements. On January 19, 2007, the Court appointed the New York City Employees' Retirement System as lead plaintiff. On March 23, 2007, plaintiffs filed a Consolidated Class Action Complaint. The Consolidated Complaint purports to be brought on behalf of several classes of holders of the Company's stock and asserts claims under Section 14(a) and 20(a) of the Securities Exchange Act as well as state law. The Consolidated Complaint seeks rescission of amendments to various stock option and other incentive compensation plans, an accounting and damages in an unspecified amount. Defendants filed a motion to dismiss on June 8, 2007, which was heard on September 7, 2007. On November 14, 2007, the Court issued an order dismissing all securities claims with prejudice, and held that any amended complaint could only be styled as a derivative case. On December 14, 2007, plaintiff filed a motion for leave to file a first amended consolidated class action complaint. On January 23, 2008, defendants filed an opposition to plaintiff's motion. Plaintiff's motion was heard on March 21, 2008. On May 14, 2008, the Court issued an order denying plaintiffs' motion for leave to amend. The court entered judgment dismissing the case on June 12, 2008. On June 17, 2008, plaintiffs filed a notice of appeal. Plaintiffs' appeal is pending.

Vogel v. Apple Inc., et al. (2008 Action)

Plaintiff filed this purported class action on June 27, 2008, in the United States District Court for the Northern District of California against the Company and certain of the Company's current and former officers and directors.

The allegations, which arise out of the Company's past stock option practices, are similar to those in the 2006 *Vogel v. Jobs et al.* action that was dismissed on June 12, 2008, as described above. The complaint purports to be brought on behalf of several classes of holders of the Company's stock and asserts claims under Sections 10(b) and 20(a) of the Securities Exchange Act. The complaint seeks rescission of amendments to various stock option and other incentive compensation plans, an accounting and damages in an unspecified amount. On July 22, 2008, the Court stayed this case pending the appeal in the 2006 Action.

Item 1A. Risk Factors

Because of the following factors, as well as other factors affecting the Company's financial condition and operating results, past financial performance should not be considered to be a reliable indicator of future performance, and investors should not use historical trends to anticipate results or trends in future periods.

Economic conditions could materially adversely affect the Company.

The Company's operations and performance depend significantly on worldwide economic conditions. Uncertainty about current global economic conditions poses a risk as consumers and businesses may postpone spending in response to tighter credit, negative financial news and/or declines in income or asset values, which could have a material negative effect on demand for the Company's products and services. Demand also could differ materially from the Company's expectations since the Company generally raises prices on goods and services sold outside the U.S. to offset the effect of the strengthening of the U.S. dollar, a trend that has been very pronounced recently. Other factors that could influence demand include continuing increases in fuel and other energy costs, conditions in the residential real estate and mortgage markets, labor and healthcare costs, access to credit, consumer confidence, and other macroeconomic factors affecting consumer spending behavior. These and other economic factors could have a material adverse effect on demand for the Company's products and services and on the Company's financial condition and operating results.

The current financial turmoil affecting the banking system and financial markets and the possibility additional financial institutions may consolidate or go out of business have resulted in a tightening in the credit markets, a low level of liquidity in many financial markets, and extreme volatility in fixed income, credit, currency, and equity markets. There could be a number of follow-on effects from the credit crisis on the Company's business, including the insolvency of key suppliers or their inability to obtain credit to finance development and/or manufacture products resulting in product delays; inability of customers, including channel partners, to obtain credit to finance purchases of the Company's products and/or customer, including channel partner, insolvencies; and failure of derivative counterparties and other financial institutions negatively impacting the Company's treasury operations. Other income and expense also could vary materially from expectations depending on gains or losses realized on the sale or exchange of financial instruments; impairment charges resulting from revaluations of debt and equity securities and other investments; interest rates; cash balances; and changes in fair value of derivative instruments. The current volatility in the financial markets and overall economic uncertainty increase the risk the actual amounts realized in the future on the Company's financial instruments could differ significantly from the fair values currently assigned to them.

Uncertainty about current global economic conditions could also continue to increase the volatility of the Company's stock price.

The matters relating to the Company's past stock option practices and the restatement of the Company's consolidated financial statements may result in additional litigation.

The findings from the Company's investigation into its past stock option granting practices and the resulting restatement of prior financial statements in the Company's Annual Report on Form 10-K for the fiscal year September 30, 2006 (the "2006 Form 10-K") have exposed the Company to greater risks associated with litigation, regulatory proceedings and government enforcement actions. As described in Part II, Item 1, "Legal Proceedings," several derivative and class action complaints have been filed in state and federal courts against the Company and certain current and former directors and executive officers pertaining to allegations relating to past stock option grants. The Company has provided the results of its investigation to the Securities and Exchange Commission (the "SEC") and the United States Attorney's Office for the Northern District of California, and the Company has responded to their requests for documents and additional information. The Company intends to continue to provide its full cooperation.

On April 24, 2007, the SEC filed an enforcement action against two former officers of the Company. In announcing the lawsuit, the SEC stated that it would not bring an enforcement action against the Company based in part on the Company's "swift, extensive, and extraordinary cooperation in the Commission's investigation." According to the SEC's statement, the Company's "cooperation consisted of, among other things, prompt self-reporting, an independent internal investigation, the sharing of the results of that investigation with the government, and the implementation of new controls designed to prevent the recurrence of fraudulent conduct." The enforcement actions against each of these former officers have now been settled.

No assurance can be given regarding the outcomes from litigation relating to the Company's past stock option practices. These and related matters have required, and will continue to require, the Company to incur substantial expenses for legal, accounting, tax, and other professional services, and may divert management's attention from the Company's business. If the Company is subject to adverse findings, it could be required to pay damages and penalties and might face additional remedies that could harm its financial condition and operating results.

Global markets for personal computers, digital music devices, mobile communication devices, and related peripherals and services are highly competitive and subject to rapid technological change. If the Company is unable to compete effectively in these markets, its financial condition and operating results could be materially adversely affected.

The Company competes in global markets that are highly competitive and characterized by aggressive price cutting, with resulting downward pressure on gross margins, frequent introduction of new products, short product life cycles, evolving industry standards, continual improvement in product price/performance characteristics, rapid adoption of technological and product advancements by competitors, and price sensitivity on the part of consumers.

The Company's ability to compete successfully depends heavily on its ability to ensure a continuing and timely introduction of innovative new products and technologies to the marketplace. The Company believes it is unique in that it designs and develops nearly the entire solution for its personal computers, consumer electronics, and mobile communication devices, including the hardware, operating system, numerous software applications, and related services. As a result, the Company must make significant investments in research and development and as such, the Company currently holds a significant number of patents and copyrights and has registered and/or has applied to register numerous patents, trademarks and service marks. By contrast, many of the Company's competitors seek to compete primarily through aggressive pricing and very low cost structures. If the Company is unable to continue to develop and sell innovative new products with attractive margins or if other companies infringe on the Company's intellectual property, the Company's ability to maintain a competitive advantage could be negatively affected and its financial condition and operating results could be materially adversely affected.

In the market for personal computers and peripherals, the Company faces a significant number of competitors, many of which have broader product lines, lower priced products, and larger installed customer bases. Consolidation in this market has resulted in larger and potentially stronger competitors. Price competition has been particularly intense as competitors selling Windows-based personal computers have aggressively cut prices and lowered product margins. The Company also faces increased competition in key market segments, including consumer, SMB, education, enterprise, government, and creative markets. An increasing number of Internet devices that include software applications and are smaller and simpler than traditional personal computers compete for market share with the Company's existing products.

The Company is currently the only authorized maker of hardware using the Mac OS. The Mac OS has a minority market share in the personal computer market, which is dominated by makers of computers using competing operating systems, most notably Windows. The Company's financial condition and operating results depend substantially on the Company's ability to continually improve the Mac platform to maintain functional and design advantages. Use of unauthorized copies of the Mac OS on other companies' hardware products may result in decreased demand for the Company's hardware products, and could materially adversely affect the Company's financial condition and operating results.

The Company is currently focused on certain mobile communication devices, such as iPhone, consumer electronic devices, including the iPod family of digital music players, and digital content distribution. The Company faces substantial competition from companies that have significant technical, marketing, distribution, and other resources, as well as established hardware, software, and digital content supplier relationships. The Company also competes with illegitimate ways to obtain digital content. The Company has only recently entered the mobile communications market, and many of its competitors in the mobile communications market have significantly greater experience, product breadth, and distribution channels than the Company. Because some current and potential competitors have substantial resources and experience and a lower cost structure, they may be able to provide such products and services at little or no profit or even at a loss. The Company also expects competition to intensify as competitors attempt to imitate the Company's approach to providing these components seamlessly within their individual offerings or work collaboratively to offer integrated solutions.

The Company currently receives subsidies from its exclusive and non-exclusive carriers providing cellular network service for iPhone. There is no assurance that such subsidies will be continued at all or in the same amounts upon renewal of the Company's agreements with these carriers or in agreements the Company enters into with new carriers.

There can be no assurance the Company will be able to continue to provide products and services that compete effectively.

To remain competitive and stimulate customer demand, the Company must successfully manage frequent product introductions and transitions.

