ESTEE LAUDER COMPANIES INC
Form 10-Q
May 03, 2017
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UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549-1004

FORM 10-Q

(Mark One)-

x **Quarterly Report Pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934**

For the quarterly period ended March 31, 2017

OR

o **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: 1-14064

The Estée Lauder Companies Inc.

(Exact name of registrant as specified in its charter)

Delaware (State or other jurisdiction of incorporation or organization)	**11-2408943** (I.R.S. Employer Identification No.)
767 Fifth Avenue, New York, New York (Address of principal executive offices)	**10153** (Zip Code)

212-572-4200

(Registrant s telephone number, including area code)

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

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (§232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). Yes x No o

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

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

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

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

At April 26, 2017, 223,870,597 shares of the registrant s Class A Common Stock, $.01 par value, and 143,961,737 shares of the registrant s Class B Common Stock, $.01 par value, were outstanding.

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PART I. FINANCIAL INFORMATION

Item 1. ***Financial Statements.***

THE ESTÉE LAUDER COMPANIES INC.

CONSOLIDATED STATEMENTS OF EARNINGS

(Unaudited)

	Three Months Ended March 31		Nine Months Ended March 31	
	2017	**2016**	**2017**	**2016**
	(In millions, except per share data)			
Net Sales	$ 2,857	$ 2,657	$ 8,930	$ 8,616
Cost of Sales	591	504	1,824	1,670
Gross Profit	2,266	2,153	7,106	6,946
Operating Expenses				
Selling, general and administrative	1,780	1,754	5,522	5,445
Restructuring and other charges	59	15	122	34
Total operating expenses	1,839	1,769	5,644	5,479
Operating Income	427	384	1,462	1,467
Interest expense	28	18	71	52
Interest income and investment income, net	8	4	19	10
Earnings before Income Taxes	407	370	1,410	1,425
Provision for income taxes	107	104	384	399
Net Earnings	300	266	1,026	1,026
Net earnings attributable to noncontrolling interests	(2)	(1)	(6)	(5)
Net Earnings Attributable to The Estée Lauder Companies Inc.	$ 298	$ 265	$ 1,020	$ 1,021
Net earnings attributable to The Estée Lauder Companies Inc. per common share				
Basic	$ .81	$ .72	$ 2.78	$ 2.76
Diluted	$ .80	$ .71	$ 2.74	$ 2.71
Weighted-average common shares outstanding				
Basic	367.0	369.1	366.8	370.4

Diluted	372.3	375.6	372.7	376.9
Cash dividends declared per common share	$ .34	$ .30	$ .98	$ .84

See notes to consolidated financial statements.

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THE ESTÉE LAUDER COMPANIES INC.

CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME (LOSS)

(Unaudited)

	Three Months Ended March 31		Nine Months Ended March 31	
	2017	2016	2017	2016
	(In millions)			
Net earnings	$ 300	$ 266	$ 1,026	$ 1,026
Other comprehensive income (loss):				
Net unrealized investment gain (loss)	2	7	(9)	3
Net derivative instrument gain (loss)	(51)	(36)	(17)	(32)
Amounts included in net periodic benefit cost	7	6	23	19
Translation adjustments	64	71	(49)	(52)
Benefit (provision) for deferred income taxes on components of other comprehensive income	17	11	(2)	4
Total other comprehensive income (loss)	39	59	(54)	(58)
Comprehensive income (loss)	339	325	972	968
Comprehensive (income) loss attributable to noncontrolling interests:				
Net earnings	(2)	(1)	(6)	(5)
Translation adjustments	1	(1)		
	(1)	(2)	(6)	(5)
Comprehensive income (loss) attributable to The Estée Lauder Companies Inc.	$ 338	$ 323	$ 966	$ 963

See notes to consolidated financial statements.

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THE ESTÉE LAUDER COMPANIES INC.

CONSOLIDATED BALANCE SHEETS

	March 31 2017 (Unaudited)	June 30 2016
	($ in millions)	
ASSETS		
Current Assets		
Cash and cash equivalents	$ 1,139	$ 914
Short-term investments	701	469
Accounts receivable, net	1,528	1,258
Inventory and promotional merchandise, net	1,310	1,264
Prepaid expenses and other current assets	294	320
Total current assets	4,972	4,225
Property, Plant and Equipment, net	1,576	1,583
Other Assets		
Long-term investments	993	1,108
Goodwill	1,942	1,228
Other intangible assets, net	1,337	344
Other assets	625	735
Total other assets	4,897	3,415
Total assets	$ 11,445	$ 9,223
LIABILITIES AND EQUITY		
Current Liabilities		
Current debt	$ 519	$ 332
Accounts payable	597	717
Other accrued liabilities	1,744	1,632
Total current liabilities	2,860	2,681
Noncurrent Liabilities		
Long-term debt	3,377	1,910
Other noncurrent liabilities	1,073	1,045
Total noncurrent liabilities	4,450	2,955
Contingencies (Note 10)		
Equity		
Common stock, $.01 par value; Class A shares authorized: 1,300,000,000 at March 31, 2017 and June 30, 2016; shares issued: 428,868,500 at March 31, 2017 and 424,109,008 at June 30, 2016; Class B shares authorized: 304,000,000 at March 31, 2017 and June 30, 2016; shares issued and outstanding: 143,961,737 at March 31, 2017 and 144,770,237 at June 30, 2016	6	6
Paid-in capital	3,462	3,161
Retained earnings	8,350	7,693
Accumulated other comprehensive loss	(599)	(545)
	11,219	10,315
	(7,100)	(6,743)

Less: Treasury stock, at cost; 205,125,233 Class A shares at March 31, 2017 and 201,119,435 Class A shares at June 30, 2016				
Total stockholders equity The Estée Lauder Companies Inc.		4,119		3,572
Noncontrolling interests		16		15
Total equity		4,135		3,587
Total liabilities and equity	$	11,445	$	9,223

See notes to consolidated financial statements.

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CONSOLIDATED STATEMENTS OF CASH FLOWS

(Unaudited)

	Nine Months Ended March 31 2017	2016
	(In millions)	
Cash Flows from Operating Activities		
Net earnings	$ 1,026	$ 1,026
Adjustments to reconcile net earnings to net cash flows from operating activities:		
Depreciation and amortization	337	305
Deferred income taxes	(84)	(51)
Noncash stock-based compensation	175	147
Excess tax benefits from stock-based compensation arrangements	(37)	(18)
Net (gain) loss on disposal of property, plant and equipment	(4)	10
Noncash restructuring and other charges	3	15
Pension and post-retirement benefit expense	59	53
Pension and post-retirement benefit contributions	(19)	(19)
Change in fair value of contingent consideration	1	16
Equity investment income	(17)	(2)
Changes in operating assets and liabilities:		
Increase in accounts receivable, net	(242)	(251)
Decrease in inventory and promotional merchandise, net	59	53
Increase in other assets, net	(30)	(82)
Decrease in accounts payable	(168)	(46)
Increase in other accrued and noncurrent liabilities	193	160
Net cash flows provided by operating activities	1,252	1,316
Cash Flows from Investing Activities		
Capital expenditures	(316)	(334)
Payments for acquired businesses, net of cash acquired	(1,690)	(101)
Proceeds from disposition of investments	955	925
Purchases of investments	(1,067)	(1,587)
Proceeds from sale of property, plant and equipment	12	
Net cash flows used for investing activities	(2,106)	(1,097)
Cash Flows from Financing Activities		
Proceeds of current debt, net	194	286
Proceeds from issuance of long-term debt, net	1,498	
Debt issuance costs	(10)	
Repayments and redemptions of long-term debt	(4)	(6)
Net proceeds from stock-based compensation transactions	94	55
Excess tax benefits from stock-based compensation arrangements	37	18
Payments to acquire treasury stock	(363)	(703)
Dividends paid to stockholders	(361)	(312)
Payments to noncontrolling interest holders for dividends	(2)	(3)
Net cash flows provided by (used for) financing activities	1,083	(665)
Effect of Exchange Rate Changes on Cash and Cash Equivalents	(4)	(19)

Net Increase (Decrease) in Cash and Cash Equivalents		225		(465)
Cash and Cash Equivalents at Beginning of Period		914		1,021
Cash and Cash Equivalents at End of Period	$	1,139	$	556

See notes to consolidated financial statements.

THE ESTÉE LAUDER COMPANIES INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

NOTE 1 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Basis of Presentation

The accompanying consolidated financial statements include the accounts of The Estée Lauder Companies Inc. and its subsidiaries (collectively, the Company). All significant intercompany balances and transactions have been eliminated.

The unaudited interim consolidated financial statements have been prepared in accordance with U.S. generally accepted accounting principles (U.S. GAAP) for interim financial information and with the instructions to Form 10-Q and Rule 10-01 of Regulation S-X. Accordingly, they do not include all of the information and footnotes required by U.S. GAAP for complete financial statements. In the opinion of management, all adjustments of a normal recurring nature considered necessary for a fair presentation have been included. The results of operations of any interim period are not necessarily indicative of the results of operations to be expected for the full fiscal year. The interim consolidated financial statements should be read in conjunction with the consolidated financial statements and accompanying footnotes included in the Company s Annual Report on Form 10-K for the fiscal year ended June 30, 2016.

Management Estimates

The preparation of financial statements and related disclosures in conformity with U.S. GAAP requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses reported in those financial statements. Certain significant accounting policies that contain subjective management estimates and assumptions include those related to revenue recognition, inventory, pension and other post-retirement benefit costs, goodwill, other intangible assets and long-lived assets, and income taxes. Descriptions of these policies are discussed in the notes to consolidated financial statements in the Company s Annual Report on Form 10-K for the fiscal year ended June 30, 2016. Management evaluates its estimates and assumptions on an ongoing basis using historical experience and other factors, including the current economic environment, and makes adjustments when facts and circumstances dictate. As future events and their effects cannot be determined with precision, actual results could differ significantly from those estimates and assumptions. Significant changes, if any, in those estimates and assumptions resulting from continuing changes in the economic environment will be reflected in the consolidated financial statements in future periods.

Currency Translation and Transactions

All assets and liabilities of foreign subsidiaries and affiliates are translated at period-end rates of exchange, while revenue and expenses are translated at weighted-average rates of exchange for the period. Unrealized translation gains (losses) reported as cumulative translation adjustments through other comprehensive income (loss) (OCI) attributable to The Estée Lauder Companies Inc. amounted to $67 million and $72 million, net of tax, during the three months ended March 31, 2017 and 2016, respectively, and $(53) million and $(57) million, net of tax, during the nine months ended March 31, 2017 and 2016, respectively.

The Company enters into foreign currency forward contracts and may enter into option contracts to hedge foreign currency transactions for periods consistent with its identified exposures. Accordingly, the Company categorizes these instruments as entered into for purposes other than trading.

The accompanying consolidated statements of earnings include net exchange gains on foreign currency transactions of $8 million and $11 million during the three months ended March 31, 2017 and 2016, respectively, and $14 million and $16 million during the nine months ended March 31, 2017 and 2016, respectively.

Accounts Receivable

Accounts receivable is stated net of the allowance for doubtful accounts and customer deductions totaling $23 million and $24 million as of March 31, 2017 and June 30, 2016, respectively.

Concentration of Credit Risk

The Company is a worldwide manufacturer, marketer and distributor of skin care, makeup, fragrance and hair care products. The Company s sales subject to credit risk are made primarily to department stores, perfumeries, specialty multi-brand retailers and retailers in its travel retail business. The Company grants credit to qualified customers and does not believe it is exposed significantly to any undue concentration of credit risk.

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The Company s largest customer sells products primarily within the United States and accounted for $230 million, or 8%, and $248 million, or 9%, of the Company s consolidated net sales for the three months ended March 31, 2017 and 2016, respectively, and $763 million, or 9%, and $840 million, or 10%, of the Company s consolidated net sales for the nine months ended March 31, 2017 and 2016, respectively. This customer accounted for $205 million, or 13%, and $164 million, or 13%, of the Company s accounts receivable at March 31, 2017 and June 30, 2016, respectively.

Inventory and Promotional Merchandise

Inventory and promotional merchandise, net consists of:

(In millions)	March 31 2017	June 30 2016
Raw materials	$ 278	$ 306
Work in process	157	177
Finished goods	727	622
Promotional merchandise	148	159
	$ 1,310	$ 1,264

Property, Plant and Equipment

(In millions)	March 31 2017	June 30 2016
Assets (Useful Life)		
Land	$ 29	$ 15
Buildings and improvements (10 to 40 years)	183	187
Machinery and equipment (3 to 10 years)	636	680
Computer hardware and software (4 to 15 years)	1,094	1,041
Furniture and fixtures (5 to 10 years)	92	84
Leasehold improvements	1,854	1,789
	3,888	3,796
Less accumulated depreciation and amortization	(2,312)	(2,213)
	$ 1,576	$ 1,583

The cost of assets related to projects in progress of $202 million and $186 million as of March 31, 2017 and June 30, 2016, respectively, is included in their respective asset categories above. Depreciation and amortization of property, plant and equipment was $106 million and $100 million during the three months ended March 31, 2017 and 2016, respectively, and $316 million and $295 million during the nine months ended March 31, 2017 and 2016, respectively. Depreciation and amortization related to the Company s manufacturing process is included in Cost of Sales, and all other depreciation and amortization is included in Selling, general and administrative expenses in the accompanying consolidated statements of earnings.

Other Accrued Liabilities

Other accrued liabilities consist of the following:

(In millions)	March 31 2017	June 30 2016
Advertising, merchandising and sampling	$ 315	$ 283
Employee compensation	437	504
Payroll and other taxes	206	163
Other	786	682
	$ 1,744	$ 1,632

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NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

Income Taxes

The effective rate for income taxes was 26.3% and 28.0% for the three months ended March 31, 2017 and 2016, respectively, and 27.2% and 28.0% for the nine months ended March 31, 2017 and 2016, respectively.

The decrease in the effective tax rate for each of the three-month and nine-month periods ended March 31, 2017 was primarily attributable to income tax reserve adjustments.

As of March 31, 2017 and June 30, 2016, the gross amount of unrecognized tax benefits, exclusive of interest and penalties, totaled $76 million and $82 million, respectively. The total amount of unrecognized tax benefits at March 31, 2017 that, if recognized, would affect the effective tax rate was $49 million. During the three months ended March 31, 2017, the Company recognized a gross interest and penalty benefit of $1 million in the accompanying consolidated statement of earnings. There was a total gross accrued interest and penalty expense during the nine months ended March 31, 2017 that was de minimis. The total gross accrued interest and penalties in the accompanying consolidated balance sheets at March 31, 2017 and June 30, 2016 totaled $18 million at the end of each respective period. On the basis of the information available as of March 31, 2017, it is reasonably possible that the total amount of unrecognized tax benefits could decrease in a range of $5 million to $10 million within the next twelve months as a result of projected resolutions of global tax examinations and controversies and a potential lapse of the applicable statutes of limitations.

Recently Issued Accounting Standards

Pension-related Costs

In March 2017, the Financial Accounting Standards Board (FASB) issued authoritative guidance that amends how companies present net periodic benefit cost in the income statement and balance sheet relating to defined benefit pension and/or other postretirement benefit plans. Within the income statement, the new guidance requires companies to report the service cost component within operating expenses and report the other components of net periodic benefit cost below operating income (if one is reported). In addition, within the balance sheet, the guidance changes the components of the pension cost eligible for capitalization to the service cost component only (e.g., as a cost of internally manufactured inventory or a self-constructed asset).

Effective for the Company Fiscal 2019 first quarter, with early adoption permitted as of the first interim period in fiscal 2018. The guidance must be applied (a) retrospectively as it pertains to the income statement classification of the components of net periodic benefit cost and (b) prospectively as it pertains to future capitalization of service costs.

Impact on consolidated financial statements The Company is currently evaluating the timing of adoption and impact of applying this guidance on its consolidated financial statements.

Goodwill

In January 2017, FASB issued authoritative guidance which simplifies the subsequent measurement of goodwill by eliminating the second step from the quantitative goodwill impairment test. The single quantitative step test requires companies to compare the fair value of a reporting unit with its carrying amount and record an impairment charge for the amount that the carrying amount exceeds the fair value, up to the total amount of goodwill allocated to that reporting unit. The Company will continue to have the option of first performing a qualitative assessment to determine whether it is necessary to perform the quantitative goodwill impairment test.