Due to the highly volatile and competitive nature of the personal computer, consumer electronics and mobile communication industries, the Company must continually introduce new products, services and technologies, enhance existing products and services, and effectively stimulate customer demand for new and upgraded products. The success of new product introductions depends on a number of factors, including timely and successful product development, market acceptance, the Company's ability to manage the risks associated with new products and production ramp issues, the availability of application software for new products, the effective management of purchase commitments and inventory levels in line with anticipated product demand, the availability of products in appropriate quantities and costs to meet anticipated demand, and the risk that new products may have quality or other defects in the early stages of introduction. Accordingly, the Company cannot determine in advance the ultimate effect of new product introductions and transitions on its financial condition and operating results.

The Company faces substantial inventory and other asset risk.

The Company records a write-down for product and component inventories that have become obsolete or exceed anticipated demand or net realizable value and accrues necessary cancellation fee reserves for orders of excess products and components. The Company also reviews its long-lived assets for impairment whenever events or changed circumstances indicate the carrying amount of an asset may not be recoverable. If the Company determines that impairment has occurred, it records a write-down equal to the amount by which the carrying value of the assets exceeds its fair market value. Although the Company believes its inventory, asset, and related provisions are currently adequate, no assurance can be given that, given the rapid and unpredictable pace of product obsolescence in the global personal computer, consumer electronics, and mobile communication industries, the Company will not incur additional inventory or asset related charges. Such charges have had, and could have, a material adverse effect on the Company's financial condition and operating results.

The Company must order components for its products and build inventory in advance of product announcements and shipments. Consistent with industry practice, components are normally acquired through a combination of purchase orders, supplier contracts, and open orders based on projected demand. Such purchase commitments typically cover forecasted component and manufacturing requirements for 30 to 150 days. Because the Company's markets are volatile, competitive and subject to rapid technology and price changes, there is a risk the Company will forecast incorrectly and order or produce excess or insufficient inventories of components or products. The Company's financial condition and operating results have been in the past and could be in the future materially adversely affected by the Company's ability to manage its inventory levels and respond to short-term shifts in customer demand patterns.

Future operating results depend upon the Company's ability to obtain key components including, but not limited to microprocessors, NAND flash memory, DRAM and LCDs at favorable prices and in sufficient quantities.

Because the Company currently obtains certain key components including, but not limited to microprocessors, enclosures, certain LCDs, certain optical drives, and ASICs, from single or limited sources, the Company is subject to significant supply and pricing risks. Many of these and other key components that are available from multiple sources including, but not limited to NAND flash memory, DRAM and certain LCDs, are subject at times to industry-wide shortages and significant commodity pricing fluctuations. The Company has entered into certain agreements for the supply of key components including, but not limited to microprocessors, NAND flash memory, DRAM and LCDs at favorable pricing, but there is no guarantee that the Company will be able to extend or renew these agreements on similar favorable terms, or at all, upon expiration or otherwise obtain favorable pricing in the future. Therefore, the Company remains subject to significant risks of supply shortages and/or price increases that can have a material adverse effect on its financial condition and operating results. The Company expects to experience decreases in its gross margin percentage in future periods, as compared to levels achieved during 2008 and 2007, due largely to the anticipated impact of product transitions, flat or reduced pricing on new and innovative products that have higher cost structures, both expected and potential future cost increases for key components, and higher logistical costs. For additional information refer to Part I, Item 2, "Management's Discussion and Analysis of Financial Condition and Results of Operations," under the subheading "Gross Margin," which is incorporated herein by reference.

The Company and other participants in the personal computer, consumer electronics and mobile communication industries compete for various components with other industries that have experienced increased demand for their products. The Company uses some custom components that are not common to the rest of the personal computer, consumer electronics or mobile communication industries. The Company's new products often utilize custom components available from only one source until the Company has evaluated whether there is a need for, and subsequently qualifies, additional suppliers. When a component or product uses new technologies, initial capacity constraints may exist until the suppliers' yields have matured. Continued availability of these components at acceptable prices, or at all, may be affected if those suppliers decided to concentrate on the production of common components instead of components customized to meet the Company's requirements. If the supply of a key single-sourced component for a new or existing product were delayed or constrained, if such components were available only at significantly higher prices, or if a key manufacturing vendor delayed shipments of completed products to the Company, the Company's financial condition and operating results could be materially adversely affected.

The Company depends on component and product manufacturing and logistical services provided by third parties, many of whom are located outside of the U.S.

Most of the Company's components and products are manufactured in whole or in part by a few third-party manufacturers. Many of these manufacturers are located outside of the U.S., and are geographically concentrated in single locations. The Company has also outsourced much of its transportation and logistics management. While these arrangements may lower operating costs, they also reduce the Company's direct control over production and distribution. It is uncertain what effect such diminished control will have on the quality or quantity of products or services, or the Company's flexibility to respond to changing conditions. In addition, the Company relies on third-party manufacturers to adhere to the Company's supplier code of conduct. Although arrangements with such manufacturers may contain provisions for warranty expense reimbursement, the Company may remain responsible to the consumer for warranty service in the event of product defects. Any unanticipated product defect or warranty liability, whether pursuant to arrangements with contract manufacturers or otherwise, could have a material adverse effect on the Company's reputation, financial condition and operating results.

Final assembly of the Company's products is currently performed in the Company's manufacturing facility in Ireland, and by external vendors in California, Korea, China and the Czech Republic. Currently, the supply and manufacture of many critical components is performed by sole-sourced third-party vendors in the U.S., China, Japan, Korea, Malaysia, Philippines, Taiwan, Thailand and Singapore. Sole-sourced third-party vendors in China perform final assembly of substantially all of the Company's portable products, including MacBook Pro, MacBook, MacBook Air, iPods, iPhones and most of the Company's iMacs. If manufacturing or logistics in these locations is disrupted for any reason, including natural disasters, information technology system failures, military actions or economic, business, labor, environmental, public health, or political issues, the Company's financial condition and operating results could be materially adversely affected.

The Company relies on third-party digital content, which may not be available to the Company on commercially reasonable terms or at all.

The Company contracts with certain third parties to offer their digital content through the Company's iTunes Store. The Company pays substantial fees to obtain the rights to audio and video content. The Company's licensing arrangements with these third parties are short-term and do not guarantee the continuation or renewal of these arrangements on reasonable terms, if at all. Some third-party content providers currently or in the future may offer competing products and services, and could take action to make it more difficult or impossible for the Company to license their content in the future. Other content owners, providers or distributors may seek to limit the Company's access to, or increase the total cost of, such content. If the Company is unable to continue to offer a wide variety of content at reasonable prices with acceptable usage rules, or continue to expand its geographic reach, the Company's financial condition and operating results may be materially adversely affected.

Many third-party content providers require that the Company provide certain digital rights management ("DRM") and other security solutions. If these requirements change, the Company may have to develop or license new technology to provide these solutions. There is no assurance the Company will be able to develop or license such solutions at a reasonable cost and in a timely manner. In addition, certain countries have passed or may propose legislation that would force the Company to license its DRM, which could lessen the protection of content and subject it to piracy and also could affect arrangements with the Company's content providers.

The Company relies on access to third-party patents and intellectual property, and the Company's future results could be materially adversely affected if it is alleged or found to have infringed intellectual property rights.

Many of the Company's products are designed to include third-party intellectual property, and in the future the Company may need to seek or renew licenses relating to various aspects of its products and business methods. Although the Company believes that, based on past experience and industry practice, such licenses generally could be obtained on reasonable terms, there is no assurance that the necessary licenses would be available on acceptable terms or at all.

Because of technological changes in the global personal computer, consumer electronics and mobile communication industries, current extensive patent coverage, and the rapid issuance of new patents, it is possible that certain components of the Company's products and business methods may unknowingly infringe the patents or other intellectual property rights of third parties. From time to time, the Company has been notified that it may be infringing such rights. Regardless of merit, responding to such claims can consume significant time and expense. At present, the Company is vigorously defending more than 26 patent infringement cases, eight of which were filed during fiscal 2009, and several pending claims are in various stages of evaluation. In certain cases, the Company may consider the desirability of entering into licensing agreements, although no assurance can be given that such licenses can be obtained on acceptable terms or that litigation will not occur. If the Company is found to be infringing such rights, it may be required to pay substantial damages. If there is a temporary or permanent injunction prohibiting the Company from marketing or selling certain products or a successful claim of infringement against the Company requires it to pay royalties to a third party, the Company's financial condition and operating results could be materially adversely affected, regardless of whether it can develop non-infringing technology. While in management's opinion the Company does not have a potential liability for damages or royalties from any known current legal proceedings or claims related to the infringement of patent or other intellectual property rights that would individually or in the aggregate have a material adverse effect on its financial condition and operating results, the results of such legal proceedings cannot be predicted with certainty. Should the Company fail to prevail in any of the matters related to infringement of patent or other intellectual property rights of others or should several of these matters be resolved against the Company in the same reporting period, the Company's financial condition and operating results could be materially adversely affected.