Effective for the Company Fiscal 2021 first quarter, with early adoption permitted for interim or annual goodwill impairment tests performed on testing dates after January 1, 2017.

Impact on consolidated financial statements The impact of applying this guidance will be evaluated by the Company for future interim and annual impairment tests.

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NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

Income Taxes

In October 2016, the FASB issued authoritative guidance that changes the way companies account for income taxes relating to intra-entity transfers of assets other than inventory. This new guidance requires that an entity recognize the income tax consequences of an intra-entity transfer of an asset other than inventory in the period in which the transfer takes place. Under current guidance, recognition of current and deferred income taxes of an intra-entity asset transfer is prohibited until the asset has been sold to an outside party. This new guidance may affect consolidated earnings where the intra-entity transfer of an asset other than inventory occurs between entities in jurisdictions with different tax rates. This guidance must be adopted using a modified retrospective approach with a cumulative-effect adjustment to retained earnings as of the beginning of the period of adoption.

Effective for the Company Fiscal 2019 first quarter, with early adoption permitted.

Impact on consolidated financial statements The Company is currently evaluating the impact of applying this guidance.

Measurement of Credit Losses on Financial Instruments

In June 2016, the FASB issued authoritative guidance that requires companies to utilize an impairment model for most financial assets measured at amortized cost and certain other financial instruments, which include trade and other receivables, loans and held-to-maturity debt securities, to record an allowance for credit risk based on expected losses rather than incurred losses. In addition, this new guidance changes the recognition method for credit losses on available-for-sale debt securities, which can occur as a result of market and credit risk, as well as additional disclosures. In general, this guidance will require modified retrospective adoption for all outstanding instruments that fall under this guidance.

Effective for the Company Fiscal 2021 first quarter.

Impact on consolidated financial statements The Company is currently evaluating the impact of applying this guidance on its financial instruments, such as accounts receivable and short- and long-term investments.

Compensation - Stock Compensation

In March 2016, the FASB issued authoritative guidance that changes the way companies account for certain aspects of share-based payments to employees. This new guidance requires that all excess tax benefits and tax deficiencies related to share-based compensation awards be recorded as income tax expense or benefit in the income statement. In addition, companies are required to treat the tax effects of exercised or vested awards as discrete items in the period that they occur. This guidance also permits an employer to withhold up to the maximum statutory withholding rates in a jurisdiction without triggering liability classification, allows companies to elect to account for forfeitures as they occur, and provides requirements for the cash flow classification of cash paid by an employer when directly withholding shares for tax-withholding purposes and for the classification of excess tax benefits. The new guidance prescribes different transition methods for the various provisions.

Effective for the Company Fiscal 2018 first quarter, with early adoption permitted.

Impact on consolidated financial statements The Company will adopt this guidance in its fiscal 2018 first quarter. For the fiscal years ended June 30, 2016 and 2015, the Company recognized $22 million and $47 million of excess tax benefits, respectively, directly in its consolidated statements of equity. These amounts may or may not be representative of future amounts to be recognized in the income statement upon the adoption of this new standard, as the impact of the adoption will be primarily dependent on the timing and intrinsic value of stock-based compensation awards, employee exercise behavior and applicable tax rates.

Leases

In February 2016, the FASB issued authoritative guidance that requires lessees to account for most leases on their balance sheets with the liability being equal to the present value of the lease payments. The right-of-use asset will be based on the lease liability adjusted for certain costs such as direct costs. Lease expense will be recognized similar to current accounting guidance with operating leases resulting in a straight-line expense, and financing leases resulting in a front-loaded expense similar to the current accounting for capital leases. This guidance must be adopted using a modified retrospective transition approach for leases that exist or are entered into after the beginning of the earliest comparative period in the financial statements, and provides for certain practical expedients.

Effective for the Company Fiscal 2020 first quarter, with early adoption permitted.

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NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

Impact on consolidated financial statements The Company currently has an implementation team in place that is performing a comprehensive evaluation of the impact of the adoption of this guidance. While the Company has not completed its evaluation, it believes the adoption of this standard will have a significant impact on its Consolidated Balance Sheets.

Revenue from Contracts with Customers

In May 2014, the FASB issued authoritative guidance that defines how companies should report revenues from contracts with customers. The standard requires an entity to recognize revenue to depict the transfer of promised goods or services to customers in an amount that reflects the consideration to which the entity expects to be entitled in exchange for those goods or services. It provides companies with a single comprehensive five-step principles-based model to use in accounting for revenue and supersedes current revenue recognition requirements, including most industry-specific and transaction-specific revenue guidance.

In March 2016, the FASB issued authoritative guidance that amended the principal versus agent guidance in its new revenue recognition standard. These amendments do not change the key aspects of the principal versus agent guidance, including the definition that an entity is a principal if it controls the good or service prior to it being transferred to a customer, but the amendments clarify the implementation guidance related to the considerations that must be made during the contract evaluation process.

In April 2016, the FASB issued authoritative guidance that amended the new standard to clarify the guidance on identifying performance obligations and accounting for licenses of intellectual property.

In May 2016, the FASB issued authoritative guidance that clarified certain terms, guidance and disclosure requirements during the transition period related to completed contracts and contract modifications. In addition, the FASB provided clarification on the concept of collectability, the calculation of the fair value of noncash consideration and the presentation of sales and other similar taxes.

In May 2016, the FASB issued authoritative guidance to reflect the Securities and Exchange Commission Staff s rescission of their prior comments that covered, among other things, accounting for shipping and handling costs and accounting for consideration given by a vendor to a customer.

In December 2016, the FASB issued authoritative guidance that amends various aspects of the new standard to clarify certain terms, guidance and disclosure requirements. In particular, the guidance addresses disclosure requirements for remaining performance obligations, impairment testing for contract costs and accrual of advertising costs, as well as clarifies several examples.

Effective for the Company Fiscal 2019, with early adoption permitted. An entity is permitted to apply the foregoing guidance retrospectively to all prior periods presented, with certain practical expedients, or apply the requirements in the year of adoption, through a cumulative adjustment.

Impact on consolidated financial statements The Company will apply all of this new guidance when they become effective in fiscal 2019 and has not yet selected a transition method. The Company currently has an implementation team in place that is performing a comprehensive evaluation of the impact of adoption and assessing the impact on third-party customer arrangements and the Company s customer loyalty programs.

No other recently issued accounting pronouncements are expected to have a material impact on the Company s consolidated financial statements.

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NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

NOTE 2 INVESTMENTS

Gains and losses recorded in accumulated OCI (AOCI) related to the Company s available-for-sale investments as of March 31, 2017 were as follows:

(In millions)	Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value
U.S. government and agency securities	$ 452	$ 2	$ (2)	$ 452
Foreign government and agency securities	103		(1)	102
Corporate notes and bonds	506		(2)	504
Time deposits	520			520
Other securities	26	1		27
Total	$ 1,607	$ 3	$ (5)	$ 1,605

Gains and losses recorded in AOCI related to the Company s available-for-sale investments as of June 30, 2016 were as follows:

(In millions)	Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value
U.S. government and agency securities	$ 560	$ 3	$	$ 563
Foreign government and agency securities	61			61
Corporate notes and bonds	454	3		457
Time deposits	390			390
Other securities	32	1		33
Total	$ 1,497	$ 7	$	$ 1,504

The following table presents the Company s available-for-sale securities by contractual maturity as of March 31, 2017:

(In millions)	Cost	Fair Value
Due within one year	$ 701	$ 701
Due after one through five years	906	904
	$ 1,607	$ 1,605

The following table presents the fair market value of the Company s investments with gross unrealized losses that are not deemed to be other-than temporarily impaired as of March 31, 2017:

	In a Loss Position for Less Than 12 Months		In a Loss Position for More Than 12 Months	
(In millions)	**Fair Value**	**Gross Unrealized Losses**	**Fair Value**	**Gross Unrealized Losses**
Available-for-sale securities	$ 702	$ (5)	$ 5	$

There were no gross gains or losses realized on sales of investments included in the consolidated statements of earnings for the three and nine months ended March 31, 2017 and 2016.