With the June 2007 introduction of iPhone, the Company has begun to compete with mobile communication device companies that hold significant patent portfolios. Regardless of the scope or validity of such patents or the merits of any potential patent claims by competitors, the Company may have to engage in protracted litigation, enter into expensive agreements or settlements and/or modify its products. Any of these events could have a material adverse impact on the Company's financial condition and operating results.

The Company's future performance depends on support from third-party software developers. If third-party software applications and services cease to be developed and maintained for the Company's products, customers may choose not to buy the Company's products.

The Company believes decisions by customers to purchase its hardware products, including its Macs, iPods and iPhones, are often based to a certain extent on the availability of third-party software applications and services. There is no assurance that third-party developers will continue to develop and maintain applications and services for the Company's products on a timely basis or at all, and discontinuance or delay of these applications and services could have a material adverse effect on the Company's financial condition and operating results.

With respect to its Mac products, the Company believes the availability of third-party software applications and services depends in part on the developers' perception and analysis of the relative benefits of developing, maintaining, and upgrading such software for the Company's products compared to Windows-based products. This analysis may be based on factors such as the perceived strength of the Company and its products, the anticipated revenue that may be generated, continued acceptance by customers of Mac OS X, and the costs of developing such applications and services. If the Company's minority share of the global personal computer market causes developers to question the Company's prospects, developers could be less inclined to develop or upgrade software for the Company's products and more inclined to devote their resources to developing and upgrading software for the larger Windows market. The Company's development of its own software applications and services may also negatively affect the decisions of third-party developers, such as Microsoft, Adobe, and Google, to develop, maintain, and upgrade similar or competitive software and services for the Company's products. Mac OS X Leopard, which became available in October 2007, includes a new feature that enables Intel-based Mac systems to run Microsoft Windows XP and Windows Vista operating systems. This feature may deter developers from creating software applications for Mac OS X if such applications are already available for the Windows platform.

With respect to iPhone and iPod touch, the Company relies on the continued availability and development of compelling and innovative software applications. Unlike third-party software applications for Mac products, the software applications for the iPhone and iPod touch platforms are distributed through a single distribution channel, the iTunes Store. The absence of multiple distribution channels, which are available for competing platforms, may limit the availability and acceptance of third-party applications by the Company's customers, thereby causing developers to curtail significantly, or stop, development for the Company's platforms. In addition, iPhone and iPod touch are subject to rapid technological change, and, if third-party developers are unable to keep up with this pace of change, third-party applications might not successfully operate and may result in dissatisfied customers. Further, if the Company develops its own software applications and services, such development may negatively affect the decisions of third-party developers to develop, maintain, and upgrade similar or competitive applications for the iPhone and iPod touch platforms. As with applications for the Company's Mac products, the availability and development of these applications also depend on developers' perceptions and analysis of the relative benefits of developing software for the Company's products rather than its competitors' products, including devices that use competing platforms. If developers focus their efforts on these competing platforms, the availability and quality of applications for the Company's devices may suffer.

The Company's products and services experience quality problems from time to time that can result in decreased sales and operating margin.

The Company sells highly complex hardware and software products and services that can contain defects in design and manufacture. Sophisticated operating system software and applications, such as those sold by the Company, often contain "bugs" that can unexpectedly interfere with the software's intended operation. Defects may also occur in components and products the Company purchases from third parties. There can be no assurance the Company will be able to detect and fix all defects in the hardware, software and services it sells. Failure to do so could result in lost revenue, harm to reputation, and significant warranty and other expenses, and could have a material adverse impact on the Company's financial condition and operating results.

The Company expects its quarterly revenue and operating results to fluctuate for a variety of reasons.

The Company's profit margins vary among its products and its distribution channels. The Company's software, accessories, and service and support contracts generally have higher gross margins than certain of the Company's other products. Gross margins on the Company's hardware products vary across product lines and can change over time as a result of product transitions, pricing and configuration changes, and component, warranty, and other cost fluctuations. The Company's direct sales generally have higher associated gross margins than its indirect sales through its channel partners. In addition, the Company's gross margin and operating margin percentages, as well as overall profitability, may be materially adversely impacted as a result of a shift in product, geographic or channel mix, new products, component cost increases, or price competition. The Company has typically experienced greater net sales in the first and fourth fiscal quarters compared to the second and third fiscal quarters due to seasonal demand related to the holiday season and the beginning of the school year, respectively. Furthermore, the Company sells more products from time-to-time during the third month of a quarter than it does during either of the first two months. Developments late in a quarter, such as lower-than-anticipated demand for the Company's products, an internal systems failure, or failure of one of the Company's key logistics, components supply, or manufacturing partners, could have a material adverse impact on the Company's financial condition and operating results.

In certain countries, including the U.S., the Company relies on a single cellular network carrier to provide service for iPhone.

In each of the U.S., U.K., Germany, Spain, Ireland, and certain other countries, the Company has contracted with a single carrier to provide cellular network services for iPhone on an exclusive basis. If these exclusive carriers cannot successfully compete with other carriers in their markets on any basis, including but not limited to the quality and coverage of wireless voice and data services, performance and timely build-out of advanced wireless networks, and pricing and other terms of conditions of end-user contracts, or if these exclusive carriers fail to promote iPhone aggressively or favor other handsets in their promotion and sales activities or service plans, sales may be materially adversely affected.

The Company is subject to risks associated with laws, regulations and industry-imposed standards related to mobile communications devices.

Laws and regulations related to mobile communications devices in the many jurisdictions in which the Company operates are extensive and subject to change. Such changes, which could include but are not limited to restrictions on production, manufacture, distribution, and use of the device, locking the device to a carrier's network, or mandating the use of the device on more than one carrier's network, could have a material adverse effect on the Company's financial condition and operating results.

Mobile communication devices, such as iPhone, are subject to certification and regulation by governmental and standardization bodies, as well as by cellular network carriers for use on their networks. These certification processes are extensive and time consuming, and could result in additional testing requirements, product modifications or delays in product shipment dates, which could have a material adverse effect on the Company's financial condition and operating results.

The Company may be subject to information technology system failures, network disruptions and breaches in data security.

Information technology system failures, network disruptions and breaches of data security could disrupt the Company's operations by causing delays or cancellation of customer, including channel partner, orders, negatively affecting the Company's online offerings and services, impeding the manufacture or shipment of products, processing transactions and reporting financial results, resulting in the unintentional disclosure of customer or Company information, or damage to the Company's reputation. While management has taken steps to address these concerns by implementing sophisticated network security and internal control measures, there can be no assurance that a system failure or data security breach will not have a material adverse effect on the Company's financial condition and operating results.

The Company's stock price continues to be volatile.

The Company's stock has at times experienced substantial price volatility as a result of variations between its actual and anticipated financial results, announcements by the Company and its competitors, or uncertainty about current global economic conditions. The stock market as a whole also has experienced extreme price and volume fluctuations that have affected the market price of many technology companies in ways that may have been unrelated to these companies' operating performance. Furthermore, the Company believes its stock price reflects high future growth and profitability expectations. If the Company fails to meet these expectations its stock price may significantly decline.

Political events, war, terrorism, public health issues, natural disasters and other circumstances could materially adversely affect the Company.

War, terrorism, geopolitical uncertainties, public health issues, and other business interruptions have caused and could cause damage or disruption to international commerce and the global economy, and thus could have a strong negative effect on the Company, its suppliers, logistics providers, manufacturing vendors and customers, including channel partners. The Company's business operations are subject to interruption by natural disasters, fire, power shortages, terrorist attacks, and other hostile acts, labor disputes, public health issues, and other events beyond its control. Such events could decrease demand for the Company's products, make it difficult or impossible for the Company to make and deliver products to its customers, including channel partners, or to receive components from its suppliers, and create delays and inefficiencies in the Company's supply chain. Should major public health issues, including pandemics, arise, the Company could be negatively affected by more stringent employee travel restrictions, additional limitations in freight services, governmental actions limiting the movement of products between regions, delays in production ramps of new products, and disruptions in the operations of the Company's manufacturing vendors and component suppliers. The majority of the Company's research and development activities, its corporate headquarters, information technology systems, and other critical business operations, including certain component suppliers and manufacturing vendors, are located near major seismic faults. Because the Company does not carry earthquake insurance for direct quake-related losses and significant recovery time could be required to resume operations, the Company's financial condition and operating results could be materially adversely affected in the event of a major earthquake.

The Company's success depends largely on the continued service and availability of key personnel.

Much of the Company's future success depends on the continued service and availability of skilled personnel, including its CEO, its executive team and key employees in technical, marketing and staff positions. Experienced personnel in the technology industry are in high demand and competition for their talents is intense, especially in the Silicon Valley, where most of the Company's key employees are located. The Company's CEO has taken a medical leave of absence until the end of June and plans to remain involved in major strategic decisions during his leave. There can be no assurance that the Company will continue to successfully retain key personnel.

Market and regulatory developments may limit the Company's ability to use equity compensation to attract and retain key personnel.

The Company has relied on equity awards as one means for recruiting and retaining this highly skilled talent. Accounting regulations requiring the expensing of stock options have resulted in increased stock-based compensation expense, which has caused the Company to reduce the number of stock-based awards issued to employees and could negatively impact the Company's ability to attract and retain key personnel. Additionally, significant adverse volatility in the Company's stock price could result in a stock option's exercise price exceeding the underlying stock's market value or a significant deterioration in the value of restricted stock units granted, thus lessening the effectiveness of retaining employees through stock-based awards. There can be no assurance that the Company will continue to successfully attract and retain key personnel.