The Company utilizes the first-in, first-out method to determine the cost of the security sold. Sales proceeds from investments classified as available-for-sale were $200 million and $120 million for the three months ended March 31, 2017 and 2016, respectively, and $532 million and $502 million for the nine months ended March 31, 2017 and 2016, respectively.

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NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

NOTE 3 ACQUISITION OF BUSINESSES

On December 19, 2016, the Company acquired 100% of Too Faced, a makeup brand, for approximately $1.5 billion. This acquisition is expected to complement the Company s distribution in the specialty-multi channel. The amount paid at closing was funded by cash on hand including the proceeds from the issuance of commercial paper. In February 2017, the Company issued long-term debt to refinance a portion of the outstanding commercial paper. See Note 6 Debt. The purchase price recorded is provisional pending final working capital adjustments and completion of the final valuation. The results of operations of Too Faced are included in the Company s consolidated financial statements commencing on the acquisition date.

The Company has recorded an allocation of the purchase price to the Company s tangible and identifiable intangible assets acquired and liabilities assumed based on their fair value at the acquisition date. The excess of the purchase price over the fair value of the net tangible and intangible assets was recorded as goodwill, which includes value associated with assembled workforce. The calculation of purchase price and purchase price allocation is as follows:

(In millions, unaudited)		
Cash	$	28
Accounts receivable(1)		40
Inventory		105
Other current assets		3
Property, plant and equipment		8
Intangible assets		858
Goodwill		613
Total assets acquired		1,655
Accounts payable		56
Other accrued liabilities		15
Deferred income taxes		100
Total liabilities assumed		171
Total purchase price	$	1,484

(1) Represents the gross amount of trade receivables of $44 million, net of estimated customer deductions of $4 million.

For the three and nine months ended March 31, 2017, the Company s statements of earnings included approximately $87 million and $100 million, respectively, of net sales and $(5) million and $(10) million, net of tax, respectively, of net earnings (loss), inclusive of acquisition-related costs, related to Too Faced. Acquisition-related costs, which primarily include financial advisory, accounting and legal fees, in the amount of $9 million for the nine months ended March 31, 2017 are included in Selling, general and administrative expenses in the accompanying consolidated statements of earnings.

On November 14, 2016, the Company also acquired 100% of BECCA, a makeup brand. Pro forma results of operations reflecting the Too Faced and BECCA acquisitions have not been presented, as the impact on the Company s consolidated financial results would not have been material.

NOTE 4 GOODWILL AND OTHER INTANGIBLE ASSETS

As previously discussed in Note 3 Acquisition of Businesses, during the nine months ended March 31, 2017, the Company acquired Too Faced and BECCA, which included the addition of goodwill of $712 million, amortizable intangible assets of $394 million (with a weighted-average amortization period of approximately 10 years) and non-amortizable intangible assets of $623 million. Goodwill associated with the acquisitions is primarily attributable to the future revenue growth opportunities associated with additional share in the makeup category. As such, the goodwill has been allocated to the Company s makeup product category. Approximately $265 million of goodwill recorded in connection with certain of these acquisitions is expected to be deductible for tax purposes. These amounts are provisional pending final working capital adjustments and completion of the final valuations. During the nine months ended March 31, 2017, the Company recognized $8 million of goodwill associated with the continuing earn-out obligations related to the acquisition of the Bobbi Brown brand.

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The intangible assets acquired in connection with the acquisitions of Too Faced and BECCA are classified as Level 3 in the fair value hierarchy. The estimate of the fair values of acquired amortizable intangible assets was determined using a multi-period excess earnings income approach. Fair value was determined under this approach by estimating future cash flows over multiple periods, as well as a terminal value, and discounting such cash flows at a rate of return that reflects the relative risk of the cash flows. The estimate of the fair values of acquired intangible assets not subject to amortization was determined using an income approach, specifically the relief-from-royalty method. This method assumes that, in lieu of ownership, a third party would be willing to pay a royalty in order to obtain the rights to use the comparable asset.

The following table presents goodwill by product category and the related change in the carrying amount:

(In millions)	Skin Care	Makeup	Fragrance	Hair Care	Total
Balance as of June 30, 2016					
Goodwill	$ 184	$ 460	$ 255	$ 393	$ 1,292
Accumulated impairments	(29)			(35)	(64)
	155	460	255	358	1,228
Goodwill acquired during the period		720			720
Translation adjustments			(6)		(6)
		720	(6)		714
Balance as of March 31, 2017					
Goodwill	183	1,180	249	392	2,004
Accumulated impairments	(28)			(34)	(62)
	$ 155	$ 1,180	$ 249	$ 358	$ 1,942

Other intangible assets consist of the following:

	March 31, 2017			June 30, 2016		
(In millions)	Gross Carrying Value	Accumulated Amortization	Total Net Book Value	Gross Carrying Value	Accumulated Amortization	Total Net Book Value
Amortizable intangible assets:						
Customer lists and other	$ 693	$ 266	$ 427	$ 299	$ 245	$ 54
License agreements	43	43		43	43	
	$ 736	$ 309	427	$ 342	$ 288	54
Non-amortizable intangible assets:						
Trademarks and other			910			290
Total intangible assets			$ 1,337			$ 344

The aggregate amortization expense related to amortizable intangible assets was $13 million and $4 million for the three months ended March 31, 2017 and 2016, respectively, and was $22 million and $12 million for the nine months ended March 31, 2017 and 2016, respectively. The estimated aggregate amortization expense for the remainder of fiscal 2017 and for each of fiscal 2018 to 2021 is $13 million, $51 million, $51 million, $44 million and $43 million, respectively.

NOTE 5 CHARGES ASSOCIATED WITH RESTRUCTURING AND OTHER ACTIVITIES

Leading Beauty Forward

Background

In May 2016, the Company announced a multi-year initiative (Leading Beauty Forward or LBF) to build on its strengths and better leverage its cost structure to free resources for investment to continue its growth momentum. LBF is designed to enhance the Company s go-to-market capabilities, reinforce its leadership in global prestige beauty and continue creating sustainable value.

The Company plans to approve specific initiatives under LBF through fiscal 2019 related to the optimization of select corporate functions, supply chain activities, and corporate and regional market support structures, as well as the exit of underperforming businesses, and expects to complete those initiatives through fiscal 2021. Inclusive of charges recorded from inception through March 31, 2017, the Company expects that LBF will result in related restructuring and other charges totaling between $600 million and $700 million before taxes.

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Restructuring actions to be taken over the duration of LBF involve the redesigning, resizing and reorganization of select corporate functions and go-to-market structures to improve effectiveness and create cost efficiencies in support of increased investment in growth drivers. As the Company continues to grow, it is important to more efficiently support its diverse portfolio of brands, channels and geographies in the rapidly evolving prestige beauty environment. The initiatives being evaluated include the creation of a shared-services structure in existing or lower-cost locations, either using Company resources or through external service providers. The Company also believes that decision-making in key areas of innovation, marketing and digital communications should be moved closer to the consumer to increase speed and local relevance.

In connection with LBF, at this time, the Company estimates a net reduction over the duration of LBF in the range of approximately 900 to 1,200 positions globally, which is about 2.5% of its current workforce. This reduction takes into account the elimination of some positions, retraining and redeployment of certain employees and investment in new positions in key areas.

Program-to-Date Approvals

Of the $600 million to $700 million restructuring and other charges expected to be incurred, total cumulative charges approved by the Company through March 31, 2017 were:

(In millions)	Sales Returns (included in Net Sales)	Cost of Sales	Operating Expenses Restructuring Charges	Operating Expenses Other Charges	Total
Approval Period					
Fiscal 2016	$ 4	$ 28(1)	$ 87	$ 71(1)	$ 190
Nine months ended March 31, 2017	11	6	78	77	172
Cumulative through March 31, 2017	$ 15	$ 34	$ 165	$ 148	$ 362

(1) Reflects approximately $25 million of supply chain consulting and professional services expected to be recognized in Cost of Sales, which were previously classified under Operating Expenses.