Unfavorable results of legal proceedings could materially adversely affect the Company.

The Company is subject to various legal proceedings and claims that have arisen out of the ordinary conduct of its business and are not yet resolved and additional claims may arise in the future. Results of legal proceedings cannot be predicted with certainty. Regardless of its merit, litigation may be both time-consuming and disruptive to the Company's operations and cause significant expense and diversion of management attention. In recognition of these considerations, the Company may enter into material settlements. Should the Company fail to prevail in certain matters, or should several of these matters be resolved against the Company in the same reporting period, the Company may be faced with significant monetary damages or injunctive relief against it that would materially adversely affect a portion of its business and might materially affect the Company's financial condition and operating results.

The Company's business is subject to the risks of international operations.

The Company derives a large and growing portion of its revenue and earnings from its international operations. As a result, its financial condition and operating results could be significantly affected by risks associated with international activities, including economic and labor conditions, political instability, tax laws (including U.S. taxes on foreign subsidiaries), and changes in the value of the U.S. dollar versus local currencies. Margins on sales of the

Company's products in foreign countries, and on sales of products that include components obtained from foreign suppliers, could be materially adversely affected by foreign currency exchange rate fluctuations and by international trade regulations, including tariffs and antidumping penalties.

The Company's primary exposure to movements in foreign currency exchange rates relate to non-U.S. dollar denominated sales in Europe, Japan, Australia, Canada, and certain parts of Asia, as well as non-U.S. dollar denominated operating expenses incurred throughout the world. Weakening of foreign currencies relative to the U.S. dollar will adversely affect the U.S. dollar value of the Company's foreign currency-denominated sales and earnings, and generally will lead the Company to raise international pricing, potentially reducing demand for the Company's products. In some circumstances, due to competition or other reasons, the Company may decide not to raise local prices to the full extent of the dollar's strengthening, or at all, which would adversely affect the U.S. dollar value of the Company's foreign currency denominated sales and earnings. Conversely, a strengthening of foreign currencies, while generally beneficial to the Company's foreign currency-denominated sales and earnings, could cause the Company to reduce international pricing, thereby limiting the benefit. Additionally, strengthening of foreign currencies may also increase the Company's cost of product components denominated in those currencies, thus adversely affecting gross margins.

The Company has used derivative instruments, such as foreign exchange forward and option positions, to hedge certain exposures to fluctuations in foreign currency exchange rates. The use of such hedging activities may not offset any or more than a portion of the adverse financial effects of unfavorable movements in foreign exchange rates over the limited time the hedges are in place.

The Company's retail business has required and will continue to require a substantial investment and commitment of resources and is subject to numerous risks and uncertainties.

Through December 27, 2008, the Company had opened 251 retail stores. The Company's retail stores have required substantial fixed investment in equipment and leasehold improvements, information systems, inventory, and personnel. The Company also has entered into substantial operating lease commitments for retail space with terms ranging from 5 to 20 years, the majority of which are for 10 years. Certain stores have been designed and built to serve as high-profile venues to promote brand awareness and serve as vehicles for corporate sales and marketing activities. Because of their unique design elements, locations and size, these stores require substantially more investment than the Company's more typical retail stores. Due to the high fixed cost structure associated with the Retail segment, a decline in sales or the closure or poor performance of individual or multiple stores could result in significant lease termination costs, write-offs of equipment and leasehold improvements, and severance costs that could have a material adverse effect on the Company's financial condition and operating results.

Many factors unique to retail operations, some of which are beyond the Company's control, pose risks and uncertainties that could have a material adverse effect on the Retail segment's future results, cause its actual results to differ from anticipated results and have a material adverse effect on the Company's financial condition and operating results. These risks and uncertainties include, among other things, macro-economic factors that could have a negative effect on general retail activity, as well as the Company's inability to manage costs associated with store construction and operation, inability to sell third-party products at adequate margins, failure to manage relationships with existing retail channel partners, more challenging environment in managing retail operations outside the U.S., costs associated with unanticipated fluctuations in the value of retail inventory, and inability to obtain and renew leases in quality retail locations at a reasonable cost.

Investment in new business strategies and initiatives could disrupt the Company's ongoing business and present risks not originally contemplated.

The Company has invested, and in the future may invest, in new business strategies or acquisitions. Such endeavors may involve significant risks and uncertainties, including distraction of management from current operations, insufficient revenue to offset liabilities assumed and expenses associated with the strategy, inadequate return of capital, and unidentified issues not discovered in the Company's due diligence. Because these new ventures are inherently risky, no assurance can be given that such strategies and initiatives will be successful and will not have a material adverse effect on the Company's financial condition and operating results.

The Company's future operating performance depends on the performance of distributors, carriers, and other resellers.

The Company distributes its products through wholesalers, resellers, national and regional retailers, value-added resellers, and cataloguers, many of whom distribute products from competing manufacturers. The Company also sells many of its products and resells third-party products in most of its major markets directly to end-users, certain education customers, and certain resellers through its online and retail stores. iPhone is distributed through the Company, its cellular network carriers' distribution channels, and certain third-party resellers.

Many resellers operate on narrow product margins and have been negatively affected in the past by weak economic conditions. Some resellers have perceived the expansion of the Company's direct sales as conflicting with their business interests as distributors and resellers of the Company's products. Such a perception could discourage resellers from investing resources in the distribution and sale of the Company's products or lead them to limit or cease distribution of those products. The Company's financial condition and operating results could be materially adversely affected if the financial condition of these resellers weakens, if resellers stopped distributing the Company's products, or if uncertainty regarding demand for the Company's products caused resellers to reduce their ordering and marketing of the Company's products. The Company has invested and will continue to invest in programs to enhance reseller sales, including staffing selected resellers' stores with Company employees and contractors and improving product placement displays. These programs could require a substantial investment while providing no assurance of return or incremental revenue.

The Company is exposed to credit risk and fluctuations in the market values of its investment portfolio.

Although the Company has not recognized any material losses on its cash, cash equivalents and marketable securities, future declines in their market values could have a material adverse effect on the Company's financial condition and operating results. Given the global nature of its business, the Company has investments both domestically and internationally. Additionally, the Company's overall investment portfolio is often concentrated in the financial sector, which has been negatively impacted by the recent market liquidity conditions. Credit ratings and pricing of these investments can be negatively impacted by liquidity, credit deterioration or losses, financial results, or other factors. As a result, the value or liquidity of the Company's cash, cash equivalents and marketable securities could decline and result in a material impairment, which could have a material adverse effect on the Company's financial condition and operating results.

The Company is exposed to credit risk on its accounts receivable and prepayments related to long-term supply agreements. This risk is heightened during periods when economic conditions worsen.

A substantial majority of the Company's outstanding trade receivables are not covered by collateral or credit insurance. The Company also has unsecured non-trade receivables resulting from purchases of components by contract manufacturers and other vendors that manufacture sub-assemblies or assemble final products for the Company. In addition, the Company has made prepayments associated with long-term supply agreements to secure supply of certain inventory components. While the Company has procedures to monitor and limit exposure to credit risk on its trade and non-trade receivables as well as long-term prepayments, there can be no assurance such procedures will effectively limit its credit risk and avoid losses, which could have a material adverse effect on the Company's financial condition and operating results.

The Company is subject to risks associated with laws and regulations related to health, safety and environmental protection.

The Company's products and services, and the production and distribution of those goods and services, are subject to a variety of laws and regulations. These may require the Company to offer customers the ability to return a product at the end of its useful life and place responsibility for environmentally safe disposal or recycling with the Company. Such laws and regulations have been passed in several jurisdictions in which the Company operates, including various countries within Europe and Asia, certain Canadian provinces and certain states within the U.S. Although the Company does not anticipate any material adverse effects based on the nature of its operations and the thrust of such laws, there is no assurance such existing laws or future laws will not have a material adverse effect on the Company's financial condition and operating results.

Changes in the Company’s tax rates could affect its future results.

The Company’s future effective tax rates could be affected by changes in the mix of earnings in countries with differing statutory tax rates, changes in the valuation of deferred tax assets and liabilities, or changes in tax laws or their interpretation. The Company is subject to the continuous examination of its income tax returns by the Internal Revenue Service and other tax authorities. The Company regularly assesses the likelihood of adverse outcomes resulting from these examinations to determine the adequacy of its provision for taxes. There can be no assurance that the outcomes from these examinations will not have a material adverse effect on the Company’s financial condition and operating results.

The Company is subject to risks associated with the availability and coverage of insurance.

For certain risks, the Company does not maintain insurance coverage because of cost and/or availability. Because the Company retains some portion of its insurable risks, and in some cases self-insures completely, unforeseen or catastrophic losses in excess of insured limits could have a material adverse effect on the Company’s financial condition and operating results.

Item 2. Unregistered Sales of Equity Securities and Use of Proceeds

None.

Item 3. Defaults Upon Senior Securities

None.