Included in the above table, cumulative restructuring initiatives approved by the Company through March 31, 2017 by major cost type were:

(In millions)	Employee-Related	Asset-Related	Contract Terminations	Other Exit Costs	Total

	Costs	Costs			
Approval Period					
Fiscal 2016	$ 75	$ 3	$ 5	$ 4	$ 87
Nine months ended March 31, 2017	75	1		2	78
Cumulative through March 31, 2017	$ 150	$ 4	$ 5	$ 6	$ 165

Specific actions taken during the nine months ended March 31, 2017 included:

- Optimize Select Corporate Functions - The Company continued to approve initiatives to realign and optimize its organization to better leverage scale, improve productivity, reduce complexity and achieve cost savings across various functions, including research and development, global information systems and legal. These actions will result in a net reduction of the workforce, which includes position eliminations, the re-leveling of certain positions and an investment in new capabilities. The Company also approved consulting and other professional services related to the design of future structures, processes and technologies of certain corporate functions and, to a lesser extent, costs for training and recruitment related to new capabilities. The Company also approved other charges to support the LBF Project Management Office (PMO). The approved charges primarily consist of internal costs for employees dedicated solely to project management activities, with a focus on project integration, program communications and change management.

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The future design of certain corporate functions includes the creation of a shared-services structure, either using Company resources or through external service providers. As part of the future service delivery model in the finance organization, the Company approved the initial phase to transition select transactional activities to an external service provider, which is expected to result in other charges for implementation, project and consulting costs.

- Optimize Corporate and Region Market Support Structures - The Company continued to approve initiatives to enhance its go-to-market support structures and achieve synergies across certain geographic regions, brands and channels. These initiatives are primarily intended to shift certain areas of focus from traditional to social and digital marketing strategies to provide enhanced consumer experience, as well as to support expanded omnichannel opportunities. These actions will result in a net reduction of the workforce, which includes position eliminations, the re-leveling of certain positions and an investment in new capabilities. The Company also approved consulting and other professional services related to the design of future structures, processes and technologies and, to a lesser extent, other costs for recruitment and training related to new capabilities. In addition, the Company approved initiatives to enhance consumer engagement strategies across certain channels in Europe, which is expected to result in product returns.

- Optimize Supply Chain - The Company approved certain activities related to an initiative to generate distribution capabilities and efficiencies through an external service provider. The Company also approved certain activities related to initiatives to enhance strategic sourcing capabilities for direct procurement activities. Collectively, these actions will result in a net reduction of the workforce, which includes position eliminations, the re-leveling of certain positions and an investment in new capabilities. To enable the implementation of these initiatives, other charges were approved for LBF PMO costs, professional fees and asset write-offs. The Company also continued to approve certain activities related to initiatives to redesign transportation management activities, to enhance its Quality Assurance organization, and to improve the organizational design of manufacturing and engineering activities related to certain product lines. To enable the implementation of these initiatives, other charges were approved for consulting fees and, to a lesser extent, project management costs.

Program-to-Date Restructuring and Other Charges

The Company records approved charges associated with restructuring and other activities once the relevant accounting criteria have been met. Total cumulative charges recorded associated with restructuring and other activities for LBF were:

(In millions)	Sales Returns (included in Net Sales)	Cost of Sales	Operating Expenses Restructuring Charges	Other Charges	Total
Fiscal 2016	$ 1	$	$ 75	$ 5	$ 81
Nine months ended March 31, 2017	2	10	70	52	134
Cumulative through March 31, 2017	$ 3	$ 10	$ 145	$ 57	$ 215

Charges recorded during the nine months ended March 31, 2017 included returns (and the related cost of sales) and inventory write-offs related to the exit of certain businesses in select markets and channels of distribution. Cost of sales also included consulting and professional services incurred, primarily related to the design of supply chain planning activities. Other charges associated with LBF initiatives primarily reflected consulting and other professional services related to the design of future structures, processes and technologies of certain corporate functions and go-to-market activities and, to a lesser extent, costs to establish and maintain the LBF PMO. Other charges are included in Restructuring and other charges in the accompanying consolidated statements of earnings.

Included in the above table, aggregate restructuring charges by major cost type were:

(In millions)	Employee-Related Costs	Asset-Related Costs	Contract Terminations	Other Exit Costs	Total
Fiscal 2016	$ 74	$ 1	$	$	$ 75
Nine months ended March 31, 2017	66	2	2		70
Charges recorded through March 31, 2017	$ 140	$ 3	$ 2	$	$ 145

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Accrued restructuring charges from program inception through March 31, 2017 were:

(In millions)	Employee-Related Costs	Asset-Related Costs	Contract Terminations	Other Exit Costs	Total
Charges	$ 74	$ 1	$	$	$ 75
Noncash asset write-offs		(1)			(1)
Translation adjustments	(1)				(1)
Balance at June 30, 2016	73				73
Charges	66	2	2		70
Cash payments	(24)		(1)		(25)
Noncash asset write-offs		(2)			(2)
Translation and other adjustments	(2)				(2)
Balance at March 31, 2017	$ 113	$	$ 1	$	$ 114

Restructuring charges for employee-related costs in fiscal 2017 are net of adjustments to the accrual estimate for certain employees who either resigned or transferred to other existing positions within the Company. Accrued restructuring charges at March 31, 2017 are expected to result in cash expenditures funded from cash provided by operations of approximately $23 million, $57 million, $32 million and $2 million in fiscal 2017, 2018, 2019 and 2020, respectively.

Global Technology Infrastructure

In October 2015, the Company approved plans to transform and modernize its global technology infrastructure (GTI) to fundamentally change the way the Company delivers information technology services internally (such initiative, the GTI Restructuring). As part of the GTI Restructuring, the Company transitioned its GTI from Company-owned assets to a primarily vendor-owned, cloud-based model where the Company pays for services as they are used. The Company incurred restructuring charges of $12 million and $29 million for the three and nine months ended March 31, 2016, respectively, reflecting contract terminations, asset write-offs and employee-related costs. Other charges in connection with the implementation of this initiative were $3 million and $5 million for the three and nine months ended March 31, 2016, respectively, primarily related to consulting services. These charges are included in Restructuring and other charges in the accompanying consolidated statements of earnings. The implementation of the GTI Restructuring was substantially completed during fiscal 2016.

NOTE 6   DEBT

In February 2017, the Company completed a public offering of $500 million aggregate principal amount of its 1.80% Senior Notes due February 7, 2020 (the 2020 Senior Notes), $500 million aggregate principal amount of its 3.15% Senior Notes due March 15, 2027 (the 2027 Senior Notes) and $500 million aggregate principal amount of its 4.15% Senior Notes due March 15, 2047 (the 2047 Senior Notes). The Company used proceeds from this offering for general corporate purposes, including to repay outstanding commercial paper as it matured and to refinance its $300 million aggregate principal amount of 5.55% Senior Notes due May 15, 2017 when it becomes due.

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These recently issued notes are summarized as follows:

Notes ($ in millions)	**Issue Date**	**Price**	**Yield**	**Unamortized Debt (Discount) Premium**	**Interest rate swap adjustments**	**Debt Issuance Costs**	**Semi-annual interest payments**
2020 Senior Notes	February 2017	99.986%	1.805%	$	$ (1)	$ 2	February 7/August 7
2027 Senior Notes (1)	February 2017	99.963	3.154		N/A	3	March 15/September 15
2047 Senior Notes (2)	February 2017	99.739	4.165	(2)	N/A	5	March 15/September 15

(1) In November 2016, in anticipation of the issuance of the 2027 Senior Notes, the Company entered into a series of treasury lock agreements on a notional amount totaling $450 million at a weighted-average all-in rate of 2.37%. The treasury lock agreements were settled upon the issuance of the new debt, and the Company recognized a gain in OCI of $2 million that is being amortized to interest expense over the life of the 2027 Senior Notes. As a result of the treasury lock agreements, the debt discount and debt issuance costs, the effective interest rate on the 2027 Senior Notes will be 3.18% over the life of the debt.

(2) In November 2016, in anticipation of the issuance of the 2047 Senior Notes, the Company entered into a series of treasury lock agreements on a notional amount totaling $350 million at a weighted-average all-in rate of 3.01%. The treasury lock agreements were settled upon the issuance of the new debt, and the Company recognized a gain in OCI of $3 million that is being amortized to interest expense over the life of the 2047 Senior Notes. As a result of the treasury lock agreements, the debt discount and debt issuance costs, the effective interest rate on the 2047 Senior Notes will be 4.17% over the life of the debt.

In February 2017, the Company decreased the size of its commercial paper program, under which it may issue commercial paper in the United States, to $1.5 billion. The commercial paper program had previously been increased to $3 billion in November 2016 to finance the Company s second quarter acquisitions. As of March 31, 2017, the Company had $195 million of commercial paper outstanding that matured through April 2017, which the Company refinanced as it matured.

In February 2017, the Company terminated its undrawn $1.5 billion senior unsecured credit agreement, which was entered into November 2016 and provided a 364 day revolving credit facility for the Company s general corporate purposes.

In October 2016, the Company replaced its undrawn $1.0 billion unsecured revolving credit facility that was set to expire on July 15, 2020 (the Prior Facility) with a new $1.5 billion senior unsecured revolving credit facility that expires on October 3, 2021, unless extended for up to two additional years in accordance with the terms set forth in the agreement (the New Facility). The New Facility may be used for general corporate purposes. Up to the equivalent of $500 million of the New Facility is available for multi-currency loans. Interest rates on borrowings under the New Facility will be based on prevailing market interest rates in accordance with the agreement. The Company incurred costs of approximately $1 million to establish the New Facility, which will be amortized over the term of the facility. The New Facility has an annual fee of approximately $1 million, payable quarterly, based on the Company s current credit ratings. The New Facility contains a cross-default provision whereby a failure to pay other material financial obligations in excess of $175 million (after grace periods and absent a waiver from the lenders) would result in an event of default and the acceleration of the maturity of any outstanding debt under this facility. At March 31, 2017, no borrowings were outstanding under the New Facility.

NOTE 7 DERIVATIVE FINANCIAL INSTRUMENTS

The Company addresses certain financial exposures through a controlled program of risk management that includes the use of derivative financial instruments. The Company enters into foreign currency forward contracts and may enter into option contracts to reduce the effects of fluctuating foreign currency exchange rates. In addition, the Company enters into interest rate derivatives to manage the effects of interest rate movements on the Company s aggregate liability portfolio, including potential future debt issuances. The Company also enters into foreign currency forward contracts and may use option contracts, not designated as hedging instruments, to mitigate the change in fair value of specific assets and liabilities on the balance sheet. The Company does not utilize derivative financial instruments for trading or speculative purposes. Costs associated with entering into derivative financial instruments have not been material to the Company s consolidated financial results.

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For each derivative contract entered into where the Company looks to obtain hedge accounting treatment, the Company formally and contemporaneously documents all relationships between hedging instruments and hedged items, as well as its risk-management objective and strategy for undertaking the hedge transaction, the nature of the risk being hedged, how the hedging instruments effectiveness in offsetting the hedged risk will be assessed prospectively and retrospectively, and a description of the method of measuring ineffectiveness. This process includes linking all derivatives to specific assets and liabilities on the balance sheet or to specific firm commitments or forecasted transactions. The Company also formally assesses, both at the inception of the hedges and on an ongoing basis, whether the derivatives that are used in hedging transactions are highly effective in offsetting changes in fair values or cash flows of hedged items. If it is determined that a derivative is not highly effective, or that it has ceased to be a highly effective hedge, the Company will be required to discontinue hedge accounting with respect to that derivative prospectively.

The fair values of the Company s derivative financial instruments included in the consolidated balance sheets are presented as follows:

	Asset Derivatives			Liability Derivatives		
		Fair Value (1)			Fair Value (1)	
(In millions)	**Balance Sheet Location**	**March 31 2017**	**June 30 2016**	**Balance Sheet Location**	**March 31 2017**	**June 30 2016**
Derivatives Designated as Hedging Instruments						
Foreign currency forward contracts	Prepaid expenses and other current assets	$ 27	$ 37	Other accrued liabilities	$ 30	$ 18
Interest rate swap contracts	Prepaid expenses and other current assets		18	Other accrued liabilities	7	
Total Derivatives Designated as Hedging Instruments		27	55		37	18
Derivatives Not Designated as Hedging Instruments						
Foreign currency forward contracts	Prepaid expenses and other current assets	4	11	Other accrued liabilities	10	8
Total Derivatives		$ 31	$ 66		$ 47	$ 26

(1) See Note 8 Fair Value Measurements for further information about how the fair value of derivative assets and liabilities are determined.

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NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

The amounts of the gains and losses related to the Company s derivative financial instruments designated as hedging instruments are presented as follows:

(In millions)	Amount of Gain or (Loss) Recognized in OCI on Derivatives (Effective Portion) Three Months Ended March 31 2017	2016	Location of Gain or (Loss) Reclassified from AOCI into Earnings (Effective Portion)	Amount of Gain or (Loss) Reclassified from AOCI into Earnings (Effective Portion) (1) Three Months Ended March 31 2017	2016
Derivatives in Cash Flow Hedging Relationships					
Foreign currency forward contracts	$ (35)	$ (16)	Cost of sales	$ 2	$ 6
			Selling, general and administrative	7	14
Interest rate-related derivatives	(6)		Interest expense	1	
Total Derivatives	$ (41)	$ (16)		$ 10	$ 20

(1) The amount of gain (loss) recognized in earnings related to the amount excluded from effectiveness testing was \$2 million and \$(3) million for the three months ended March 31, 2017 and 2016, respectively. There was no gain (loss) recognized in earnings related to the ineffective portion of the hedging relationships for the three months ended March 31, 2017 and March 31, 2016.

(In millions)	Amount of Gain or (Loss) Recognized in OCI on Derivatives (Effective Portion) Nine Months Ended March 31 2017	2016	Location of Gain or (Loss) Reclassified from AOCI into Earnings (Effective Portion)	Amount of Gain or (Loss) Reclassified from AOCI into Earnings (Effective Portion) (1) Nine Months Ended March 31 2017	2016
Derivatives in Cash Flow Hedging Relationships					
Foreign currency forward contracts	$ 13	$ 20	Cost of sales	$ 8	$ 13
			Selling, general and administrative	26	38
Interest rate-related derivatives	5		Interest Expense	1	1
Total Derivatives	$ 18	$ 20		$ 35	$ 52

(1) The amount of gain (loss) recognized in earnings related to the amount excluded from effectiveness testing was de minimis and $(2) million for the nine months ended March 31, 2017 and 2016, respectively. The amount of gain recognized in earnings related to the ineffective portion of the hedging relationships was de minimis for the nine months ended March 31, 2017 and 2016.

		Amount of Gain or (Loss) Recognized in Earnings on Derivatives (1)			
	Location of Gain or (Loss) Recognized in Earnings on Derivatives	Three Months Ended March 31		Nine Months Ended March 31	
(In millions)		2017	2016	2017	2016
Derivatives in Fair Value Hedging Relationships					
Interest rate swap contracts	Interest expense	$ (3)	$ 7	$ (25)	$ 13

(1) Changes in the fair value of the interest rate swap agreements are exactly offset by the change in the fair value of the underlying long-term debt.

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The amounts of the gains and losses related to the Company s derivative financial instruments not designated as hedging instruments are presented as follows:

		Amount of Gain or (Loss) Recognized in Earnings on Derivatives			
	Location of Gain or (Loss) Recognized in Earnings on Derivatives	Three Months Ended March 31		Nine Months Ended March 31	
(In millions)		**2017**	**2016**	**2017**	**2016**
Derivatives Not Designated as Hedging Instruments					
Foreign currency forward contracts	Selling, general and administrative	$ (11)	$ 20	$ (10)	$ 21

Cash-Flow Hedges

The Company enters into foreign currency forward contracts to hedge anticipated transactions, as well as receivables and payables denominated in foreign currencies, for periods consistent with the Company s identified exposures. The purpose of the hedging activities is to minimize the effect of foreign exchange rate movements on costs and on the cash flows that the Company receives from foreign subsidiaries. The majority of foreign currency forward contracts are denominated in currencies of major industrial countries. The Company may also enter into foreign currency option contracts to hedge anticipated transactions where there is a high probability that anticipated exposures will materialize. The foreign currency forward contracts entered into to hedge anticipated transactions have been designated as cash-flow hedges and have varying maturities through the end of March 2019. Hedge effectiveness of foreign currency forward contracts is based on a hypothetical derivative methodology and excludes the portion of fair value attributable to the spot-forward difference which is recorded in current-period earnings. Hedge effectiveness of foreign currency option contracts is based on a dollar offset methodology.