Item 4. Submission of Matters to a Vote of Security Holders

None.

Item 5. Other Information

None.

Item 6. Exhibits

(a) **Index to Exhibits**

Exhibit Number	Exhibit Description	Incorporated by Reference Form	Filing Date/ Period End Date
3.1	Restated Articles of Incorporation, filed with the Secretary of State of the State of California on January 27, 1988.	S-3	7/27/88
3.2	Certificate of Amendment to Restated Articles of Incorporation, filed with the Secretary of State of the State of California on May 4, 2000.	10-Q	5/11/00
3.3	Certificate of Amendment to Restated Articles of Incorporation, as amended, filed with the Secretary of State of the State of California on February 25, 2005.	10-Q	3/26/05
3.4	By-Laws of the Registrant, as amended through August 20, 2008.	8-K	8/25/08
4.1	Form of Stock Certificate of the Registrant.	10-Q	12/30/06
10.1*	Employee Stock Purchase Plan, as amended through May 10, 2007.	8-K	5/16/07
10.2*	Form of Indemnification Agreement between the Registrant and each officer of the Registrant.	10-K	9/26/97
10.3*	1997 Employee Stock Option Plan, as amended through October 19, 2001.	10-K	9/28/02
10.4*	1997 Director Stock Option Plan, as amended through May 10, 2007.	8-K	5/16/07
10.5*	2003 Employee Stock Plan, as amended through May 10, 2007.	8-K	5/16/07
10.6*	Reimbursement Agreement dated as of May 25, 2001 by and between the Registrant and Steven P. Jobs.	10-Q	6/29/02
10.7*	Performance Bonus Plan dated April 21, 2005.	10-Q	3/26/05
10.8*	Form of Option Agreements.	10-K	9/24/05
10.9*	Form of Restricted Stock Unit Award Agreement effective as of August 28, 2007.	10-K	9/29/07
10.10**	Form of Restricted Stock Unit Award Agreement effective as of November 11, 2008.		
10.11**	Transition Agreement and Settlement Agreement and Release dated as of November 3, 2008 by and between the Registrant and Anthony Fadell.		
14.1	Business Conduct Policy of the Registrant dated January 2008.	10-Q	12/29/07
18.1**	Letter Regarding Change in Accounting Principles.		
31.1**	Rule 13a-14(a) / 15d-14(a) Certification of Chief Executive Officer.		
31.2**	Rule 13a-14(a) / 15d-14(a) Certification of Chief Financial Officer.		
32.1***	Section 1350 Certifications of Chief Executive Officer and Chief Financial Officer.		

* Indicates management contract or compensatory plan or arrangement.

** Filed herewith.

*** Furnished herewith.

SIGNATURE

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

January 22, 2009	APPLE INC.
	By: /s/ Peter Oppenheimer Peter Oppenheimer Senior Vice President and Chief Financial Officer

Exhibit 10.10

APPLE INC.
2003 EMPLOYEE STOCK PLAN
RESTRICTED STOCK UNIT AWARD AGREEMENT

NOTICE OF GRANT

Name:	______________________________	(the "Participant")
Employee ID:	______________________________	
Grant Number:	______________________________	
No. of Units Subject to Award:	______________________________	
Award Date:	______________________________	(the "Award Date")
Vesting Commencement Date:	The first day after the Award Date that is the 15th day of a calendar month.	

Vesting Schedule:

This restricted stock unit award (the "Award") is granted under and governed by the terms and conditions of the Apple Inc. 2003 Employee Stock Plan and the Terms and Conditions of Restricted Stock Unit Award, which are attached hereto and incorporated herein by reference.

You do not have to accept the Award. If you wish to decline your Award, you should promptly notify Apple Inc.'s Human Resources Equity Group of your decision in writing at 1 Infinite Loop MS: 84-CO, Cupertino CA 95014. If you do not provide such written notification within thirty (30) days after the Award Date, you will be deemed to have accepted your Award on the terms and conditions set forth herein.

TERMS AND CONDITIONS OF RESTRICTED STOCK UNIT AWARD

1. General. These Terms and Conditions of Restricted Stock Unit Award (these "**Terms**") apply to a particular restricted stock unit award (the "**Award**") granted by Apple Inc., a California corporation (the "**Company**"), and are incorporated by reference in the Notice of Grant (the "**Grant Notice**") corresponding to that particular grant. The recipient of the Award identified in the Grant Notice is referred to as the "**Participant**." The effective date of grant of the Award as set forth in the Grant Notice is referred to as the "**Award Date**." The Award was granted under and is subject to the provisions of the Apple Inc. 2003 Employee Stock Plan (the "**Plan**"). Capitalized terms are defined in the Plan if not defined herein. The Award has been granted to the Participant in addition to, and not in lieu of, any other form of compensation otherwise payable or to be paid to the Participant. The Grant Notice and these Terms are collectively referred to as the "**Award Agreement**" applicable to the Award.

2. Stock Units. As used herein, the term "**Stock Unit**" shall mean a non-voting unit of measurement which is deemed for bookkeeping purposes to be equivalent to one outstanding share of the Company's Common Stock ("**Share**") solely for purposes of the Plan and this Award Agreement. The Stock Units shall be used solely as a device for the determination of the payment to eventually be made to the Participant if such Stock Units vest pursuant to this Award Agreement. The Stock Units shall not be treated as property or as a trust fund of any kind.

3. Vesting. Subject to Section 8 below, the Award shall vest and become nonforfeitable as set forth in the Grant Notice. (Each vesting date set forth in the Grant Notice is referred to herein as a "**Vesting Date**").

4. Continuance of Employment. The vesting schedule requires continued employment or service through each applicable Vesting Date as a condition to the vesting of the applicable installment of the Award and the rights and benefits under this Award Agreement. Employment or service for only a portion of the vesting period, even if a substantial portion, will not entitle the Participant to any proportionate vesting or avoid or mitigate a termination of rights and benefits upon or following a termination of employment or services as provided in Section 8 below or under the Plan.

Nothing contained in this Award Agreement or the Plan constitutes an employment or service commitment by the Company, affects the Participant's status as an employee at will who is subject to termination with or without cause, confers upon the Participant any right to remain employed by or in service to the Company or any Subsidiary, interferes in any way with the right of the Company or any Subsidiary at any time to terminate such employment or services, or affects the right of the Company or any Subsidiary to increase or decrease the Participant's other compensation or benefits. Nothing in this paragraph, however, is intended to adversely affect any independent contractual right of the Participant without his consent thereto.

5. No Shareholder Rights. The Participant shall have no rights as a shareholder of the Company, no dividend rights and no voting rights with respect to the Stock Units or any Shares underlying or issuable in respect of such Stock Units until such Shares are actually issued to and held of record by the Participant. No adjustments will be made for dividends or other rights of a holder for which the record date is prior to the date of issuance of the stock certificate evidencing such Shares.

6. <u>Restrictions on Transfer</u>. Except as provided in Section 4(c) of the Plan, neither the Award, nor any interest therein or amount or Shares payable in respect thereof may be sold, assigned, transferred, pledged or otherwise disposed of, alienated or encumbered, either voluntarily or involuntarily.

7. <u>Timing and Manner of Payment of Stock Units</u>. On or as soon as administratively practical following each Vesting Date of the applicable portion of the total Award pursuant to Section 3 or Section 8 (and in all events not later than two and one-half ($2\,^1/_2$) months after such vesting event), the Company shall deliver to the Participant a number of Shares (either by delivering one or more certificates for such Shares or by entering such Shares in book entry form, as determined by the Company in its discretion) equal to the number of Stock Units subject to this Award that vest on the applicable Vesting Date, less Tax-Related Items (as defined in Section 10 below), unless such Stock Units terminate prior to the given Vesting Date pursuant to Section 8. The Company's obligation to deliver Shares or otherwise make payment with respect to vested Stock Units is subject to the condition precedent that the Participant or other person entitled under the Plan to receive any Shares with respect to the vested Stock Units deliver to the Company any representations or other documents or assurances required pursuant to Section 13(c) of the Plan. The Participant shall have no further rights with respect to any Stock Units that are paid or that terminate pursuant to Section 8.

8. <u>Effect of Termination of Employment</u>. The Participant's Stock Units shall terminate to the extent such units have not become vested prior to the first date the Participant is no longer employed by or providing services to the Company or one of its Subsidiaries (the "**Severance Date**"), regardless of the reason for the termination of the Participant's employment with the Company or a Subsidiary, whether with or without cause, voluntarily or involuntarily; provided, however, that in the event such termination of employment is due to the Participant's death or Disability, (a) the Award shall vest with respect to the number of Stock Units determined by multiplying (i) the number of then-outstanding and unvested Stock Units subject to the Award that would have otherwise vested pursuant to Section 3 on the next Vesting Date following the Severance Date but for such termination of employment, by (ii) a fraction, the numerator of which shall be the number of whole calendar months that have elapsed between the Vesting Date that immediately preceded the Severance Date (or, in the case of a termination prior to the initial Vesting Date, the Vesting Commencement Date) and the Severance Date, and the denominator of which shall be the number of whole calendar months between the Vesting Date that immediately preceded the Severance Date (or, in the case of a termination prior to the initial Vesting Date, the Vesting Commencement Date) and the next Vesting Date following the Severance Date that would have occurred but for such termination of employment; and (b) any Stock Units that are not vested after giving effect to the foregoing clause (a) shall terminate. If any unvested Stock Units are terminated hereunder, such Stock Units shall automatically terminate and be cancelled as of the applicable Severance Date without payment of any consideration by the Company and without any other action by the Participant, or the Participant's beneficiary or personal representative, as the case may be.