The Company may enter into interest rate forward contracts to hedge anticipated issuance of debt for periods consistent with the Company s identified exposures. The purpose of the hedging activities is to minimize the effect of interest rate movements on the cost of debt issuance.

The ineffective portion of both foreign currency forward and interest rate derivatives is recorded in current-period earnings. For hedge contracts that are no longer deemed highly effective, hedge accounting is discontinued and gains and losses in AOCI are reclassified to earnings when the underlying forecasted transaction occurs. If it is probable that the forecasted transaction will no longer occur, then any gains or losses in AOCI are reclassified to current-period earnings. As of March 31, 2017, the Company s foreign currency cash-flow hedges were highly effective.

At March 31, 2017, the Company had foreign currency forward contracts in the amount of $3,175 million. The foreign currencies included in foreign currency forward contracts (notional value stated in U.S. dollars) are principally the British pound ($565 million), Swiss franc ($397 million), Hong Kong dollar ($364 million), Chinese yuan ($328 million), Euro ($305 million), Australian dollar ($196 million) and Taiwan dollar ($138 million).

The estimated net gain on the Company s derivative instruments designated as cash-flow hedges as of March 31, 2017 that is expected to be reclassified from AOCI into earnings, net of tax, within the next twelve months is $4 million. The accumulated gain on derivative instruments in AOCI was $33 million and $50 million as of March 31, 2017 and June 30, 2016, respectively.

Fair-Value Hedges

The Company enters into interest rate derivative contracts to manage the exposure to interest rate fluctuations on its funded indebtedness. The Company has interest rate swap agreements, with notional amounts totaling $250 million, $450 million and $250 million to effectively convert the fixed rate interest on its 2020 Senior Notes, 1.70% Senior Notes due May 10, 2021 and 2.35% Senior Notes due August 15, 2022, respectively, to variable interest rates based on three-month LIBOR plus a margin. These interest rate swap agreements are designated as fair-value hedges of the related long-term debt, and the changes in the fair value of the interest rate swap agreements are exactly offset by the change in the fair value of the underlying long-term debt.

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Credit Risk

As a matter of policy, the Company enters into derivative contracts only with counterparties that have a long-term credit rating of at least A- or higher by at least two nationally recognized rating agencies. The counterparties to these contracts are major financial institutions. Exposure to credit risk in the event of nonperformance by any of the counterparties is limited to the gross fair value of contracts in asset positions, which totaled $31 million at March 31, 2017. To manage this risk, the Company has strict counterparty credit guidelines that are continually monitored. Accordingly, management believes risk of loss under these hedging contracts is remote.

NOTE 8   FAIR VALUE MEASUREMENTS

The Company records certain of its financial assets and liabilities at fair value, which is defined as the price that would be received to sell an asset or paid to transfer a liability, in the principal or most advantageous market for the asset or liability, in an orderly transaction between market participants at the measurement date. The accounting for fair value measurements must be applied to nonfinancial assets and nonfinancial liabilities that require initial measurement or remeasurement at fair value, which principally consist of assets and liabilities acquired through business combinations and goodwill, indefinite-lived intangible assets and long-lived assets for the purposes of calculating potential impairment. The Company is required to maximize the use of observable inputs and minimize the use of unobservable inputs when measuring fair value. The three levels of inputs that may be used to measure fair value are as follows:

Level 1: Inputs based on quoted market prices for identical assets or liabilities in active markets at the measurement date.

Level 2: Observable inputs other than quoted prices included in Level 1, such as quoted prices for similar assets and liabilities in active markets; quoted prices for identical or similar assets and liabilities in markets that are not active; or other inputs that are observable or can be corroborated by observable market data.

Level 3: Inputs reflect management s best estimate of what market participants would use in pricing the asset or liability at the measurement date. The inputs are unobservable in the market and significant to the instrument s valuation.

The following table presents the Company s hierarchy for its financial assets and liabilities measured at fair value on a recurring basis as of March 31, 2017:

(In millions)	Level 1	Level 2	Level 3	Total
Assets:				
Foreign currency forward contracts	$	$ 31	$	$ 31
Available-for-sale securities:				
U.S. government and agency securities		452		452
Foreign government and agency securities		102		102
Corporate notes and bonds		504		504
Time deposits		520		520
Other securities		27		27
Total	$	$ 1,636	$	$ 1,636
Liabilities:				
Foreign currency forward contracts	$	$ 40	$	$ 40
Interest rate swap contracts		7		7
Contingent consideration			197	197
Total	$	$ 47	$ 197	$ 244

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The following table presents the Company s hierarchy for its financial assets and liabilities measured at fair value on a recurring basis as of June 30, 2016:

(In millions)	Level 1	Level 2	Level 3	Total
Assets:				
Foreign currency forward contracts	$	$ 48	$	$ 48
Interest rate swap contracts		18		18
Available-for-sale securities:				
U.S. government and agency securities		563		563
Foreign government and agency securities		61		61
Corporate notes and bonds		457		457
Time deposits		390		390
Other securities		33		33
Total	$	$ 1,570	$	$ 1,570
Liabilities:				
Foreign currency forward contracts	$	$ 26	$	$ 26
Contingent consideration			196	196
Total	$	$ 26	$ 196	$ 222

The estimated fair values of the Company s financial instruments are as follows:

(In millions)	March 31 2017 Carrying Amount	March 31 2017 Fair Value	June 30 2016 Carrying Amount	June 30 2016 Fair Value
Nonderivatives				
Cash and cash equivalents	$ 1,139	$ 1,139	$ 914	$ 914
Available-for-sale securities	1,605	1,605	1,504	1,504
Current and long-term debt	3,896	4,007	2,242	2,482
Additional purchase price payable	37	37	37	37
Contingent consideration	197	197	196	196
Derivatives				
Foreign currency forward contracts asset (liability), net	(9)	(9)	22	22
Interest rate swap contracts asset (liability), net	(7)	(7)	18	18

The following methods and assumptions were used to estimate the fair value of the Company s financial instruments for which it is practicable to estimate that value:

Cash and cash equivalents Cash and all highly-liquid securities with original maturities of three months or less are classified as cash and cash equivalents, primarily consisting of cash deposits in interest bearing accounts, money market funds and time deposits. The carrying amount approximates fair value primarily due to the short maturity of cash equivalent instruments.

Available-for-sale securities Available-for-sale securities are classified within Level 2 of the valuation hierarchy and are valued using third-party pricing services, and for time deposits, the carrying amount approximates fair value. To determine fair value, the pricing services use market prices or prices derived from other observable market inputs such as benchmark curves, credit spreads, broker/dealer quotes, and other industry and economic factors.

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Foreign currency forward contracts The fair values of the Company s foreign currency forward contracts were determined using an industry-standard valuation model, which is based on an income approach. The significant observable inputs to the model, such as swap yield curves and currency spot and forward rates, were obtained from an independent pricing service. To determine the fair value of contracts under the model, the difference between the contract price and the current forward rate was discounted using LIBOR for contracts with maturities up to 12 months, and swap yield curves for contracts with maturities greater than 12 months.

Interest rate swap contracts The fair values of the Company s interest rate swap contracts were determined using an industry-standard valuation model, which is based on the income approach. The significant observable inputs to the model, such as treasury yield curves, swap yield curves, and LIBOR forward rates, were obtained from independent pricing services.

Current and long-term debt The fair value of the Company s debt was estimated based on the current rates offered to the Company for debt with the same remaining maturities. To a lesser extent, debt also includes capital lease obligations for which the carrying amount approximates the fair value. The Company s debt is classified within Level 2 of the valuation hierarchy.

Additional purchase price payable The Company s additional purchase price payable represents fixed minimum additional purchase price that was discounted using the Company s incremental borrowing rate, which was approximately 1%. The additional purchase price payable is classified within Level 2 of the valuation hierarchy.

Contingent consideration Contingent consideration obligations consist of potential obligations related to the Company s acquisitions in previous years. The amounts to be paid under these obligations are contingent upon the achievement of stipulated financial targets by the business subsequent to acquisition. The fair values of the contingent consideration related to certain acquisition earn-outs were estimated using a probability-weighted discount model that considers the achievement of the conditions upon which the respective contingent obligation is dependent (Monte Carlo Method).