9. Adjustments Upon Specified Events. Upon the occurrence of certain events relating to the Company's stock contemplated by Section 11 of the Plan (including, without limitation, an extraordinary cash dividend on such stock), the Committee shall make adjustments in accordance with such section in the number of Stock Units then outstanding and the number and kind of securities that may be issued in respect of the Award.

10. Responsibility for Taxes. Regardless of any action the Company and/or the Participant's employer (the "**Employer**") take with respect to any or all income tax (including U.S. federal, state and local tax and/or non-U.S. tax), social insurance, payroll tax, payment on account or other tax-related items related to the Participant's participation in the Plan and legally applicable to the Participant or deemed by the Company or the Employer to be an appropriate charge to the Participant even if technically due by the Company or the Employer ("**Tax-Related Items**"), the Participant acknowledges that the ultimate liability for all Tax-Related Items is and remains the Participant's responsibility and may exceed the amount actually withheld by the Company or the Employer. The Participant further acknowledges that the Company and/or the Employer (i) make no representations or undertakings regarding the treatment of any Tax-Related Items in connection with any aspect of the Award, including the grant of the Stock Units, the vesting of the Stock Units, the delivery of Shares, the subsequent sale of any Shares acquired at vesting and the receipt of any dividends and/or dividend equivalents; and (ii) do not commit to and are under no obligation to structure the terms of the grant or any aspect of the Award to reduce or eliminate the Participant's liability for Tax-Related Items or achieve any particular tax result. Further, if the Participant is or becomes subject to tax in more than one jurisdiction, the Participant acknowledges that the Company and/or the Employer (or former employer, as applicable) may be required to withhold or account for Tax-Related Items in more than one jurisdiction.

Prior to the relevant taxable or tax withholding event, as applicable, the Participant shall pay or make arrangements satisfactory to the Company and/or the Employer to satisfy all withholding and payment on account obligations of the Company and/or the Employer. In this regard, the Participant authorizes the Company and/or the Employer, at its discretion and pursuant to such procedures as it may specify from time to time, to satisfy withholding and all other obligations with regard to all Tax-Related Items legally payable by the Participant by one or a combination of the following:

(a) withholding from any wages or other cash compensation payable to the Participant by the Company and/or the Employer;

(b) withholding otherwise deliverable Shares to be issued upon vesting/settlement of the Award;

(c) arranging for the sale of Shares otherwise deliverable to the Participant (on the Participant's behalf and at the Participant's direction pursuant to this authorization), including selling shares as part of a block trade with other Participants in the Plan; or

(d) withholding from the proceeds of the sale of Shares acquired upon vesting/settlement of the Award.

To avoid negative accounting treatment, the Company may withhold or account for Tax-Related Items by considering applicable minimum statutory withholding amounts or other applicable withholding rates. If the obligation for Tax-Related Items is satisfied by withholding a number of Shares as described herein, for tax purposes, the Participant is deemed to have been issued the full number of Shares subject to the Award, notwithstanding that a number of the Shares are held back solely for the purpose of paying the Tax-Related Items due as a result of any aspect of the Participant's participation in the Plan. The Participant shall pay to the Company and/or the Employer any amount of Tax-Related Items that the Company and/or the Employer may be required to withhold or account for as a result of the Participant's participation in the Plan that cannot be satisfied by the means previously described. The Company may refuse to deliver to the Participant any Shares pursuant to the Participant's Award if the Participant fails to comply with the Participant's obligations in connection with the Tax-Related Items as described in this Section.

11. Electronic Delivery and Acceptance. The Company may, in its sole discretion, deliver any documents related to the Award by electronic means or request the Participant's consent to participate in the Plan by electronic means. The Participant hereby consents to receive all applicable documentation by electronic delivery and to participate in the Plan through an on-line (and/or voice activated) system established and maintained by the Company or a third party vendor designated by the Company.

12. Data Privacy. The Participant acknowledges and consents to the collection, use, processing and transfer of personal data as described in this Section 12. The Company, its related entities, and the Participant's employer hold certain personal information about the Participant, including the Participant's name, home address and telephone number, date of birth, social security number or other employee identification number, salary, nationality, job title, any Shares or directorships held in the Company, details of all options or any other entitlement to Shares awarded, canceled, purchased, vested, unvested or outstanding in the Participant's favor, for the purpose of managing and administering the Plan ("**Data**"). The Company and its related entities may transfer Data amongst themselves as necessary for the purpose of implementation, administration and management of the Participant's participation in the Plan, and the Company and its related entities may each further transfer Data to any third parties assisting the Company or any such related entity in the implementation, administration and management of the Plan. The Participant acknowledges that the transferors and transferees of such Data may be located anywhere in the world and hereby authorizes each of them to receive, possess, use, retain and transfer the Data, in electronic or other form, for the purposes of implementing, administering and managing the Participant's participation in the Plan, including any transfer of such Data as may be required for the administration of the Plan and/or the subsequent holding of Shares on the Participant's behalf to a broker or to other third party with whom the Participant may elect to deposit any Shares acquired under the Plan (whether pursuant to the Award or otherwise).

13. Notices. Any notice to be given under the terms of this Award Agreement shall be in writing and addressed to the Company at its principal office to the attention of the Secretary, and to the Participant at the Participant's last address reflected on the Company's records, or at such other address as either party may hereafter designate in writing to the other. Any such notice shall be given only when received, but if the Participant is no longer an employee of the Company, shall be deemed to have been duly given by the Company when enclosed in a properly sealed envelope addressed as aforesaid, registered or certified, and deposited (postage and registry or certification fee prepaid) in a post office or branch post office regularly maintained by the United States Government.

14. Plan. The Award and all rights of the Participant under this Award Agreement are subject to the terms and conditions of the provisions of the Plan, incorporated herein by reference. The Participant agrees to be bound by the terms of the Plan and this Award Agreement. The Participant acknowledges having read and understood the Plan, the Prospectus for the Plan, and this Award Agreement. Unless otherwise expressly provided in other sections of this Award Agreement, provisions of the Plan that confer discretionary authority on the Board or the Committee do not (and shall not be deemed to) create any rights in the Participant unless such rights are expressly set forth herein or are otherwise in the sole discretion of the Board or the Committee so conferred by appropriate action of the Board or the Committee under the Plan after the date hereof.

15. Entire Agreement. This Award Agreement and the Plan together constitute the entire agreement and supersede all prior understandings and agreements, written or oral, of the parties hereto with respect to the subject matter hereof. The Plan and this Award Agreement may be amended pursuant to Section 15 of the Plan. Such amendment must be in writing and signed by the Company. The Company may, however, unilaterally waive any provision hereof in writing to the extent such waiver does not adversely affect the interests of the Participant hereunder, but no such waiver shall operate as or be construed to be a subsequent waiver of the same provision or a waiver of any other provision hereof.

16. Limitation on the Participant's Rights. Participation in the Plan confers no rights or interests other than as herein provided. This Award Agreement creates only a contractual obligation on the part of the Company as to amounts payable and shall not be construed as creating a trust. Neither the Plan nor any underlying program, in and of itself, has any assets. The Participant shall have only the rights of a general unsecured creditor of the Company with respect to amounts credited and benefits payable, if any, with respect to the Stock Units, and rights no greater than the right to receive the Common Stock as a general unsecured creditor with respect to Stock Units, as and when payable hereunder.

17. Counterparts. This Award Agreement may be executed simultaneously in any number of counterparts, each of which shall be deemed an original but all of which together shall constitute one and the same instrument.

18. Section Headings. The section headings of this Award Agreement are for convenience of reference only and shall not be deemed to alter or affect any provision hereof.

19. Governing Law and Choice of Venue. This Award Agreement shall be governed by and construed and enforced in accordance with the laws of the State of California without regard to conflict of law principles thereunder.

For purposes of litigating any dispute that arises directly or indirectly from the relationship of the parties evidenced by this grant or this Award Agreement, the parties hereby submit to the exclusive jurisdiction of the State of California and agree that such litigation shall be conducted only in the courts of Santa Clara Country, California, or the federal courts for the Northern District of California, and no other courts, where this grant is made and/or to be performed.

20. Construction. It is intended that the terms of the Award will not result in the imposition of any tax liability pursuant to Section 409A of the Code. This Award Agreement shall be construed and interpreted consistent with that intent.

21. Severability. The provisions of this Award Agreement are severable and if any one of more provisions are determined to be illegal or otherwise unenforceable, in whole or in part, the remaining provisions shall nevertheless be binding and enforceable.

22. Imposition of Other Requirements. The Company reserves the right to impose other requirements on the Participant's participation in the Plan, on the Stock Units and on any Shares acquired under the Plan, to the extent the Company determines it is necessary or advisable in order to comply with local law or facilitate the administration of the Plan, and to require the Participant to sign any additional agreements or undertakings that may be necessary to accomplish the foregoing.

Exhibit 10.11

APPLE CONFIDENTIAL

To: Tony Fadell
From: Dan Cooperman
Date: November 3, 2008
Re: Transition Agreement

As we discussed, I want to confirm the terms of your transition from your current position at Apple to a new role.

Apple has agreed to extend your employment through at least March 24, 2010 pursuant to the conditions of this Transition Agreement and attached Settlement Agreement and Release (the “Term”). This will allow you to continue to receive a salary and benefits as well as to vest in certain Restricted Stock Units as described below. We have agreed that you will immediately resign from your position as Senior Vice President, iPod, and as a member of the Apple Executive Team. In your new role as Special Advisor to Apple’s Chief Executive Officer, you shall provide such advice and other services concerning the business of Apple as may be reasonably requested by the Chief Executive Officer from time to time on a part time, but not a full time basis. During the Term, you will not be employed by or perform consulting services for any other entity absent Apple’s prior written consent.

Your new salary shall be $300,000 USD per year, subject to standard deductions and payable during Apple’s normal payroll cycle. You shall continue to receive all other benefits of employment generally available to other members of the Company’s management, and shall be entitled to participate in Apple’s VP/Director Bonus Program. All salary, benefits and bonus eligibility shall cease upon the termination of your employment with Apple. You will be entitled to the full FY’08 SVP Annual Bonus Program and all of your accrued vacation time to date shall be paid in full at your pre-transition salary. Any subsequent vacation accrual shall be paid at your new salary. In the event that your wife is no longer employed at Apple, then you will not be subject to any blackout restrictions regarding your sale of Apple securities when and if such restrictions lapse for her.

In consideration for Apple’s offer of continued employment, and upon the new grant of the RSUs set forth herein, you agree to cancel all of your outstanding unvested restricted stock units (“RSUs”) (as reflected below). You will have no further rights with respect to any of the cancelled RSUs, but your stock options shall remain outstanding and the terms and conditions of such options, including the vesting provisions, shall remain in full force and effect. The chart below lists your unvested RSUs that will be cancelled per your understanding and agreement:

Grant Date	Grant Number	Equity Type	Current Number of Unvested RSUs [1]	Cancellation Date	Cancelled RSUs	New Number of RSUs
8/30/2005	128049	RSU	5,000	Effective Date	5,000	0
12/17/2007	145216	RSU	50,000	Effective Date	50,000	0
2/2/2006	130714	RSU	100,000	Effective Date	100,000	0

[1] Unvested RSUs as of 9/30/08

Subject to the approval of and at a date to be determined by the Board of Directors, Apple will recommend that you be granted an award of RSUs in the amount of 77,500 shares. The grant date and vesting commencement date will be determined by the Board, and shall be subject to the terms and conditions of Apple's 2003 Employee Stock Plan. The RSUs subject to the award will vest all at once on March 24, 2010, contingent upon your continued employment on that date, provided, however, that should Apple terminate your employment before March 24, 2010 without "Cause", your RSUs will accelerate and immediately vest and you shall be entitled to continuation of your salary payments (or pay in lieu at Apple's discretion) and benefits or COBRA reimbursement through March 24, 2010 subject to your execution of a new release commensurate with the terms of the attached release.

For purposes of this Agreement, "Cause" shall be defined as (i) an intentional material act of fraud or dishonesty in connection with your duties, or in the course of your employment with the Company; (ii) the conviction of a felony or crime involving moral turpitude; (iii) Your breach of this Transition Agreement or attached Settlement Agreement and Release; (iv) a willful act by you which constitutes gross misconduct and which is injurious to the Company; or (v) a willful breach of a material Apple policy or your Intellectual Property Agreement. Prior to any termination for "Cause" Apple will provide you with written notice of the basis for a "Cause" termination. In addition, prior to any termination for "Cause" under (iii) above, Apple will provide you with a ten (10) day opportunity to cure. No act or failure to act by you shall be considered "willful" unless committed without good faith and without a reasonable belief that the act or omission was in the Company's best interest.

You will have an opportunity to review in advance all press releases and SEC filings referencing your change in roles with Apple pursuant to the Transition Agreement. Unless otherwise required by law, these announcements will not infer or suggest that you have been demoted and/or terminated.

In order to receive the consideration outlined in this Transition Agreement, you will need to sign the attached Settlement Agreement and Release, and another similar agreement after your date of separation. The second agreement will release claims for the period between the date you sign the first agreement and the end of your employment. If you fail to sign the attached release of claims within seven days, your employment at Apple will come to an immediate end.

From today until your final date, I know that you will continue to adhere to Apple policies, and confidentiality agreements (including your Intellectual Property Agreement). Your employment shall remain at-will which means that either you or Apple may terminate your employment with or without notice or cause at any time subject to your rights under this Agreement.

Please be aware, the content of this memo and any related discussions or documents are confidential and are bound by the Intellectual Property Agreement that you signed as a condition of your employment with Apple. You are free to discuss this with your spouse and or legal/financial advisor.

Sincerely,

/s/ Dan Cooperman
Dan Cooperman
Apple Inc.

SETTLEMENT AGREEMENT AND RELEASE

This Settlement Agreement and General Release (Agreement) is made and entered into between Anthony Fadell (Employee) and Apple Inc. (Apple).

1. In exchange for the mutual promises set forth in this Agreement and in the Transition Agreement, Apple agrees as follows:

a. Apple will continue Employee's employment pursuant to terms set forth in the Transition Agreement. (Attached hereto as Exhibit 1 is a true and correct copy of the Transition Agreement which is hereby incorporated by reference.)

b. Effective as of the close of business on the date indicated in the Transition Agreement, or earlier as provided therein, Employee shall be terminated from the employ of Apple. At such time, Employee shall receive all benefits due him pursuant to the Transition Agreement, and all other benefits and sums otherwise due shall be computed in accordance with Apple's standard procedures and applicable benefit or other plan documents.

2. In exchange for the consideration herein, Employee agrees to the following separate and independent covenants:

a. <u>Transition Agreement</u>: Employee understands and agrees to the terms and conditions outlined in the attached Transition Agreement.

b. <u>Communications</u>: Employee agrees for the length of his employment and for one (1) year thereafter that he will not make any public statement to the press or media regarding Apple or his employment at Apple without the prior written approval of a Senior Officer of Apple. For avoidance of doubt, during the aforementioned period Employee shall not grant interviews, make public communications, take speaking opportunities, publish or provide any information or materials regarding Apple, its products, employees or his experiences at Apple absent the prior written approval of a Senior Officer of Apple. Employee further agrees that he shall not disparage Apple and its officers, directors and employees in any way in response to any inquiry from the press, public media or other third parties except as otherwise required by law. Apple's current Chief Executive Officer, and current Executive Team shall, in return, not disparage Employee, except as otherwise required by law. Other than as required by law, or as reasonably required to enforce its terms, Employee agrees not to disclose the terms or existence of this Agreement or the attached Transition Agreement to persons other than his spouse and his professional advisers.

c. Post Termination – Settlement Agreement & Release: Employee agrees that after his termination from Apple, provided there has been no breach of this Agreement or the Transition Agreement by Apple, he will execute an agreement releasing all claims and potential claims that he may have that have arisen between the effective date of this Agreement and his separation date in a form substantially similar to this Agreement.

d. No Solicitation of Apple Employees: Employee agrees that for a period of one (1) year following his termination date, to not, either directly or indirectly, for himself or on behalf of others, solicit or recruit Apple employees or contractors to terminate their relationship with Apple.

3. In exchange for the promises contained in this Agreement and the Transition Agreement above Employee, on behalf of Employee's heirs, estate, executors, administrators, successors and assigns does fully and completely release, discharge and agree to hold harmless Apple, its past, present and future successors, officers, directors, attorneys, agents, employees, shareholders, assigns, subsidiaries and affiliates from all charges, actions, claims, judgments, obligations, liabilities, costs, expenses, damages (including but not limited to general, special, punitive, liquidated and compensatory damages) or causes of action of every kind, nature and character, known or unknown, in law or equity, fixed or contingent, which Employee may now have, or ever had arising from or in any way connected with Employee's relationship or termination of employment with Apple. This release includes, but is not limited to:

a. Any charges or claims relating to, arising out of, or connected with Employee's employment with Apple, whether or not based upon any alleged violations of public policy; compliance (or lack thereof) with any internal Apple policy, procedure, practice or guideline; or any oral, written, express, and/or implied employment contract or agreement, or the breach of any term thereof, including but not limited to, any implied covenant of good faith and fair dealing; or any federal, state, county or municipal statute, law, regulation, order or ordinance whether or not relating to labor or employment; or any other charges or claims relating to the law of contract or tort;

b. any charges or claims relating to employment discrimination on account of race, sex, national origin, creed, religion, disability, or other basis, including harassment, whether or not arising under the federal Civil Rights Acts (Title VII), 42 U.S.C. Section 1981, the Rehabilitation Act of 1973, the Americans With Disabilities Act, any amendments to the foregoing laws, or any other federal, state, county, municipal or other law, statute, regulation or order relating to employment discrimination; and any claims relating to employment discrimination on account of age, whether or not arising under the Age Discrimination in Employment Act (ADEA) or any state law, statute or regulation relating to age discrimination.

c. any charges or claims arising under the Employee Retirement and Income Security Act, and any other laws and regulations relating to employment, and any and all claims for attorney's fees and costs;

d. any charges or claims relating to pay or leave of absence arising under the Fair Labor Standards Act, the Family & Medical Leave Act, and any similar state laws or regulations;

e. any charges or claims for reemployment, salary, wages, bonuses, vacation pay, stock options, acquired rights, appreciation from stock options, stock appreciation rights, any other form of equity or equity rights, benefits or other compensation of any kind; and

f. any charges or claims relating to, arising out of, or connected with any other matter or event occurring prior to the execution of the Agreement whether or not brought before any judicial, administrative, or other tribunal.