The Monte Carlo Method has various inputs into the valuation model, in addition to the risk-adjusted projected future operating results of the acquired entities, which include the following ranges at March 31, 2017:

Risk-adjusted discount rate	1.5% to 2.4%
Revenue volatility	3.5% to 8.3%
Asset volatility	21.7% to 26.5%
Revenue/earnings before income tax, depreciation and amortization (EBITDA) correlation factor	80%
Revenue discount rates	2.9% to 4.9%
EBITDA discount rates	11.1% to 11.9%

Significant changes in the projected future operating results would result in a significantly higher or lower fair value measurement. Changes to the discount rates, volatilities or correlation factors would have a lesser effect. The implied rates are deemed to be unobservable inputs and, as such, the Company s contingent consideration is classified within Level 3 of the valuation hierarchy.

Changes in the fair value of the contingent consideration obligations for the nine months ended March 31, 2017 are included in Selling, general and administrative expenses in the accompanying consolidated statements of earnings and were as follows:

(In millions)	**Fair Value**
Contingent consideration at June 30, 2016	$ 196
Change in fair value	1
Contingent consideration at March 31, 2017	$ 197

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NOTE 9 PENSION AND POST-RETIREMENT BENEFIT PLANS

The Company maintains pension plans covering substantially all of its full-time employees for its U.S. operations and a majority of its international operations. The Company also maintains post-retirement benefit plans which provide certain medical and dental benefits to eligible employees. Descriptions of these plans are discussed in the notes to consolidated financial statements in the Company s Annual Report on Form 10-K for the fiscal year ended June 30, 2016.

The components of net periodic benefit cost for the three months ended March 31, 2017 and 2016 consisted of the following:

	Pension Plans				Other than Pension Plans	
	U.S.		International		Post-retirement	
(In millions)	**2017**	**2016**	**2017**	**2016**	**2017**	**2016**
Service cost	$ 9	$ 8	$ 7	$ 6	$	$ 1
Interest cost	8	8	3	4	2	2
Expected return on plan assets	(13)	(12)	(4)	(5)		(1)
Amortization of:						
Prior service cost		1				
Actuarial loss	4	2	3	3		
Special termination benefits			1			
Net periodic benefit cost	$ 8	$ 7	$ 10	$ 8	$ 2	$ 2

The components of net periodic benefit cost for the nine months ended March 31, 2017 and 2016 consisted of the following:

	Pension Plans				Other than Pension Plans	
	U.S.		International		Post-retirement	
(In millions)	**2017**	**2016**	**2017**	**2016**	**2017**	**2016**
Service cost	$ 27	$ 24	$ 21	$ 18	$ 2	$ 3
Interest cost	23	24	9	12	5	6
Expected return on plan assets	(39)	(36)	(12)	(15)	(1)	(2)
Amortization of:						
Prior service cost	1	1	1	1		
Actuarial loss	12	8	8	9	1	
Special termination benefits			1			
Net periodic benefit cost	$ 24	$ 21	$ 28	$ 25	$ 7	$ 7

During the nine months ended March 31, 2017, the Company made contributions to its international pension plans totaling approximately $9 million.

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The amounts recognized in the consolidated balance sheets related to the Company s pension and post-retirement benefit plans consist of the following:

(In millions)	March 31 2017	June 30 2016
Other assets	$ 75	$ 79
Other accrued liabilities	(27)	(27)
Other noncurrent liabilities	(443)	(429)
Funded status	(395)	(377)
Accumulated other comprehensive loss	400	427
Net amount recognized	$ 5	$ 50

NOTE 10 CONTINGENCIES

Legal Proceedings

The Company is involved, from time to time, in litigation and other legal proceedings incidental to its business. Management believes that the outcome of current litigation and legal proceedings will not have a material adverse effect upon the Company s results of operations, financial condition or cash flows. However, management s assessment of the Company s current litigation and other legal proceedings could change in light of the discovery of facts with respect to legal actions or other proceedings pending against the Company not presently known to the Company or determinations by judges, juries or other finders of fact which are not in accord with management s evaluation of the possible liability or outcome of such litigation or proceedings. Reasonably possible losses in addition to the amounts accrued for litigation and other legal proceedings are not material to the Company s consolidated financial statements.

NOTE 11 STOCK PROGRAMS

Total net stock-based compensation expense is attributable to the granting of, and the remaining requisite service periods of, stock options, restricted stock units (RSUs), performance share units (PSUs), PSUs based on total stockholder return (TSR), long-term PSUs, and share units. Compensation expense attributable to net stock-based compensation is as follows:

	Three Months Ended March 31	Nine Months Ended March 31

(In millions)	2017	2016	2017	2016
Compensation expense	$ 41	$ 36	$ 175	$ 147
Income tax benefit	14	12	58	48

Stock Options

During the nine months ended March 31, 2017, the Company granted approximately 2.5 million stock options with a weighted-average exercise price per share of $89.24 and a weighted-average grant date fair value per share of $22.79. The fair value of each option grant was estimated on the date of grant using the Black-Scholes option-pricing model. The aggregate intrinsic value of stock options exercised during the three and nine months ended March 31, 2017 was $45 million and $116 million, respectively.

Restricted Stock Units

The Company granted approximately 1.6 million RSUs during the nine months ended March 31, 2017 with a weighted-average grant date fair value per share of $88.54 which, at the time of grant, were scheduled to vest as follows: 0.5 million in fiscal 2018, 0.5 million in fiscal 2019, 0.5 million in fiscal 2020 and 0.1 million in fiscal 2022. Vesting of RSUs granted is generally subject to the continued employment of the grantees. RSUs are accompanied by dividend equivalent rights, payable upon settlement either in cash or shares (based on the terms of the particular award) and, as such, were valued at the closing market price of the Company s Class A Common Stock on the date of grant.

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Performance Share Units

In September 2016, the Company granted PSUs with a target payout of approximately 0.3 million shares with a weighted-average grant date fair value per share of $89.47, which will be settled in stock subject to the achievement of the Company s net sales, diluted net earnings per common share and return on invested capital goals for the three fiscal years ending June 30, 2019. In January 2017, the Company granted PSUs with a target payout of approximately 0.3 million shares with a weighted-average grant date fair value per share of $80.79, which will be settled in stock subject to the achievement of certain net sales and net operating profit goals of a subsidiary of the Company for the fiscal year ending June 30, 2020. In January 2017, the Company granted PSUs with a target payout of approximately 0.2 million shares with a weighted-average grant date fair value per share of $80.79, which will be settled in stock subject to the achievement of certain net sales and net operating profit goals of a subsidiary of the Company for the fiscal year ending June 30, 2022. For PSU grants, no settlement will occur for results below the applicable minimum threshold. Vesting of PSUs is generally subject to continued employment of the grantees. PSUs are accompanied by dividend equivalent rights that will be payable in cash upon settlement.

In September 2016, approximately 0.3 million shares of the Company s Class A Common Stock were issued and related accrued dividends were paid, relative to the target goals set at the time of the issuance, in settlement of 0.3 million PSUs which vested as of June 30, 2016.

Performance Share Units Based on Total Stockholder Return

In September 2016, 49,882 shares of the Company s Class A Common Stock were issued, and related dividends paid, in accordance with the terms of the grant, related to the performance period ended June 30, 2016.

NOTE 12 NET EARNINGS ATTRIBUTABLE TO THE ESTÉE LAUDER COMPANIES INC. PER COMMON SHARE

Net earnings attributable to The Estée Lauder Companies Inc. per common share (basic EPS) is computed by dividing net earnings attributable to The Estée Lauder Companies Inc. by the weighted-average number of common shares outstanding and contingently issuable shares (which satisfy certain conditions). Net earnings attributable to The Estée Lauder Companies Inc. per common share assuming dilution (diluted EPS) is computed by reflecting potential dilution from stock-based awards.

A reconciliation between the numerator and denominator of the basic and diluted EPS computations is as follows:

	Three Months Ended March 31		Nine Months Ended March 31	
(In millions, except per share data)	**2017**	**2016**	**2017**	**2016**
Numerator:				