Employee represents and warrants that Employee has not assigned any such charge or claim or authorized any other person or entity to assert such charge or claim on Employee's behalf. Further, Employee agrees that under this Agreement, Employee waives any claim for damages incurred at any time in the future because of alleged continuing effects of past wrongful conduct involving any such claims and any right to sue for injunctive relief against Apple.

In entering into this Agreement, Employee has intended that this Agreement be a full and final settlement of all matters, whether or not presently disputed, that could have arisen between the parties. Employee understands and expressly agrees that by this Agreement he expressly waives all claims of every nature and kind whatsoever, known or unknown, suspected or unsuspected, past or present and all rights under Section 1542 of the California Civil Code and/or any similar statute or law of any other jurisdiction. Such section reads as follows:

Section 1542. "A general release does not extend to claims which the creditor does not know or suspect to exist in his favor at the time of executing the release, if known by him must have materially affected his settlement with the debtor."

It is expressly agreed that the charges and claims released pursuant to this Agreement include all charges and claims against individual employees of Apple, whether or not such employees were acting within the course and scope of their employment.

Notwithstanding the above, nothing in this Settlement Agreement shall release or in any manner impair any rights Employee may have under California Labor Code Section 2802 or any other right to indemnification under applicable law, policy, agreement, applicable Apple by-laws, certificate of incorporation, or directors and officers liability insurance. Further the release contained herein shall not extend to any obligations incurred under this Agreement or the Transition Agreement, as well as any claims that cannot be released as a matter of law.

4. Non-Waiver; Complete Agreement; Governing Law. No provisions of this Agreement may be modified, waived or discharged except in writing signed by both Employee and a Senior Officer of Apple. No waiver by either party at any time of any breach by the other party of, or compliance with, any condition or provision of this Agreement shall be deemed a waiver of similar or dissimilar provisions or conditions at the same or at any prior to subsequent time. This Agreement and the attached Transition Agreement is the complete agreement of the parties as to the subject matter hereof. No agreements or representations, oral or otherwise, express or implied, with respect to the subject matter hereof have been made by either party which are not set forth expressly in this Agreement or the Transition Agreement, and Employee and Apple represent and acknowledge that they have not relied upon any agreements or representations not set forth in either document, and that any prior agreements or representations relating to the subject matter of this Agreement are hereby superseded. Notwithstanding the above, this Agreement is not intended to modify, supersede, or otherwise extinguish the provisions of Employee's Intellectual Property Agreement. To the extent any provisions of the Intellectual Property Agreement have continuing force and effect after the termination of Employee's employment with Apple, this Agreement does not alter or affect those provisions in any way. This Agreement shall be governed by and construed in accordance with the laws of the State of California, other than its conflict of law provisions.

5. Severability. The invalidity or unenforceability of any provisions of this Agreement shall not affect the validity or enforceability of any other provision of this Agreement, which shall remain in full force and effect.

6. Release of Claims. Employee understands that Employee has seven (7) days from the date Employee receives this Agreement to consider and sign this Agreement, but that Employee may waive this period of time.

7. Counterparts. This Agreement may be executed in one or more counterparts, each of which shall be deemed to be an original but all of which together shall constitute one and the same instrument.

8. Attorneys' Fees. In the event of the bringing of any action, proceeding, arbitration or suit by a party hereto against another party hereunder by reason of any breach of any of the covenants, agreements, or provisions arising out of this Agreement, the prevailing party shall be entitled to recover all costs and expenses of that action or suit, or at trial, arbitration or on appeal, and in collection of judgment, including reasonable attorneys' fees, accounting, and other professional fees resulting therefrom.

IN WITNESS WHEREOF, the Employee and Apple have executed this Agreement, effective as of the date first above written.

Apple

Date: November 3, 2008

By: /s/ Dan Cooperman

Dan Cooperman, Apple Inc.

By signing this Agreement, I acknowledge that I have had the opportunity to review this Agreement carefully with an attorney of my choice; that I have carefully read this Agreement, and that I fully I understand the terms of this Agreement and attached Transition Agreement along with their final and binding effect; and that I knowingly and voluntarily agree to them.

Date: November 3, 2008

By: /s/ Anthony M. Fadell

Anthony M. Fadell

Exhibit 18.1

January 22, 2009

The Board of Directors
Apple Inc.
1 Infinite Loop
Cupertino, CA 95014

Ladies and Gentlemen:

We have been furnished with a copy of the quarterly report on Form 10-Q of Apple Inc. and subsidiaries (the Company) as of and for the three months ended December 27, 2008, and have read the Company's statements contained in notes 1 and 2 to the condensed consolidated interim financial statements included therein. As stated in notes 1 and 2, the Company changed its method for presenting certain of its investment securities previously classified as current assets to non-current assets. The Company states that this new presentation is preferable as it is more reflective of the Company's assessment of the timing of when such investment securities will be converted to cash.

In accordance with your request, we have reviewed and discussed with Company officials the circumstances and business judgment and planning upon which the decision to make this change in the method of accounting was based.

We have not audited any financial statements of the Company as of any date or for any period subsequent to September 27, 2008, nor have we audited the information set forth in the aforementioned notes 1 and 2 to the condensed consolidated interim financial statements; accordingly, we do not express an opinion concerning the factual information contained therein.

With regard to the aforementioned accounting change, authoritative criteria have not been established for evaluating the preferability of one acceptable method of accounting over another acceptable method. However, for purposes of the Company's compliance with the requirements of the Securities and Exchange Commission, we are furnishing this letter.

Based on our review and discussion, with reliance on management's business judgment and planning, we concur that the newly adopted method of accounting is preferable in the Company's circumstances.

Very truly yours,

/s/ KPMG LLP

Exhibit 31.1

CERTIFICATIONS

I, Steven P. Jobs, certify that:

1. I have reviewed this quarterly report on Form 10-Q of Apple Inc.;

2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;

3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;

4. The registrant's other certifying officer(s) and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f)) for the registrant and have:

   (a) Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;

   (b) Designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles;

   (c) Evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and

   (d) Disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter (the registrant's fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting; and

5. The registrant's other certifying officer(s) and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of the registrant's board of directors (or persons performing the equivalent functions):

   (a) All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize, and report financial information; and

   (b) Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal control over financial reporting.

Date: January 22, 2009

By: /s/ Steven P. Jobs
Steven P. Jobs
Chief Executive Officer

Exhibit 31.2

CERTIFICATIONS

I, Peter Oppenheimer, certify that:

1. I have reviewed this quarterly report on Form 10-Q of Apple Inc.;
2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;
3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;
4. The registrant's other certifying officer(s) and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f)) for the registrant and have:
   (a) Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;
   (b) Designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles;
   (c) Evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and
   (d) Disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter (the registrant's fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting; and
5. The registrant's other certifying officer(s) and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of the registrant's board of directors (or persons performing the equivalent functions):
   (a) All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize, and report financial information; and
   (b) Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal control over financial reporting.

Date: January 22, 2009

By: /s/ Peter Oppenheimer
Peter Oppenheimer
Senior Vice President and
Chief Financial Officer

Exhibit 32.1

CERTIFICATION OF CHIEF EXECUTIVE OFFICER 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

I, Steven P. Jobs, certify, pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002, that the Quarterly Report of Apple Inc. on Form 10-Q for the period ended December 27, 2008 fully complies with the requirements of Section 13(a) or 15(d) of the Securities Exchange Act of 1934 and that information contained in such Form 10-Q fairly presents in all material respects the financial condition and results of operations of Apple Inc.

Date: January 22, 2009

By: /s/ Steven P. Jobs
Steven P. Jobs
Chief Executive Officer

I, Peter Oppenheimer, certify, pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002, that the Quarterly Report of Apple Inc. on Form 10-Q for the period ended December 27, 2008 fully complies with the requirements of Section 13(a) or 15(d) of the Securities Exchange Act of 1934 and that information contained in such Form 10-Q fairly presents in all material respects the financial condition and results of operations of Apple Inc.

Date: January 22, 2009

By: /s/ Peter Oppenheimer
Peter Oppenheimer
Senior Vice President and
Chief Financial Officer

A signed original of this written statement required by Section 906 has been provided to Apple Inc. and will be retained by Apple Inc. and furnished to the Securities and Exchange Commission or its staff upon request.